Annual Institute on Mineral Law

Volume 55 *The 55th Annual Institute on Mineral Law* Article 6

3-27-2008

OCS Title and Current MMS Regulatory Matters

Anthony C. Marino

Paul J. Goodwine

Steven K. Waddell

2. OCS Title and Current MMS Regulatory Matters

Anthony C. Marino
Paul J. Goodwine
Schully, Roberts, Slattery & Marino
New Orleans,Louisiana

Steven K. Waddell, CPL
United States Department of the Interior
Minerals Management Service
New Orleans,Louisiana

In this paper, we attempt to set-forth our current thoughts on certain unique aspects of title to oil and gas leases on the Outer Continental Shelf ("OCS")[1] and attempt to encapsulate and comment upon certain of the current federal regulations applicable to leasing for the exploration and production of oil and gas in the Gulf of Mexico ("GOM").

I. OCS Title.

A. OCSLA, Applicable Law, and General Principles.

The Outer Continental Shelf Lands Act, as amended, 43 U.S.C. §1331, et seq. ("OCSLA"), provides:

> To the extent that they are applicable and not inconsistent with this subchapter or with other Federal laws and regulations of the Secretary [of the Interior] now in effect or hereafter adopted, the civil and criminal laws of each adjacent State, now in effect or hereafter adopted, amended or repealed are declared to be the law of the United States for that portion of the subsoil and seabed of the outer Continental Shelf, and artificial islands and fixed structures erected thereon, which would be within the area of the State if its boundaries were extended seaward to the outer margin of the outer Continental Shelf.

43 U.S.C. §1333(a)(2)(A). These provisions suggest that the laws of the State of Louisiana, including its laws of registry,[2] apply to title issues dealing with OCS leasing activities in the GOM, so long as such laws are not inconsistent with the laws and regulations of the United States and the Department of the Interior.

---

[1] "Outer Continental Shelf" is defined in the Outer Continental Shelf Lands Act, 43 U.S.C. §1331, *et seq.*, as "all submerged lands lying seaward and outside of the area of lands beneath navigable waters as defined in section 1301 of this title, and of which the subsoil and seabed appertain to the United States and are subject to its jurisdiction and control."

[2] *See*, generally, La. R.S. 9:2721 through 2729 and La. Civ. Code art. 3338, et seq. In addition, please note that Mineral Code article 18 (La. R.S. 31:18) states that "[a]ll sales, contracts, and judgments affecting mineral rights are subject to the laws of registry."

Presently, however, there is no reported decision by any state or federal court which specifically holds that the Louisiana recording statutes, laws, and jurisprudence apply unquestionably to federal leases covering OCS lands. However, *Union Texas Petroleum Corp. v. PLT Engineering, Inc.*, 895 F.2d 1043 (5th Cir. 1990), cert denied, 498 U.S. 848 (1990), a case decided by the United States Court of Appeals for the Fifth Circuit, held that the recordation requirements for perfection of lien rights under the Louisiana Oil Well Lien Act, La. R.S. 9:4861, et seq. ("LOWLA"), apply to lands and leases situation on the OCS offshore Louisiana. The Fifth Circuit held that a lien claimant complied with LOWLA by filing its lien in the adjacent coastal parish. The Fifth Circuit reasoned that OCSLA (i) adopted the provision of Louisiana law that ". . [t]he gulfward boundaries of all said coastal parishes extend coextensively with the gulfward boundary of the State of Louisiana" (La. R.S. 49:6), and (ii) extended the "boundaries of [such] parish(es) to the outer limits of the OCS by providing that state law applies to the subsoil and seabed of the OCS and all artificial islands thereon 'which would be within the area of the state if the boundaries were extended seaward to the outer margin of the Outer Continental Shelf . . .'." *Union Texas*, 895 F.2d at 1051-52. Consequently, Louisiana lien law is applicable to OCS lands adjacent to Louisiana.

B. State Adjacency Issues.

As noted above, 43 U.S.C. §1333(a)(2)(A) declares the law of the adjacent state to be applicable to OCS lands. Although not unequivocal, we believe that this provision of OCSLA and the *Union Texas* decision strongly suggest that the Louisiana recording statutes govern public records filings relating to oil and gas leases on the OCS adjacent to Louisiana. Although OCSLA calls for the President of the United States to draw extended state boundary lines to create clarity, no President has ever undertaken this task. This begs the question: how is the adjacent state determined?

Reeves v. B & S Welding, Inc., 897 F.2d 178, 179-80 (5th Cir. 1990), has suggested that certain factors (or evidence) should be reviewed to determine state adjacency issues. These four categories of evidence include: (i) geographic proximity; (ii) considerations of other federal agencies as to which state was adjacent to a particular offshore block; (iii) prior court determinations (if applicable); and (iv) projected boundaries. However, *Snyder Oil Corp. v. Samedan Oil Corp.*, 208 F.3d. 521, 525 (5th Cir. 2000), refused to follow this strict formalistic test; *Snyder* held that all relevant evidence should be considered to determine which state is the adjacent state for jurisdictional purposes.

These Fifth Circuit decisions demonstrate that geographic proximity of an offshore block to a particular state is not necessarily conclusive evidence of the adjacent state for state law application. All relevant

factors, whatever they may be, should be considered and examined. These are important determinations because an OCS title examiner must know which state is the adjacent state and which parishes (or counties) need to be researched in conjunction with the preparation and rendition of a title opinion covering OCS properties.

Because there is not absolute clarity on these issues,[3] we always include limitation language in our OCS title opinions which indicates to the recipient that certain subject leases may arguably be considered adjacent to a state other than Louisiana and that we, as Louisiana attorneys, are only rendering opinions pursuant to Louisiana law. In addition, multiple opinions from multiple attorneys licensed to practice law in multiple states are often required. For example, OCS leases in the Vioska Knoll, Main Pass, Mississippi Canyon, and Atwater Valley areas of the OCS may be adjacent to Louisiana, Mississippi, and/or Alabama; leases in the Garden Banks and Keathley Canyon areas of the OCS may be adjacent to Louisiana and/or Texas.

C. Louisiana Parish Boundary Extensions.

Even if a particular OCS lease is unequivocally adjacent to Louisiana, identifying the appropriate parish or parishes to conduct public records searches may not always be clear.[4] Louisiana law itself helps in determining which parishes should be searched in conjunction with the preparation and rendition of an OCS title opinion.

"The historic gulfward boundary of the State of Louisiana extends a distance into the Gulf of Mexico 3 marine leagues from the coast." La. R.S. 49:1. Louisiana law also indicates that coastal parish boundary lines are extended into the GOM in precise directions depending on their location:

> a. The gulfward boundaries of the coastal parishes of the state of Louisiana situated east of the Mississippi River extend from the outer land terminus of their common boundary due east, true bearing, to the outer gulfward boundary of the state of Louisiana, and the gulfward boundaries of the coastal boundaries situated west of the Mississippi River extend from the outer land terminus of their common boundaries due south true bearing, to the outer gulfward boundary of the state of Louisiana, and the gulfward boundary of all

---

[3] In fact, *Snyder* refused to conclusively set any state boundaries: "Therefore, while *Reeves* instructs that proposed boundary projections are relevant to a private dispute, it would be improper for a court to hold that a given boundary projection was conclusively established for purposes of §1333(a)(2)(A)." *Snyder*, 208 F.3d at 523.

[4] Getting comfortable with identifying the appropriate parish or parishes to conduct public records searches is important because recordation of an instrument is effective "only with respect to immovables located *within the parish where the instrument is recorded.*" La. Civ. Code art. 3341 (emphasis supplied).

said coastal parishes extend coextensively with the gulfward boundary of the state of Louisiana.

b. The interior or inland boundaries of all coastal parishes shall remain as now existing or fixed by applicable state laws.

La. R.S. 49:6. These Louisiana statutes suggest the means to project parish boundaries into the GOM, which is one of the factors outlined in *Reeves*, 897 F.2d 178.

Furthermore, the *Union Texas* case, cited above, explicitly mandates that such parish boundaries be projected further onto the OCS consistent with La. R.S. 49:6, which provides:

> OCSLA adopts this state law [La. R.S. 49:6] and extends the boundaries of [Vermilion] parish to the outer limits of the OCS by providing that state law applies to the subsoil and seabed of the OCS and all artificial islands thereon 'which would be within the area of the State if its boundaries were extended seaward to the outer margin of the Outer Continental Shelf . . ..' 43 U.S.C. §1333(a)(2)(A). Thus the liens were actually filed *in the parish where the property is located.*

Union Texas, 895 F.2d at 1052 (emphasis supplied).

A simple logical extension to this holding is that the Louisiana laws of registry also apply to OCS properties and that parish boundary lines are extended to the outer margin of the OCS. This allows for La. Civ. Code art. 3341 to have effect because the immovable properties located on the OCS will be located within specific parish(es).

As a practical matter, when we analyze particular lease blocks to determine what states/parishes/counties may need to be searched, we take a conservative view and, if necessary, select multiple states, multiple parishes, and/or multiple counties to ensure that any possible reading of the jurisprudence on these boundary extension issues are covered. Although this often mandates the need to hire additional attorneys from Texas, Alabama, and/or Mississippi, and may require an analysis of multiple parishes for a single lease block, such additional work allows for a greater analysis of potential OCS/GOM title issues.

