STATE OF NEW MEXICO
ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT
OIL CONSERVATION COMMISSION

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**APPLICATION OF THE NEW MEXICO OIL CONSERVATION DIVISION, THROUGH THE ENFORCEMENT AND COMPLIANCE MANAGER, FOR THE ADOPTION OF NEW RULES, 19.15.1.37 NMAC, 19.15.1.38 NMAC, 19.15.3.100 NMAC, AND 19.15.14.1227 NMAC; AND THE AMENDMENT OF 19.15.1.7 NMAC, 19.15.3.101 NMAC, 19.15.3.102 NMAC, 19.15.4.201 NMAC, 19.15.4.203 NMAC, 19.15.4.1101 NMAC, 19.15.9.701 NMAC, 19.15.13.1103 NMAC, 19.15.13.1104 NMAC, AND 19.15.13.1115 NMAC**

**CASE NO. 13564**

**BRIEF IN SUPPORT OF**
**APPLICATION FOR RULE ADOPTION AND AMENDMENT**

The New Mexico Oil Conservation Division (the Division) files this brief in support of its application for rule adoption and amendment in case 13564.

The proposed rule changes will improve the Division's ability to enforce the Oil and Gas Act, Chapter 70, Article 2 NMSA 1978 (the Act), and the rules and orders issued pursuant to that Act. The Act gives the Division broad enforcement powers, including "jurisdiction, authority and control of and over all persons, matters or things necessary or proper to enforce effectively the provisions of this act or any other law of this state relating to the conservation of oil or gas...." NMSA 1978, § 70-2-6(A). The Division is also empowered,

> and it is its duty, to prevent waste prohibited by this act and to protect correlative rights, as in this act provided. To that end, the division is empowered to make and enforce rules, regulations and orders, and to do whatever may be reasonably necessary to carry out the purpose of this act, whether or not indicated or specified in any section hereof.

NMSA 1978, § 70-2-11 (A). And "apart from any authority, express or implied, elsewhere given to or existing in the oil conservation division by virtue of the Oil and Gas Act or the statutes of this state, the division is authorized to make rules, regulations and orders for the purposes and with respect to" its enumerated powers. NMSA 1978, § 70-2-12(B). Those powers include the Division's environmental duties, such as regulating the disposition of produced water to protect against the contamination of fresh

water, NMSA 1978, § 70-2-12(B)(15), and regulating the disposition of nondomestic wastes to protect public health and the environment, NMSA 1978, §§ 70-2-12(B)(21) and (22).

The Division proposes to use those broad powers, as well as specific statutory powers addressed below, to create rules that will allow the Division to carry out its duties, and make best use of its limited enforcement resources.

The purpose of this brief is to present a detailed description of the proposed rule changes, to reduce the need for a line-by-line discussion of the proposed changes at the hearing.

Note that the Division proposes to amend existing rules to conform to the capitalization and format requirements of the New Mexico Administrative Code (NMAC). The Division has also re-written existing rules in the active voice. These changes are not discussed below, unless the change from passive voice to active voice resulted in a substantive change in the rule.

## ESTABLISHING PROCEDURES FOR COMPLIANCE ACTIONS

### 1. [New] 19.15.14.1227 COMPLIANCE PROCEEDINGS

The Division's current procedural rules (the 1200 series) set out requirements for rulemaking proceedings and adjudicatory proceedings brought to resolve disputes between operators. The rules do not address cases brought to obtain compliance. The Division proposes new rule 19.15.14.1227 NMAC [Rule 1227] to address procedural issues unique to compliance cases.

**Paragraph A** provides that the rules in the 1200 series applicable to adjudicatory proceedings will apply to compliance proceedings unless specified in Rule 1227. This eliminates unnecessary duplication.

**Paragraph B** defines compliance proceeding as an adjudicatory proceeding in which the Division seeks an order imposing sanctions for violation of the Act or a rule or order issued pursuant to the Act. Note that as written, the rule recognizes compliance proceedings brought by the Division; other entities may not initiate a compliance proceeding. The proposed rule provides a non-exclusive list of the sanctions the Division may seek. Those sanctions are discussed below.

a) Compliance. At a minimum, the Division may seek an order requiring future compliance.

b) Civil penalties. By statute,

> [a]ny person who knowingly and willfully violates any provision of the Oil and Gas Act or any provision of any rule or order issued pursuant to that act shall be subject to a civil penalty of not more than one thousand

dollars ($1,000) for each violation. For purposes of this subsection, in the case of a continuing violation, each day of violation shall constitute a separate violation. The penalties provided in this subsection shall be recoverable by a civil suit filed by the attorney general in the name and on behalf of the commission or the division...