D. Federal Regulations Affecting OCS Title.

OCSLA charges the Secretary of Interior with authority and responsibility to manage leasing activities on federal public lands, specifically including such lands on the OCS and in the GOM. 43 U.S.C. §1334(a). The Minerals Management Service, a division of the United States Department of the Interior ("MMS"), performs these functions on behalf of the Secretary of the Interior. 30 CFR part 256, entitled Leasing of Sulphur or Oil and Gas in the Outer Continental Shelf, contains the primary regulations affecting OCS title issues.

> The purpose of the regulations in this part is to establish the procedure under which the Secretary of the Interior (Secretary) will exercise the authority to administer a leasing program for oil, gas and sulphur.

30 CFR §256.1 (Purpose).

> The management of Outer Continental Shelf resources is to be conducted in accordance with the findings, purposes and policy directions provided by the Outer Continental Shelf Lands Act Amendment of 1978 (43 U.S.C. §§1332, 1801, 1802), and other Executive, legislative, judicial and Departmental guidance. The Secretary of the Interior shall consider available environmental information in making decisions affecting Outer Continental Shelf resources.

30 CFR §256.2 (Policy).

> The Outer Continental Shelf Lands Act (OCSLA) (43 U.S.C. §1331 *et seq.*) authorizes the Secretary of the Interior to issue, on a competitive basis, leases for oil and gas, and sulphur in submerged lands of the outer continental shelf (OCS). The act authorizes the Secretary to grant rights-of-way, rights-of-use and easements through the submerged lands of the OCS. The Energy Policy and Conservation Act of 1975 (42 U.S.C. §6213), prohibits joint bidding by major oil and gas producers.

30 CFR §256.4 (Authority). By these regulations, it is clear that the Secretary of the Interior has authority to regulate leasing on the OCS, and does so through the MMS. The regulations promulgated by the Secretary of the Interior affecting such leasing activities affect title to OCS properties, and an OCS title examiner must be familiar with their application.[5]

For purposes of this part of the paper, it is the leasing records (lease files) maintained by the MMS to regulate OCS leasing activities which are of primary importance. Although these records were once maintained in hard copy at the MMS offices, located in New Orleans, Louisiana, such records are now available on the MMS website (*www.gomr.mms.gov*). Because the MMS, pursuant to federal regulations, has full authority to approve or deny transfers of leases, we have always utilized the MMS lease files as an integral part of our OCS title analysis and our starting point to establish an appropriate chain-of-title prior to commencing searches within the applicable parish records.

To start the OCS title review process, we generally review MMS documents from or relating to: (i) the Adjudication Unit (lease files); (ii)

---

[5] Additional discussion on applicable MMS regulations can be found in sections II and III of this paper, below.

public information; (iii) production information; (iv) well information; (v) OSFR information; (vi) unitization information; (vii) non-required filings; and (viii) pending instruments. All of these documents filed and maintained by the MMS affect, directly or indirectly, title to OCS leases and help provide an appropriate chain-of-title and background to aid when abstractors commence searches in the applicable parish records.

There are certain concepts and/or definitions which are important to note in conjunction with reviewing OCS title:

> *Lessee*: According to the Federal Oil and Gas Royalty Simplification and Fairness Act of 1996 (Pub. L. 104-185, as corrected by Pub. L. 104-200) ("FOGRSFA"), which amended certain portions of the Federal Oil and Gas Management Act of 1982, 30 U.S.C. §1702, *et seq.*, "lessee" is defined as any person to whom the United States issues an oil and gas lease or any person to whom operating rights in a lease have been assigned.
>
> *Record Title*: "A lessee's interest in a lease which includes the obligation to pay rent, and the rights to assign and relinquish the lease. Overriding royalty and operating rights are severable from record title interests (43 CFR §3100.0-5(c)).
>
> *Operating Rights Owner*: MMS regulations implementing OCSLA define the term "operating rights" as meaning "any interest held in a lease with the right to explore for, develop and produce leased substances (30 CFR §250.105); the owner of an operating rights interest, being an interest derived from a "record title" holder, may be subject to having its interest extinguished if the record title holder should fail to meet lease obligations or chose to relinquish the lease (43 CFR §3100.0-5(c)).

Because leases may have lessees who meet one or both of the definitions of record title owner and/or operating rights owner, our OCS title opinions include separate statements regarding ownership interest (working interest and net revenue interest) for both record title and operating rights.

Furthermore, pipeline concepts on the OCS create unique title issues. Again, definitions are helpful:

> *Lease Term Pipelines*: Those pipelines owned and operated by a lessee or operator and are completely contained within the boundaries of a single lease, unit, or contiguous (not cornering) leases of that lessee or operator. 30 CFR §250.105.
>
> *Right-of-Way Pipelines*: Those pipelines that are contained within: (1) the boundaries of a single lease or unit, but are not owned and operated by a lessee or operator of that lease or unit; (2) the boundaries of contiguous (not cornering) leases that do not have a common lessee or operator; (3) the boundaries of contiguous (not

cornering) leases that have a common lessee or operator but are not owned and operated by that common lessee or operator; or (d) an unleased block(s). 30 CFR §250.105.

Although both lease term lines and right-of-way pipelines are granted segment numbers by the MMS, right-of-way pipelines are granted their own OCS-G identification numbers and require separate adjudication for their transfer. On occasion, opinions may be requested solely on rights-of-way, which is wholly appropriate given the fact that they are considered separate grants of title by the MMS.

Furthermore, please note that it is the current position of the MMS that, absent a statement to the contrary, a transfer of a record title interest in a lease carries with it a transfer of ownership of any and all lease term lines owned by the transferor of such interest and for which ownership, as recognized by the MMS, is not held separately or differently from the record title interest in the lease. In order to transfer an interest in a right-of-way pipeline, however, a separate assignment must be executed and filed for approval with the MMS in accordance with applicable regulations.

E. Unique OCS Chain-of-Title Issues and Title Curative.

Unique chain-of-title issues often arise when reviewing title to OCS leases. As noted above, we generally commence our OCS title opinion preparation activities by reviewing MMS records. Often times, the complete chain-of-title identified in the MMS lease files is not reproduced in the appropriate public records of the applicable coastal parish(es). Therefore, OCS title examiners must often record certified copies of chain-of-title documents, obtained from the MMS, in the appropriate parish records (preferably in the appropriate sequential order) to ensure that the full chain-of-title is noted. Attached as *Exhibit No. 1* in the Appendix [omitted – ed.] is a cover page we generally utilize to place on top of certain documents that may need to be re-recorded to complete a full and sequential chain-of-title in an effort to aid future title examiners in their review and to ensure that the public records do not unwittingly demonstrate duplicative assignments of interests in OCS leases.

In addition, as further discussed below, assignments of OCS leases filed with the MMS must be submitted on applicable MMS forms. Frequently, industry does not always utilize these forms for assignments filed in the parish (or county) records. Therefore, careful comparisons between assignments found in the chain-of-title at the MMS and in the relevant parish(es) should be undertaken to confirm that different instruments in fact make the same conveyances. Furthermore, when making such title comparisons, care should be taken to ensure that duplicative assignments are not mistakenly credited when the assignments convey, in fact, one and the same interest.

F. MMS Non-Required Filings.

Mortgages, encumbrances, liens, other security/financing documentation, net profits interests, carried working interests, and overriding royalty interests are often filed with the MMS, although such documents do not require approval of the Regional Supervisor and do not appear in the lease files. Because such documents are often filed in the non-required lease files, a review of such records may give the title examiner a preview of what the parish records may contain from a mortgage, lien, claim, or encumbrance standpoint.

In 1997, the MMS regulations were revised and 30 CFR §256.64(a)(7) was added (62 FR 27948), which states:

> You may create or transfer carried working interests, overriding royalty interests, or payments out of production without obtaining the Regional Director's approval. However, you must file instruments creating or transferring carried working interests, overriding royalty interests, or payments out of production with the Regional Director for record purposes.

Because this particular subpart of 30 CFR §256.64 was not added until 1997, MMS records are *not* a reliable source for a true indication of what interests (e.g. overriding royalty interests) need to be segregated from the working interest to calculate an accurate net revenue interest, especially for leases issued prior to 1997. Parish records must *always* be searched to accurately calculate new revenue interests.

G. Contents of OCS Opinions.

Once a full review of both MMS records and applicable parish records is conducted, a title opinion can be drafted and rendered. Generally, we cover the following topics within our OCS opinions:

(i) Opinion as to working interests (record title and/or operating rights);

(ii) Opinion as to net revenue interests (and calculations affecting same);

(iii) Chain-of-title;

(iv) Mortgages, liens, and encumbrances affecting the interest covered;

(v) Title defects (which are often disclosed prior to the opinion being finalized so that appropriate curative action may be accomplished);

(vi) Commentary (if applicable) regarding important documents referenced in the chain-of-title (e.g. "subject to" contracts) and other applicable public records;[6]

---

[6] Generally, from a pure Louisiana title perspective, when a document filed of public

(vii) Commentary (if applicable) pertaining to documents associated with the underlying transaction (for example, an underlying purchase agreement);

(viii) Limitations applicable to the use and benefit of the opinion;

(ix) Identification of the materials examined; and

(x) Other traditional comments, requirements, and limitations.

H. "Subject to" Contracts.

According to Louisiana's law of registry, La. R.S. 9:2721 through 2729 and La. Civ. Code art. 3338, et seq., Louisiana is a race recording state. As such, third parties are generally only bound by what appears of public record.[7] However, in *In re Century Offshore Management Corporation*, 119 F.3d 409 (6th Cir. 1997) (applying Louisiana law), the court determined that a mortgage made, by its own terms, "subject to" an operating agreement was inferior in rank to the consensual liens granted by the operator to non-operators thereunder, even though the operating agreement was not itself filed of record.

In *Century Offshore*, a typical lender brought a bankruptcy adversary proceeding against several mechanics and materialman lienholders, seeking a determination of the priority of the parties' claims against the debtor's interest in West Cameron Block 368, offshore Louisiana. The non-operating working interest owners intervened and requested that the court recognize the superiority of their security interests granted pursuant to the operating agreement. The Sixth Circuit concluded that, under Louisiana law, the non-operating working interest owners, which held unperfected reciprocal liens on debtor's West Cameron Block 368 lease interest through the operating agreement, had

---

record references an unrecorded document, there is no duty of inquiry placed upon third parties to "look beyond" the public record. *Judice-Henry-May Agency, Inc. v. Franklin, et al.*, 376 So.2d 991 (La. App. 1 Cir.), writ denied 381 So.2d 508 (La. 1979); *Julius Gindi and Sons, Inc. v. E.J.W. Enterprises, Inc.*, 438 So. 2d 594, 579 (La. App. 4th Cir. 1983) ("The duty to inquire should be limited only to recorded instruments because unrecorded instruments have no effect upon third parties. Generally, a duty to inquire *outside* of the record would be fruitless for even if something does exist it would not be binding upon third parties."); *Cardinal Federal Savings Bank v. Corporate Tower Partners, Ltd.*, 564 So.2d 1282 (La. App. 3 Cir. 1990). However, if the referenced document is itself of public record, a duty of further inquiry may apply. See, e.g., *Julius Gindi and Sons, Inc. v. E.J.W. Enterprises, Inc.*, 348 So.2d 594 (La. App. 4th Cir. 1983) ("The duty to inquire should be limited only to recorded instruments because unrecorded instruments have no effect on third parties."); but see *Port Arthur Towing Co. v. Owens-Illinois, Inc.*, 352 F. Supp. 392 (W.D. La. 1972) ("A particularly significant corollary to the Louisiana law of recordation is that when there appears on the face of the record such language that should give notice to a potential purchaser that his title is not free from all prior burdens, he must make further inquiry outside the record.").

[7] See footnote 6, above.

priority over the lender, which held a perfected security interest in the debtor's West Cameron Block 368 lease, because the mortgage expressly acknowledged that it was "subject to" the operating agreement.

> Our holding rests on the principal that even if the default rule under Louisiana's race recording statutes would ordinarily allow a third party with notice – perhaps, even actual notice – to rely solely on the public records in ranking its lien, this default rule may be avoided by the parties by contract: The public records doctrine does not prevent the third party from *contractually agreeing by express language to subordinate its interest* to interests that would otherwise be inferior.

Century Offshore, 119 F.3d at 413 (emphasis supplied). The key to this holding appears to be the express language of the bank to subordinate its interest behind those contained in and granted by an unrecorded document.

Consequently, when reviewing title to OCS properties (and all properties affected by Louisiana law), please note that such documents should be reviewed in their entirety to see what "subject to" qualifications may exist in light of the holding of *Century Offshore*. At a bare minimum, all "subject to" contracts should be noted for the recipient of the title opinion because such contracts may bear upon instruments affecting title.

I. OCS Title Conclusions.

In order to effectively prepare OCS title opinions, both MMS records and applicable parish records need to be analyzed. An OCS title examiner should have an understanding of OCSLA, applicable MMS regulations, Louisiana law, and the interplay among these authorities so that a comprehensive and effective title opinion can be prepared and rendered.

II. MMS Regulations Dealing with Leasing.

A. Background.

A Congressional declaration of policy is contained in OCSLA at 43 U.S.C. §1332:

> It is hereby declared to be the policy of the United States that -
>
> (1) the subsoil and seabed of the outer Continental Shelf appertain to the United States and are subject to its jurisdiction, control, and power of disposition as provided in this subsection;
>
> (2) this subchapter should be construed in such a manner that the character of the waters above the outer Continental Shelf as high seas and the right to navigation and fishing therein shall not be affected;

(3) the outer Continental Shelf is a vital national resource reserve held by the Federal Government for the public, which should be made available for expeditious and orderly development, subject to environmental safeguards, in a manner which is consistent with the maintenance of competition and other national needs;

(4) since exploration, development, and production of the minerals of the outer Continental Shelf will have significant impacts on coastal and non-coastal areas of the coastal States, and on other affected States, and, in recognition of the national interest in the effective management of the marine, coastal, and human environments -

(a) such States and their affected local governments may require assistance in protecting their coastal zones and other affected areas from any temporary or permanent adverse effects of such impacts;

(b) the distribution of a portion of the receipts from the leasing of mineral resources of the outer Continental Shelf adjacent to such State lands, as provided under section 1337(g) of this title, will provide affected coastal States and localities with funds which may be used for the mitigation of adverse economic and environmental effects related to development of such resources; and

(c) such States, and through such States, affected local governments, are entitled to an opportunity to participate, to the extent consistent with the national interest, in the policy and planning decisions made by the Federal Government relating to exploration for, and development and production of, minerals of the outer Continental Shelf;

(5) the rights and responsibilities of all States and, where appropriate, local governments, to preserve and protect their marine, human, and coastal environments through such means as regulation of land, air, and water uses, of safety, and of related development and activity should be considered and recognized; and

(6) operations in the outer Continental Shelf should be conducted in a safe manner by well-trained personnel using technology, precautions, and techniques sufficient to prevent or minimize the likelihood of blowouts, loss of well control, fires, spillages, physical obstruction to other users of the waters or subsoil and seabed, or other occurrences which may cause damage to the environment or property, or endanger life or health.

Although this is an extremely broad declaration of policy, we will concentrate on regulations promulgated pursuant to this policy declaration and which are applicable to the administration of leasing on the OCS.

The Secretary of the Interior has the authority to administer leasing on the OCS. "The Secretary [of the Interior] shall administer the provisions of this subchapter relating to the leasing of the outer Continental Shelf, and shall prescribe such rules and regulations as may be necessary to carry out such provisions." 43 U.S.C. §1334(a); see also 30 CFR §256.4.

Title 30 of the Code of Federal Regulations is entitled Mineral Resources. 30 CFR Chapter 2 Subpart B – Offshore (30 CFR Parts 250–282) contains the primary federal regulations applicable to OCS activities. A summary of the various topics covered is as follows:

Part 250 – Oil and Gas Sulphur Operations in the Outer Continental Shelf

Part 251 – Geological and Geophysical (G&G Explorations of the Outer Continental Shelf)

Part 252 – Outer Continental Shelf (OCS) Oil and Gas Information Program

Part 253 – Oil Spill Financial Responsibility for Offshore Facilities

Part 254 – Oil Spill Response Requirements for Facilities Located Seaward of the Coastline

Part 256 – Leasing of Sulphur or Oil and Gas in the Outer Continental Shelf

Part 259 – Mineral Leasing: Definitions

Part 260 – Outer Continental Shelf Oil and Gas Leasing

Part 270 – Non-Discrimination in the Outer Continental Shelf

Part 280 – Prospecting for Minerals Other than Oil, Gas, and Sulphur on the Outer Continental Shelf

Part 281 – Leasing of Mineral Other than Oil, Gas, and Sulphur in the Outer Continental Shelf

Part 282 – Operations in the Outer Continental Shelf for Minerals Other than Oil, Gas, and Sulphur

For the balance of this paper, 30 CFR part 256 is of primary importance.

B. Important OCS Leasing Regulations.

1. Qualification.

In order to hold a lease on the OCS granted by the MMS, a lessee must be qualified. Mineral leases issued pursuant to OCSLA may only be held by: (i) citizens and nationals of the United States; (ii) aliens lawfully admitted for permanent residence in the United States as defined in 8 U.S.C. §1101(a)(20); (iii) private, public, or municipal corporations organized under the laws of the United States or of any State or of the District of Columbia or territory thereof; or (iv) associations of such

citizens, nationals, resident aliens, or private, public, or municipal corporations, States, or political subdivisions of states. 30 CFR §256.35. Although persons or certain juridical entities will meet or not meet these definitions based upon purely objective factors, such persons or juridical entities must file appropriate qualification paperwork with the MMS to receive a qualification number.[8] Once this number is issued, the person or juridical entity may begin to conduct business with the federal government and to commence leasing activities on the OCS.