NMSA 1978, § 70-2-31(A). This provision gives the Division and the Commission authority to assess penalties administratively, and recover penalties through a civil lawsuit. The recovery provision is necessary because the Division and Commission do not have the power to collect a penalty assessment from an uncooperative operator except by obtaining a district court order. The proposed rule recognizes that the Division may seek administrative penalties in a compliance proceeding.

c) Corrective action. The Division may seek corrective action, including abatement or remediation (see 19.15.1.19 NMAC and 19.15.3.116 NMAC) in order to carry out its statutory duty to protect human health and the environment. The Division may also seek corrective action designed to bring a non-compliant operator back into compliance. For example, the Division may seek an order requiring an operator to fix a leaking tank to comply with 19.15.1.13.B NMAC, or reconfigure an unlined vent/flare pit to comply with 19.15.2.50.C(2)(b)(i) NMAC.

d) Well plugging. The Division has specific statutory authority to use well plugging as a sanction:

> If any of the requirements of the Oil and Gas Act or the rules promulgated pursuant to that act have not been complied with, the oil conservation division, after notice and hearing, may order any well plugged and abandoned by the operator or surety or both in accordance with division rules. If the order is not complied with in the time period set out in the order, the financial assurance shall be forfeited.

NMSA 1978, § 70-2-14(B). The Division may also require well plugging as a remedy for violations of 19.15.4.201 NMAC, the inactive well rule. See 19.15.3.101.M NMAC.

e) Denial, cancellation or suspension of a permit.
f) Denial, cancellation or suspension of authorization to transport.
g) Shutting in a well or wells.

The Division grants certain privileges to operators. In a compliance proceeding, the Division may seek an order suspending or revoking privileges previously granted. See Cerrillos Gravel Products, Inc. v. Board of County Commissioners, 2005-NMSC-023 ¶16, "We agree that the power to revoke a permit is necessarily implied from the power to approve a permit.")

**Paragraph C** sets out the requirements for a compliance proceeding application. Those requirements are designed to give the alleged violator sufficient notice of the charges.

The Division's application must identify the entity against whom compliance is sought; specify the alleged violations; provide a general description of the facts supporting the alleged violations; and state the remedy or remedies sought. Note that the rule requires the application to identify the surety, as well as the operator or other responsible parties, if the Division seeks an order allowing forfeiture of a surety bond. The statutes contemplate that the surety will be given the opportunity to plug the well in order to avoid forfeiture. See NMSA 1978, § 70-2-14(B). If the financial assurance is in the form of a cash bond or a letter of credit, the financial institution is simply holding funds for the benefit of the state, and identification of the financial institution in the compliance proceeding is not necessary.

**Paragraph D** sets out the notice requirements for compliance proceedings, specifically adopting the publication requirements of 19.15.14.1207 NMAC and the notice provisions of 19.15.14.1210 NMAC. There is one difference: when notifying an operator required to provide the Division with a current address pursuant to proposed rule 19.15.3.100 NMAC, it is sufficient for the Division to send notice by first class mail to the most recent address provided by the operator. Providing notice by mail to an address the operator is required to provide satisfies due process because it is reasonably calculated, under the circumstances, to apprise the interested parties of the action. See Morris v. State, 894 S.W.2d 22, 25 (Tex. App. –Austin 1994)(writ dism'd w.o.j.).

**Paragraph E** recognizes the validity of agreed compliance orders entered into by the division director and the entity whose compliance is sought. Such orders may be entered whether or not the Division has filed an application for a compliance proceeding. If the division director and the entity against whom compliance is sought enter into an agreed compliance order after an application is filed, the order may resolve all or some of the allegations raised in the application.

**Paragraph F** clarifies that the rule applies only to administrative compliance cases; nothing in the rule precludes the Division from bringing enforcement-related actions in district court, as permitted by the Act.