2. Assignments and Transfers.

Assignments and transfers of OCS leases are governed by Subpart J of Part 256, entitled Assignments, Transfers, and Extensions. 30 CFR §256.62 mandates that the MMS may approve of an assignment in a lease only if:

(i) the assignee qualifies to hold a lease under 30 CFR §256.35(b);

(ii) bond coverage pursuant to Subpart I is provided; and

(iii) the Regional Director of the MMS approves of the assignment.

Once the Regional Director approves the assignment, it shall be deemed to be effective on the first day of the lease month following its filing in the appropriate office of the MMS, unless, at the request of the parties, an earlier date is specified in the approval. Of primary importance, however, is that the assignor remains liable for all obligations that accrue under the lease before the date that the Regional Director approves the request for the assignment of the record title and the lease. The Regional Director's approval of the assignment does not relieve the assignor of accrued lease obligations that your assignee, or any subsequent assignee, fails to perform. 30 CFR §256.62(d). Furthermore, if an assignee, or a subsequent assignee, fails to perform any obligation under the lease or the regulations, the Regional Director may require prior assignors to bring the lease into compliance to the extent that the obligation accrued before the Regional Director approved the assignment. 30 CFR §256.62(f).

From a more practical standpoint, 30 CFR §256.64 explains how to file transfer documentation with the MMS, and pertinent parts of this section are reproduced below with emphasis supplied to aid in reading:

> This section explains how to file instruments with MMS that create and/or transfer interests in OCS oil and gas or sulphur leases.

---

[8] Guidance regarding the practicalities associated with conducting business with the MMS, specifically including how to file qualification documents, is included within a publication entitled Outer Continental Shelf Oil and Gas Leasing Procedures Guidelines (OCS Report 2001-076) ("MMS Leasing Guidelines Handbook"), which may be downloaded from the MMS website (*www.gomr.mms.gov*), and which is further discussed below.

(a) You must submit to the Regional Director for approval *all* instruments that create or transfer ownership of a lease interest.

(1) You must submit *two copies* of the instrument that create or transfer an interest. Each instrument that creates or transfers an interest *must describe by officially designated subdivision the interest you propose to create or transfer.*

(2) You must *submit* your proposal to create or transfer an interest, or create or transfer separate operating rights, subleases, and record title interests *within 90 days of the last date that a party executes the transferee agreement.*

(3) The transferee must meet the *citizenship and other qualification criteria* specified in §256.35 of this part. When you submit an instrument to create or transfer an interest as an association, you must include a statement signed by the transferee about the transferee's citizenship and qualifications to own a lease.

(4) Your instrument to create or transfer an interest must contain all of the terms and conditions to which you and the other parties agree.

(5) You do *not* gain a release of any nonmonetary obligation under your lease or the regulations in this chapter by creating a sublease or transferring operating rights.

(6) You do *not* gain a release from any accrued obligation under your lease or the regulations in this chapter by assigning your record title interest in the lease.

(7) You may create or transfer carried working interests, overriding royalty interests, or payment out of production without obtaining the Regional Director's approval. However, *you must file instruments creating or transferring carried working interests, overriding royalty interests, or payments out of production with the Regional Director for record purposes.*

(8) You must *pay the service fee* listed in §256.63 of this subpart with your application for approval of any instrument of transfer you are required to file (Record Title/Operating Rights (Transfer) Fee). Where multiple transfers of interest are included in a single instrument, a separate fee applies to each individual transfer of interest. For any document you are not required to file by these regulations but which you submit for record purposes per lease affected, you must also pay the service fee listed in §256.63 (Non-required Document Filing Fee). Such documents may be rejected at the discretion of the authorized officer.

* * *

(c) When you request approval for an assignment that assigns all your record title interest in a lease or that creates a segregated lease,

your assignee must furnish a bond in the amount pre-scribed in §§ 256.52 and 256.53 of this part.

* * *

(h) Your heirs, executors, administrators, successors, and assigns are bound to comply with each obligation under any lease and under the regulations in this chapter.

(1) You are jointly and severally liable for the performance of each nonmonetary obligation under the lease and under the regulations in this chapter with each prior lessee and with each operating rights owner holding an interest at the time the obligation accrued, unless this chapter provides otherwise.

(2) Sublessees and operating rights owners are jointly and severally liable for the performance of each nonmonetary obligation under the lease and under the regulations in this chapter to the extent that:

(i) The obligation relates to the area embraced by the sublease;

(ii) Those owners held their respective interest at the time the obligation accrued; and

(iii) This chapter does not provide otherwise.

* * *

Recently, the MMS has promulgated various forms to ensure that the filing of assignments, transfers, and various other regulatory documents are more uniform and to improve the accuracy and efficiency of adjudicating such filings.[9] Please note that separate forms for assignments must be filed on a lease by lease basis. 30 CFR §256.67.

C. Utilizing the MMS Leasing Guidelines Handbook.

Although OCSLA and the Code of Federal Regulations provide the law and regulations governing leasing, exploration, and production on the OCS, the MMS Leasing Guidelines Handbook provides the nuts and bolts of how to interact with the MMS, especially in relation to leasing and lease maintenance activities. As noted above, the MMS Leasing Guidelines Handbook can be downloaded from the MMS website (*www.gomr.mms.gov*), and provides practical guidance and information on the following topics:

(i) Qualifications and Issuance of Qualification Numbers;

(ii) Bond Requirements;

(iii) Oil and Gas Lease Sale Activities and Bidding Procedures;

---

[9] An index of relevant MMS forms, taken from the MMS website (*www.gomr.mms.gov*) is attached hereto as *Exhibit No. 2* in the Appendix.

(iv) Issuance, Maintenance, Transfers, and Relinquishment of Leases;

(v) Non-Required Filings;

(vi) MMS Lease Files;

(vii) Pipeline Rights-of-Way;

(viii) Fisherman's Contingency Fund; and

(ix) OCS Information Resources: Public Information Office.

We utilize this practical guide on a daily basis, but it does not provide sufficient information to cover every unique situation. Therefore, direct interaction with the MMS, primarily the adjudication office, is often necessary.

D. OCS Connect.

The MMS website (*www.gomr.mms.gov*) introduces OCS Connect as follows:

> The OCS Connect Vision . . .
>
> To increase operational efficiency and better serve MMS stakeholders — employees, citizens, industry, and other government agencies — through customized, secure electronic information exchange.

The website also touts the benefits to stakeholders, as follows:

(i) Maximize citizen involvement by delivering essential information and receiving input via the internet;

(ii) Streamline mission delivery by automating major business transactions and providing 'digital' data management, resulting in more timely decisions;

(iii) Simplify and unify government by minimizing redundant reporting, and streamlining government interactions with industry and the public; and

(iv) Leverage industry best practices by using common oil and gas standards and solutions (e.g. data model, exchange standards).

First indications that the MMS was becoming more web-based occurred a few years ago with the commencement of the process of scanning all lease files, public information files, and various additional files into a format for on-line accessibility. Presently, virtually all of the MMS lease files are now available on line. This obviously alleviates the need to be physically present at the MMS to conduct detailed reviews of lease files and other pertinent files.

OCS Connect is also designed to further enhance operational efficiency. The project commenced in 2001, and the transformation activities necessary to re-engineer data sharing were grouped into eight clusters, namely:

(i) Manage and Administer Leasing Program;

(ii) Protect Environmental Resources;

(iii) Analyze and Coordinate G&G Review;

(iv) Manage Plan Submittals;

(v) Manage Permit Requests;

(vi) Inspect Operations and Enforce Regulations;

(vii) Monitor Lessee and Operator Activity; and

(viii) Manage Reserves Inventory Program, Perform Resource Assessment.

As OCS Connect continues to unfold, we can all look for enhanced productivity and data sharing in these clusters in the years to come.

III. Abandonment Obligations and Bonding Requirements.

A. Background on Authorities.

Abandonment and bonding are important aspects of OCS leasing activities and, as such, MMS bonding regulations and related materials deserve special attention in this paper.

In addition to OCSLA (the primary source of authority) and applicable regulations,[10] the following publications of the MMS affect leasing activities, specifically including abandonment and bonding:

(a) Notice to Lessees ("NTL") - a notice to lessees and operators are instructions for the specifics of how the MMS will implement the promulgated rules and regulations.

(b) Letter to Lessees ("LTL") - a letter sent to all lessees and operators advising parties of official rules.

(c) Information to Lessees ("ITL") - an advisory or informational statement to lessees and operators of proposed policy or rulemaking changes.

As such, this section of the paper includes an analysis of these forms of "authority" promulgated by the MMS, as well as analysis and commentary on abandonment obligations themselves, assignor and assignee liability, MMS bonding requirements, including commentary and information on lease surety bonds, areawide bonds and supplemental bonds, leasing and operational procedures, and internal departmental functional responsibilities.

B. Abandonment Obligations.

Abandonment obligations generally encapsulate "non-monetary obligations" owed to the MMS and relate to (i) plugging and abandonment of wells (either temporary abandonment or permanent

[10] Identification of changes to regulations are initially published in the Federal Register and thereafter codified in the CFR.

abandonment), (ii) platform, pipeline and facility removal, (iii) site clearance, and (iv) other related decommissioning activities. Section 22 of the present form OCS lease includes contractual obligations of OCS lessees in favor of the lessor for abandonment obligations.

1. MMS Decommissioning Regulations.

Title 30, Part 250, Subpart Q of the Code of Federal Regulations discusses decommissioning activities in general, and provides:

(a) Decommissioning means:

(1) Ending oil, gas, or sulphur operations; and

(2) Returning the lease or pipeline right-of-way to a condition that meets the requirements of regulations of MMS and other agencies that have jurisdiction over decommissioning activities.

(b) Obstructions means structures, equipment, or objects that were used in oil, gas, or sulphur operations or marine growth that, if left in place, would hinder other users of the OCS. Obstructions may include, but are not limited to, shell mounds, wellheads, casing stubs, mud line suspensions, well protection devices, subsea trees, jumper assemblies, umbilicals, manifolds, termination skids, production and pipeline risers, platforms, templates, pilings, pipelines, pipeline valves, and power cables.

(c) *Facility* means any installation other than a pipeline used for oil, gas, or sulphur activities that is permanently or temporarily attached to the seabed on the OCS. Facilities include production and pipeline risers, templates, pilings, and any other facility or equipment that constitutes an obstruction such as jumper assemblies, termination skids, termination skids, umbilicals, anchors, and mooring lines.

30 CFR §250.1700.

The regulations expressly provide that the lessees (record title owner) and operating rights owners are "jointly and severally" responsible for all decommissioning obligations for facilities on leases, including those obligations related to lease-term pipelines, as those obligations accrue and until each obligation is met. The joint and several liability similarly applies to all holders of a right-of-way, including the physical pipelines and risers. 30 CFR §250.1701.

The regulations enumerate those activities which trigger decommissioning obligations. Decommissioning obligations arise or accrue when the lessees (record title owner) or operating rights owners do any of the following:

(a) Drill a well;

(b) Install a platform, pipeline, or other facility;

(c) Create an obstruction to other users of the OCS;

(d) Are or become a lessee or the owner of operating rights of a lease on which there is a well that has not been permanently plugged according to this subpart, a platform, a lease term pipeline, or other facility, or an obstruction;

(e) Are or become the holder of a pipeline right-of-way on which there is a pipeline, platform, or other facility, or an obstruction; or

(f) Re-enter a well that was previously plugged according to this subpart.

30 CFR §250.1702.

In connection with any decommissioning activity, a lessee must submit decommissioning applications and reports. 30 CFR §1704. Such applications are typically in Form MMS-124, Application for Permit to Modify.

a. Abandonment of Wells..

Depending on the circumstances, lessees must either permanently or temporarily abandon all wells as provided in the following sections discussing applicable MMS regulations.

i. Permanent Abandonment of Wells.

Lessees must permanently abandon all wells in a manner to ensure (a) downhole isolation of hydrocarbon and sulphur zones; (b) protection of freshwater aquifers; and (c) prevention of migration of formation fluids within the wellbore or to the seafloor. 30 CFR §250.1714. Any well which (a) poses a hazard to safety or the environment, or (b) is no longer used or useful for lease operations must be plugged and abandoned in accordance with the provisions of this subpart. 30 CFR §250.1711. The filing of Form MMS-124 is required when lessees seek to either temporarily or permanently abandon or plug wells. 30 CFR §§250.1712 and 250.1721. Within 30 days after the well is permanently plugged and abandoned, lessees must submit Form MMS-124. 30 CFR §250.1717. Furthermore, as required under Section 22 of the current lease form, the regulations provide that all wells must be permanently plugged.

While the District Manager may require additional well plugs in certain circumstances, 30 CFR §250.1715 includes a chart which spells out the requirements for permanent well plugging and abandonment for the following scenarios:

(1) Zones in open hole;

(2) Open hole below casing;

(3) A perforated zone that is currently open and not previously squeezed or isolated;

(4) A casing stub where the stub end is within the casing;

(5) A casing stub where the stub end is below the casing;

(6) An annular space that communicates with open hole and extends to the mud line;

(7) A subsea well with unsealed annulus;

(8) A well with casing;

(9) Fluid left in the hole; or

(10) Permafrost areas.

30 CFR § 250.1715.

ii. Temporary Abandonment of Wells.

A lessee wishing to temporarily abandon a well must not only meet certain specified permanent abandonment requirements, but also meet additional requirements found in 30 CFR §250.1721. In order to maintain the temporarily abandoned status of a well, the lessee shall provide Form MMS-124, Application for Permit to Modify, as well as adhering to the plugging and testing requirements for permanently plugged wells, but without the need to sever the casings, remove the wellhead or clear the site. 30 CFR §250.1721.

b. Removal of Platforms, Facilities, and Pipelines.

All platforms and facilities must be removed within one (1) year after the lease or pipeline right-of-way terminates, unless MMS grants approval to maintain the structure to conduct other activities (30 CFR §250.1725(a)), and an application must be submitted to the Regional Supervisor to obtain approval prior to commencing removal operations. 30 CFR §250.1725(b).

For leases and pipeline rights-of-way located in the Pacific OCS Region or the Alaska OCS Region, an "initial platform removal application" is required. It must include the following information:

(a) Platform and other facility removal procedures, including the types of vessels and equipment you will use;

(b) Facilities (including pipelines) you plan to remove or leave in place;

(c) Platform or other facility transportation and disposal plans;

(d) Plans to protect marine life and the environment during decommissioning operations, including a brief assessment of the environmental impacts of the operations, and procedures and mitigation measures that you will take to minimize the impacts; and

(e) A projected decommissioning schedule.

30 CFR §250.1726.

As for pipelines, the Regional Supervisor may allow for abandonment in place if the pipeline does not constitute a hazard (obstruction) to navigation and commercial fishing operations, unduly

interfere with other uses of the OCS, or have adverse environmental effects. 30 CFR §250.1750. Otherwise, you must:

(a) Submit a pipeline removal application in triplicate to the Regional Supervisor for approval. Your application must be accompanied by payment of the service fee listed in §250.125. Your application must include the following:

(1) Proposed removal procedures;

(2) If the Regional Supervisor requires it, a description, including anchor pattern(s), of the vessel(s) you will use to remove the pipeline;

(3) Length (feet) to be removed;

(4) Length (feet) of the segment that will remain in place;

(5) Plans for transportation of the removed pipe for disposal or salvage;

(6) Plans to protect archaeological and sensitive biological features during removal operations, including a brief assessment of the environmental impacts of the removal operations and procedures and mitigation measures that you will take to minimize such impacts; and

(7) Projected removal schedule and duration.

(b) Pig the pipeline, unless the Regional Supervisor determines that pigging is not practical; and

(c) Flush the pipeline.

30 CFR §250.1752. If the Regional Supervisor determines that a pipeline decommissioned in place becomes an obstruction, it must be removed. 30 CFR §250.1754.

c. Site Clearance.

Within sixty (60) days after you permanently plug a well or remove a platform or other facility, you must verify that the site is clear of obstructions by using one of the following methods:

(a) For a well site, you must either:

(1) Draft a trawl over the site;

(2) Scan across the location using sonar equipment;

(3) Inspect the site using a diver;

(4) Videotape the site using a camera on a remotely operated vehicle (ROV); or

(5) Use another method approved by the District Manager if the particular site conditions warrant.

(b) For a platform or other facility site in water depths less than 300 feet, you must drag a trawl over the site;

(c) For a platform or other facility site in water depths 300 feet or more, you must either:

(1) Draft a trawl over the site;

(2) Scan across the site using sonar equipment; or

(3) Use another method approved by the Regional Supervisor if the particular site conditions warrant.

30 CFR §250.1740.

2. Assignor/Assignee Liability.

As noted above, 30 CFR §256.62 (Assignment of Lease or Interest in Lease) discusses the retention of liabilities by assignors. Subsections 256.62(d), (e), and (f) provide the following:

(d) The assignor shall be liable for all obligations under the lease accruing prior to the approval of the assignment.

(e) The assignee shall be liable for all obligations under the lease that accrue after the approval date of an assignment and shall comply with all regulations under the act.

(f) The Regional Director may require the assignor to bring the lease into compliance if its assignee, or any subsequent assignee, fails to perform any obligations under the lease or applicable regulations, so long as the obligations accrued prior to approval of the assignment.[11]

3. Designation of Operator Issues.

Designating an operator under 30 CFR §250.143 will serve as acceptable authority for the operator to act on behalf of the lessee to fulfill the lessee's abandonment obligations under OCSLA, the lease, and the applicable regulations. 30 CFR §250.146.

---

[11] Subsections (d) and (e) of 30 CFR §256.62 provide, in their entirety, as follows:

(d) You, as assignor, are liable for all obligations that accrue under your lease before the date that the Regional Director approves your request for assignment of the record title in the lease. The Regional Director's approval of the assignment does not relieve you of accrued lease obligations that your assignee, or a subsequent assignee, fails to perform.

(e) Your assignee of each subsequent assignee are liable for all obligations that accrue under the lease after the date that the Regional Director approves the governing assignment. They must:

(1) Comply with all the terms and conditions of the lease and all regulations issued under the Act; and

(2) Remedy all existing environmental problems on the tract, property abandon all wells, and reclaim the lease site in accordance with part 250, subpart Q.

(f) If your assignee, or a subsequent assignee, fails to perform any obligation under the lease or the regulations in this chapter, the Regional Director may require you to bring the lease into compliance to the extent that the obligation accrued before the Regional Director approved the assignment of your interest in the lease.

4. Abandonment Obligations Under Lease Agreement.

Under the current version of the Oil and Gas Lease of Submerged Lands Under the Outer Continental Shelf Lands Act, Form MMS-2005 (March 1986), which supersedes MMS-2005 (August 1982),[12] section 22 states as follows:

> *Removal* of *Property on Termination* of *Lease.* Within a period of one year after termination of this lease in whole or in part, the lessee shall remove all devices, works and structures from the premises no longer subject to the lease in accordance with applicable regulations and orders of the director. However, the Lessee may with the approval of a director, continue to maintain devices, works and structures on the leased area for drilling or producing on other leases.

As previously noted, if a lessee can demonstrate to the MMS that a particular platform, facility, satellite, or structure has some future utility, the MMS will permit the structure to remain so long as that structure can serve a purpose for exploration, production, or development on the OCS. 30 CFR §250.1725.

5. Removal Extensions.

In certain instances the MMS has granted extensions of time within which to remove existing facilities or to clear the site for abandonment purposes. An application for an extension of time in which to remove structures should be made to the Regional Supervisor for Field Operations of the MMS.

Usually, the MMS will grant an additional six (6) month extension to comply with abandonment obligations. Extensions may be premised upon unavailability of equipment or materials to remove those structures. Notwithstanding the extension, the lessee is obligated to maintain the integrity and safety of those structures even though the lease has terminated.

C. Bonding Rules, Regulations, and Related Authorities.

1. 1993 Final Rule.

On August 27, 1993, a final rule was promulgated by the MMS entitled "Surety Bond Coverage for Leasing of Sulphur or Oil and Gas in the Outer Continental Shelf (OCS)." 58 Fed. Reg. 45,255 (August 27,

---

[12] In 62 Federal Register 19961, issued on April 24, 1997, the MMS indicated its intent to review the offshore lease form, Form MMS-2005, which document had not been revised since 1986. Part of the review and revision process was to satisfy then President Clinton's directive to use "plain English." In addition, the MMS considered changes to the lease form to reflect current policies and to address any issues that may arise during the review period. However, the effort to amend the lease form never developed beyond the notice for comment in 1997.

1993). The final rule became effective November 26, 1993 ("1993 Final Rule).[13]

The MMS took the position that, after approval of a lease assignment, the assignor continues to be liable to the MMS for the performance of the obligations with respect to wells, structures or obstructions in existence and not plugged or removed at the time of the assignment.

The MMS noted that where there are two or more lessees, only one needs to maintain the bond for the lease inasmuch as each lessee is responsible for the full performance of the lease obligation. This MMS position has caused most large companies to express substantial disagreement.

Under a Notice to Lessees (NTL No. 93-2N) dated October 6, 1993 "Liability of Assignors, Assignees and Co-lessees for Plugging of Wells and Removal of Property on Termination of an Outer Continental Shelf Oil and Gas Lease," the MMS specifically stated that it is not authorized or funded to assume responsibility for these obligations.

Based on this NTL, the MMS looks first to the designated operator to perform activities to address plugging and abandonment and related decommissioning obligations. Should the operator be unable to perform

---

[13] The 1993 Final Rule broke up bonding requirements based upon lease status:

(i) $50,000 for a single lease or $300,000 area wide bond with no MMS approved operational activity and no submittal of assignments.

(ii) $200,000 for a single lease or $1,000,000 areawide bond for proposed exploration plans or revisions on proposed assignment.

(iii) $500,000 for a single lease or $3,000,000 areawide bond for proposed development plan or revision with proposed assignment.

The comments in the Federal Register stated that the 1993 Final Rule established a three tier approach to the bond coverage requirements for OCS oil and gas leases similar to the one proposed in the Notice of Proposed Rulemaking that was published on January 24, 1990, 55 Fed. Reg. 2388, as corrected, on February 2, 1990, 55 Fed. Reg. 3603.

The 1993 Final Rule permitted a lessee to maintain a $300,000 area-wide bond if it holds leases that have no proposed exploration and development and production activity. The 1993 Final Rule still permitted a successful bidder to place a $50,000 surety bond on a lease. A $50,000 lease surety bond is not necessary if an area-wide bond is place. The 1993 Final Rule retained the ability to substitute an operator's bond in an equal amount.

The 1993 Final Rule permitted the MMS a great deal of discretion in determining additional security in the form of a supplemental bond or requiring increases in coverage in an existing bond when additional security is deemed necessary. This discretionary authority allowed the authorized officer to review a number of factors, including without limitation, (i) financial wherewithal, (ii) record of meeting obligations, (iii) projected financial strength.

The comments indicate that the inclusion of such examples informs the public of the kind of considerations that have been and will be evaluated in determining the need for an increase in the bond coverage required on a lease. The MMS stated that it is not a substantive change from the kinds of facts the MMS currently examines.

the lessee's obligations to plug and abandon wells, remove platforms and other facilities, and clear the sea floor of obstructions, the MMS will normally require any and all of the lessees to perform the activities necessary to bring about compliance. If there is no current lessee able to perform, the MMS will require lessees who held the lease during or after the time when the facilities were installed or the constructions created to perform those functions. This approach is logically tied to a factual assumption that the party who benefited financially in the past should be responsible for the removal.

2. 1997 Final Rule.

On May 22, 1997, a final rule was promulgated by the MMS entitled "Surety Bonds for Outer Continental Shelf Leases" (the "1997 Final Rule"). The 1997 Final Rule was published at 62 Federal Register 27948 and became effective August 20, 1997.

The 1997 Final Rule amended the 1993 Final Rule. The 1993 Final Rule, discussed above, was a transitional device to introduce levels of bonding coverage for all lessees. The 1997 Final Rule set a deadline of December 8, 1997 for every lessee to fully comply with the bond coverage requirements. Most importantly, the 1997 Final Rule was issued to clarify the rule that co-lessees (record title owners) and operating rights owners are jointly and severally liable for compliance with the regulations and the terms and conditions of the OCS oil and gas leases for non-monetary obligations. In addition, the 1997 Final Rule clarified the position of the MMS that an assignor remains responsible for all wells and facilities that were in existence at the time the assignor assigned its interest until the wells are plugged and abandoned, the facilities are decommissioned, and the site is reclaimed. The 1997 Final Rule also established a mechanism for the use of lease-specific abandonment accounts and third party guarantees in lieu of supplemental bond requirements. Finally, the rule set higher levels of bond coverage.

With respect to present bond requirements, the regulations continue to provide that, before the MMS issues a new lease or approves an assignment of an interest in an existing lease, the following minimum bonds must be in place:

Stage of Development	*Lease Bond*	*Areawide Bond*
Issuance of Lease	$50,000	$300,000
Exploration Plan for Approval	$200,000	$1,000,000
Development and Production Plan or Development Operations Co-ordination Document for Approval	$500,000	$3,000,000

While these bonding levels are the same as those required under the 1993 Final Rule, the 1997 Final Rule requires that, as of December 8, 1997, all affected parties must be in compliance and satisfy the bond

requirements set forth above. The Regional Director may determine that additional security in the form of a supplemental bond(s) over and above these amounts may be necessary to ensure compliance with the non-monetary obligations under the lease.

There was a challenge to the MMS regulatory change of the general bonding requirements. Pacific Operators Offshore, Inc., a lessee for OCS-P 0166, sought a waiver of the lessee's regulatory duty to provide a $500,000 bond. Pacific Operators appealed the denial of the waiver by the Pacific OCS Regional Office of the MMS. See *In re: Pacific Operators Offshore, Inc.*, 154 IBLA 100 (December 20, 2000). The appellant asserted that the 1997 Final Rule was ambiguous in identifying the bonding obligations of long-time operators. The appellant argued that the application of the new $500,000 bond requirement to an existing long-time operator imposed a retroactive duty that was not clearly articulated in the earlier notice of proposed rulemaking. The record disclosed a series of exchanges of communications between the MMS and the appellant concerning the bonding requirements. Administrative Law Judge James P. Terry, writing the IBLA decision, found that the MMS stated objective of the 1993 Final Rule was to identify the appropriate levels of bond coverage required of lessees. The 1993 Final Rule provided that, if a lessee could demonstrate to the satisfaction of the MMS that the appellant's wells and platforms could be abandoned and removed and the site cleared for less than the amount of the lease bond coverage, the MMS would have to accept a surety bond in an amount less than the $500,000 lease bond. The IBLA decision also indicated that the record demonstrated that the MMS gave ample and consistent notices of its intent to increase bonding requirements for all OCS lessees, and that the 1997 Final Rule was clear that as of December 8, 1997, all lessees were required to be in compliance with the higher bonding requirements.

The 1997 Final Rule also mandated that all bonds must be payable upon demand to the Regional Director, guarantee compliance with all obligations under the lease and the regulations, and guarantee compliance with the obligations of *all* lessees, operating rights owners and operators on the lease. The rule also allows, as alternatives to traditional bonds, the creation of lease-specific abandonment accounts or the use of third-party guarantees. The requirements for the issuance of a third-party guarantee are quite extensive, and the rule requires that (a) the guarantor execute an indemnity agreement which includes a confession of judgment, and (b) the guaranty provide that, if the Regional Director determines that the guarantor, the lessee, the operator or the operating rights owner is in default under a lease, the guarantor will not challenge such determination and will remedy the default. Although a third party guarantor need not qualify as a surety, it must agree to perform all guaranteed obligations without the dollar limitation permitted a surety.

The 1997 Final Rule also includes provisions regarding joint and several liability for the performance of non-monetary obligations under a lease and the regulations. In particular, the rule provides that co-lessees and operating rights owners are jointly and severally liable for all lease and regulatory non-monetary obligations and continues the MMS' position that an assignor of lease interests remains liable for abandonment obligations associated with wells drilled or used while the assignor held its OCS lease interest. In the Comment Section of the Final Rule, the MMS spends considerable time attempting to justify its position taken in this new rule regarding joint and several liability. The MMS rejected recommendations that there be pro-rata responsibility among lease interest owners or that co-lessees be able to object to the approval of an assignment if the existing co-lessees are concerned that the new assignee may not have the financial wherewithal to fulfill the non-monetary obligations. The MMS responded that "since lessees are jointly and severally responsible for compliance with lease terms and conditions, it is not necessary, desirable or practical to require every owner of an interest in a lease to submit and maintain a separate lease bond that only addresses its interest." The MMS also argues that it is appropriate to have a different treatment of parties with respect to lease non-monetary obligations versus monetary obligations; with respect to royalty payments (*i.e.*, monetary obligations), the lessees and operating rights owners are treated on a pro-rata basis under the Federal Oil and Gas Royalty Simplification and Fairness Act and the implementing payor liability provisions. Finally, under the 1997 Final Rule, the MMS has taken a position that, with respect to non-monetary obligations, it does not serve the public interest to allow the release of an undivided lessee or an operating rights owner from responsibility if there has been only partial performance of the non-monetary base obligations such as well abandonment. While this is the first time that joint and several liability for non-monetary lease obligations has been articulated in the regulations, the rule does reflect the position the MMS has taken since the late 1980s and early 1990s.

For cross reference purposes, please note that the provisions of the 1997 Final Rule have been incorporated into applicable regulations, primarily at 30 CFR §256.52, et seq.

3. General Surety Bonds.

a. General Lease Surety Bond.

The MMS has established Guidelines for General Lease Surety Bonds. See NTL No. 2000-G16 dated effective September 7, 2000 (the "Guidelines"). As previously indicated, the Guidelines establish levels of lease activities to determine the amount of required general surety bond coverage. The levels of coverage for a general lease surety bond are as follows:

No Operations - A $50,000 lease-specific bond or $300,000 area-wide general lease surety bond for leases with no MMS approved operational activity plan, or for leases under an MMS approved operational activity plan but with no submittal to MMS of assignment or operational plan.

Exploration - A $200,000 lease-specific or $1,000,000 area-wide general lease surety bond for leases included within a proposed Exploration Plan (EP) or a significant revision to an approved EP, or for a proposed assignment of lease with an approved EP.

Development - A $500,000 lease specific or $3,000,000 area-wide general lease surety bond for leases included within a proposed Development and Production Plan (DPP) or Development Operations Coordination Document (DOCD) or a significant revision to an approved DPP or DOCD, or for a proposed assignment with an approved DPP or DOCD.

The current General Bond Form is the Outer Continental Shelf (OCS) Mineral Lessee's and Operator's Bond - Form MMS-2028 (August 2007).

b. General Pipeline Surety Bond.

In addition to the requirement to post a general lease surety bond, a holder of a pipeline right-of-way grant that crosses or traverses OCS blocks is required to post a bond in the amount of $300,000. The current General Pipeline Bond Form is the Outer Continental Shelf (OCS) Pipeline Right-of-Way Grant Bond - Form MMS-2030 (January 2006). The general pipeline surety of $300,000 is sufficient bond coverage for multiple right-of-way grants.

4. Supplemental Bonding and Procedures.

It should be stressed that the Regional Director also has the discretionary authority to require additional security above the amounts of the general lease bonds prescribed under 30 CFR §256.52(a) and 30 CFR §256.53(a) and (b). The regulations, specifically, 30 CFR §256.53(d) and (e), provide that the Regional Director can require that additional security be in the form of a supplemental bond. The additional amount of security is based upon calculations of the potential lease abandonment liability and an evaluation, among other considerations, of the lessee's ability to carry out its financial obligations. Each lease with lease abandonment liability must be covered by a supplemental bond ***unless at least one lessee can demonstrate*** to the satisfaction of the MMS ***that such lessee has the financial ability to ensure*** that all wells, platforms and other structures can be abandoned, removed and the sites are cleared of such obstructions. The current Supplemental Bond Form is the Outer Continental Shelf (OCS) Mineral Lessee's and Operator's Supplemental Plugging and Abandonment Bond — Supplemental Bond

(Form MMS-2028A). Supplemental bonding and the procedures are also outlined in the NTL No. 2003-N06, entitled "Supplemental Bond Procedures."

The MMS will review potential lease liabilities prior to the approval of the following:

(a) assignment of record title interest in a lease with any abandonment liability; or

(b) exploration plans; or

(c) development and production plans; or

(d) development operations coordination documents; and

(e) any other time when the MMS infers that the lessee may not have the wherewithal to carry out the obligations of an OCS lease.

Certain factors are considered by the MMS in making a determination as to supplemental bond requirements, such as the size and number of existing facilities, abandonment and site clearance estimates, proven reserves and production expectations, among other considerations. The MMS may require a total bond amount immediately, or may permit the bond amount to accumulate over a period of time. The rate of accumulation is usually based upon the relationship between the total abandonment cost and the quality of the financial assets maintained by the lessee.

The MMS may permit a staged increase of supplemental bond amounts. The initial supplemental bond may be set at less than 50% of the abandonment cost if the applicant can satisfy select criteria. To determine a lessee's experience and reliability, the MMS may look at the following:

(a) sufficient financial strength to carry out existing and anticipated lease activities and obligations as evidenced by any one of the following: (i) credit references; (ii) available bank credit; (iii) audited financial statements, including auditors' certificates, balance sheets, and profit and loss statements; and (iv) sufficient trade references to demonstrate capability to carry out existing and anticipated lease activities and obligations as evidenced by a listing of names and addresses of lessees, drilling contractors and suppliers with whom the applicant has dealt;

(b) a sufficient track record of OCS operations to demonstrate capability to carry out existing and anticipated lease activities and obligations as evidenced by (i) an objective listing of projects successfully completed and (ii) resumes of the key people involved.

30 CFR §256.53.

The MMS has established general guidelines for plugging, abandonment and site clearance estimates for wells, platforms, and other structures. These general estimates are as follows:

A. Plugging and abandoning a wellbore will cost $100,000 per wellbore for all water depths.[14]

B. Dismantling and removing a platform will vary with water depth as follows (removing and scrapping on-shore):

Water depths of 150 feet or less -	$400,000
Water depths between 151 and 200 feet -	$600,000
Water depths between 201 and 299 feet -	$1,250,000
Water depths of 300 feet or more -	$2,000,000+

C. Site clearance will vary with water depth as follows:

Water depths of 150 feet or less -	$300,000
Water depths between 151 and 249 feet -	$400,000
Water depths of 250 feet and greater -	$500,000+

The MMS maintains a database for specific leases and pipeline rights-of-way which details the actual structures. You can access the database by using the MMS Online Query for Plugging and Abandonment Liability located on the MMS website (*www.gomr.mms.gov*).

Within forty-five (45) days following written notification by the MMS that additional security is requires, the lessee must submit one of the following:

1. A lease-specific supplemental bond, United States Treasury Securities, or an alternate form approved by the MMS, in the full amount required.

2. A plan whereby lessee commits to fully fund a lease-specific abandonment escrow account. Generally, the lessee must fully fund a lease-specific abandonment account within four (4) years or by the beginning of the year in which it is projected that eighty (80) percent of the originally recoverable reserves have been produced, whichever is earlier.

3. A Third-Party Guarantee in lieu of a supplemental bond.[15]

---

[14] We have verbally been told by MMS personnel that this may be raised to $150,000 in the very near future.

[15] Please note the following from 30 CFR §256.57:

(a) *When the Regional Director may accept a third-party guarantee.* The Regional Director may accept a third-party guarantee instead of an additional bond under §256.53(d) if:

(1) The guarantee meets the criteria in paragraph (c) of this section;

(2) The guarantee includes the terms specified in paragraph (d) of this

It should be noted that the regulations allow for other forms of security to cover general lease performance obligations, although such arrangements are not commonly used.[16]

---

section;

(3) The guarantor's total outstanding and proposed guarantees do not exceed 25 percent of its unencumbered net worth in the United States; and

(4) The guarantor submits an indemnity agreement meeting the criteria in paragraph (e) of this section;

(b) *What to do if your guarantor becomes unqualified.* If, during the life of your third-party guarantee, your guarantor no longer meets the criteria of paragraphs (a)(3) and (c)(3) of this section, you must:

(1) Notify the Regional Director immediately; and

(2) Cease production until you comply with the bond coverage requirements of this subpart.

(c) *Criteria for acceptable guarantees.* If you propose to furnish a third party's guarantee, that guarantee must ensure compliance with all lessees' lease obligations, the obligations of all operating rights owners, and the obligations of all operators on the lease. The Regional Director will base acceptance of your third-party guarantee on the following criteria:

(1) The period of time that your third-party guarantor (guarantor) has been in continuous operation as a business entity where:

(i) Continuous operation is the time that your guarantor conducts business immediately before you post the guarantee; and

(ii) Continuous operation excludes periods of interruption in operations that are beyond your guarantor's control and that do not affect your guarantor's likelihood of remaining in business during exploration, development, production, abandonment, and clearance operations on your lease.

(2) Financial information available in the public record or submitted by your guarantor, on your guarantor's own initiative, in sufficient detail to show to the Regional Director's satisfaction that your guarantor is qualified based on:

(i) Your guarantor's current rating for its most recent bond issuance by either Moody's Investor Service or Standard and Poor's Corporation;

(ii) Your guarantor's net worth, taking into account liabilities under its guarantee of compliance with all the terms and conditions of your lease, the regulations in this chapter, and your guarantor's other guarantees;

(iii) Your guarantor's ratio of current assets to current liabilities, taking into account liabilities under its guarantee of compliance with all the terms and conditions of your lease and the regulations in this chapter and your guarantor's other guarantees; and

(iv) Your guarantor's unencumbered fixed assets in the United States.

(3) When the information required by paragraph (c) of this section is not publicly available, your guarantor may submit the information in the following table. Your guarantor must update the information annually within 90 days of the end of the fiscal year or by the date prescribed by the Regional Director.

[Table Omitted]

16 *See* 30 CFR §256.52(f):

You may pledge U.S. Department of the Treasury (Treasury) securities instead of a bond. The Treasury securities you pledge must be negotiable for an amount of cash

5. Supplemental Bond Waivers.

The MMS maintains a listing of those companies who, by virtue of the company's financial strength or the strength of a third party guarantor, are deemed exempt from the requirements to post supplemental bonds because the financial strength (based on the ratios established by the regulations) is sufficient to fulfill the outstanding abandonment obligations for leases owned by such companies. Currently, the MMS database reflects that there are 154 lessees who possess waivers by virtue of (i) meeting the financial ratios; (ii) third party guarantees; or (iii) thresholds met by current production. The waived or exempt list may be viewed online on the MMS website (*www.gomr.mms.gov*)

6. Termination of Period of Liability.

The regulations governing the General Lease Bond (Form MMS-2028), General Pipeline Bond (Form MMS-2030) and the Supplemental Bond (Form MMS-2028A) establish a period of liability for which a bond may be terminated. The termination of the period of liability must be made as a written request by the principal and must justify a need. (See, Oil and Gas Leasing Procedures Guidelines - OCS Report MMS 2001-076). It should be noted that if there are any outstanding liabilities, such as unpaid royalties, lease abandonment obligations, civil penalties (either assessed or unassessed which are under review), the bond will not be terminated until the outstanding obligation has been satisfied. Both the general bond and supplemental bond have a section in their respective bond forms which require that, in addition to the obligations

---

equal to the value of the bond they replace.

(1) If you pledge Treasury securities under this paragraph (f), you must monitor their value. If their market value falls below the level of bond coverage required under this subpart, you must pledge additional Treasury securities pledged to the required amount.

(2) If you pledge Treasury securities, you must include authority for the Regional Director to sell them and use the proceeds when the Regional Director determines that you fail to satisfy any lease obligation;

See also 30 CFR §256.52(g):

You may pledge alternative types of security instruments instead of providing a bond if the Regional Director determines that the alternative security protects the interests of the United States to the same extent as the required bond.

(1) If you pledge an alternative type of security under this paragraph, you must monitor the securities value. If its market value falls below the level of bond coverage required under this subpart, you must pledge additional securities to raise the value of the securities pledged to the required amount.

(2) If you pledge an alternative type of security, you must include authority for the Regional Director to sell the security and use the proceeds when the Regional Director determines that you failed to satisfy any lease obligation.

of the principal during the period of liability for a given bond, the principal and the surety agree and accept the certain obligations.

The bond forms require the principal and surety to check the applicable obligations to be covered by the bond, as follows:

1. No obligations other than the obligations of the principal during the period of liability of this bond.

2. All obligations of all previous sureties or guarantors even if the obligations are not obligations of the principal during the period of liability of this bond.

3. All obligations of all previous sureties or guarantors even if the obligations are not obligations of the principal during the period of this bond (with certain exceptions or limitations).

Checking the applicable obligations is critical in the determination of liabilities covered by the bond. You should note before each of the categories of obligations there is actually no box to place the checkmark. You should place a checkmark at the beginning of the sentence that is applicable to the obligations the principal and surety are agreeing to assume. Furthermore, both forms specifically indicate that the selection of the second or third category is subject to the approval of the Regional Director.

It should be noted that the regulations distinguish between "termination" of the period of liability and "cancellation" of all liability. Terminating the period of liability of a bond ends the period during which obligations continue to accrue, but does not relieve the surety of the responsibility for obligations that accrued during the period of liability. Canceling a bond relieves the surety of all liability. The liabilities that accrue during a period of liability include (i) obligations that started to accrue prior to the beginning of such period of liability and which have not been satisfied and (ii) obligations that begin to accrue during the period of liability. See 30 CFR §256.58.

Specific requirements apply for cancellation of a surety bond. The Regional Director must determine (a) there are no outstanding obligations and (b) the replacement bond is provided and the new surety agrees to assume all presently outstanding and all future liabilities under the bond that is to be cancelled. See 30 CFR §256.58(b).[17]

---

[17] 30 CFR §256.58 provides, in its entirety:

This section defines the terms and conditions under which MMS will terminate the period of liability of a bond or cancel a bond. Terminating the period of liability of a bond ends the period during which obligations continue to accrue but does not relieve the surety of the responsibility for obligations that accrued during the period of liability. Canceling a bond relieves the surety of all liability. The liabilities that accrue during a period of liability include obligations that started to accrue prior to the beginning of the period of liability and had not been met and obligations that begin accruing during the period of liability.

It should be noted that MMS will issue a determination letter which indicates that the Adjudication Unit has reviewed the relevant records to either cancel or terminate the bond. The MMS may determine that the period of liability is considered to be terminated as of a date certain ("Termination Date"), except as to any liability which may have accrued prior to that date. Furthermore, the MMS may indicate that, notwithstanding the fact that the period of liability has terminated, the bond cannot be cancelled until all liabilities that may have accrued under such bond are assumed by another principal and/or surety or seven (7) from the Termination Date.

(a) When the surety under your bond requests termination:

(1) The Regional Director will terminate the period of liability under your bond within 90 days after MMS receives the request; and

(2) If you intend to continue operations, or have not met all end of lease obligations, you must provide a replacement bond of an equivalent amount.

(b) If you provide a replacement bond, the Regional Director will cancel your previous bond and the surety that provided your previous bond will not retain any liability, provided that:

(1) The new bond is equal to or greater than the bond that was terminated, or you provide an alternative form of security, and the Regional Director determines that the alternative form of security provides a level of security equal to or greater than that provided for by the bond that was terminated;

(2) For a base bond submitted under §256.52(a) or under §256.53(a) or (b), the surety issuing the new bond agrees to assume all outstanding liabilities that accrued during the period of liability that was terminated; and

(3) For supplemental bonds submitted under §256.53(d), the surety issuing the new supplemental bond agrees to assume that portion of the outstanding liabilities that accrued during the period of liability which was terminated and that the Regional Director determines may exceed the coverage of the base bond, and of which the Regional Director notifies the provided of the bond.

(c) This paragraph applies if the period of liability is terminated for a bond but the bond is not replaced by a bond of an equivalent amount. The surety that provided your terminated bond will continue to be responsible for accrued obligations:

(1) Until the obligations are satisfied; and

(2) For additional periods of time in accordance with paragraph (d) of this section.

(d) When your lease expires or is terminated, the surety that issued a bond will continue to be responsible.

IV. Conclusion.

After reviewing this paper, it is apparent that there is an overlap between OCS title issues and pertinent MMS regulations. Although all possible aspects of OCS title and MMS regulations cannot be included in a single paper, we hope that the information provided herein is beneficial in creating an appropriate overview of these activities which are vital to the oil and gas industry as it operates on the OCS and in the GOM.