## 2. 19.15.1.7.K KNOWINGLY AND WILLFULLY

NMSA 1978, § 70-2-31(A) authorizes the imposition of civil penalties against any person who "knowingly and willfully" violates the Act or any rule or order issued pursuant to the Act. A person who "knowingly and willfully" commits the same violation may also be convicted of a felony under NMSA 1978, § 70-2-31(B). According to law dictionaries and case law, the definition of the terms "knowingly" and "willfully" often depends on the context, and they can carry a different meaning depending on whether they appear in a civil or criminal statute. See, for example, Ballentine's Law Dictionary (1969), "willful;" and discussion in Screws v. United States, 325 U.S. 91, 101 (1945); United States v. Weintraub, 273 F.2d 139 (2nd Cir. 2001). The Division currently has no definition of "knowingly and willfully."

The Division proposes to adopt a definition of "knowingly and willfully" appropriate for a statute imposing civil penalties. The proposed definition is based on the definition applied by the Bureau of Land Management in matters involving the use, occupancy and development of oil and gas on public lands through leases, permits and easements. See 43 C.F.R. § 2920.0-5(m) (10-1-03 Edition).

### 3. [New] 19.15.1.38 ENFORCEABILITY OF PERMITS AND ADMINISTRATIVE ORDERS

As discussed above, a violation of the Act or any rule or order issued pursuant to the Act may result in the imposition of penalties. The Act requires public hearings before the entry of an order, except for emergency orders that expire after 15 days. See NMSA 1978, § 70-2-23. Not all directives from the Division take the form of a rule or an order issued after notice and hearing. Permits, administrative orders, approvals of abatement plans and remediation plans, for example, may be issued administratively, without hearing. Currently, the Division can only enforce these directives only by reference to a violation of another order or a rule. For example, Operator A operates an injection well pursuant to a permit that limits injection pressure to a certain level. Operator A exceeds his permitted injection pressure. To impose a penalty, the division must identify a violation of the Act, a rule or an order. If the permit was issued by order after notice and hearing, a violation of that order may subject the operator to a penalty. But if the permit was approved administratively, the Division may only impose a penalty after proving a violation of the Act, an order or a rule. The Division would have to argue that the operator was in violation of 19.15.9.701(A) NMAC, which requires a permit for injection, because the operator was acting outside the scope of his permit. The proposed rule would clarify that violation of the Division's written directive is itself a violation.

## II. "GOOD STANDING" AND OTHER ENFORCEMENT TOOLS

The concept of "good standing" is the cornerstone of a new enforcement program that will allow the Division to deny privileges to well operators who are in serious violation of Division rules. The Division proposes a new rule that defines what it means to be in "good standing," and to amend existing rules to require that an operator be in "good standing" before the Division will register an operator; approve a change of operator; issue a permit to drill, deepen or plug back; assign an allowable; or issue an injection permit.

Other states have adopted similar provisions. Texas and Arizona require operators to have a "certificate of compliance" in order to produce or connect with a pipeline or carrier. See Tex. Res. Code Ann. Tit. 3, §§ 85.161, 85.162, and 85.164. Ariz. Rev. Stat. § 27-509. Illinois requires a permit to drill or operate. See 62 Ill. Adm. Code 240.1400(a) and (b); 62 Ill. Adm. Code 240.1460; 62 Ill. Adm. Code 240.1470.

Note that the proposed "good standing" concept applies only to well operators. That is because the privileges that can be taken away if the operator is not in good standing are privileges that apply only to well operators. Enforcement against transporters and waste

facility operators should be addressed through denial, suspension or revocation of their permits.

## 4. [New] 19.15.14.37 GOOD STANDING

**Paragraph A** defines "good standing" in terms of specific issues:

**A(1)** requires the operator to be in compliance with the financial assurance requirements of 19.15.3.101 NMAC [Rule 101]. This is consistent with current rules: a well operator must have the appropriate financial assurance in place in order to operate in New Mexico. Note that, as discussed below, the Division proposes to amend Rule 101 to make the financial assurance requirements more stringent.

**A(2)** states that the operator must not be subject to an order, issued after notice and hearing, finding the operator to be in violation of an order requiring corrective action. Note the protections in place for the operator. First, the operator must already be subject to an order requiring corrective action. Examples of corrective action include completion of abatement or remediation, or action required to come into compliance with a Division rule. If the operator fails to comply with the order requiring corrective action, the Division must conduct a hearing and obtain an order finding the operator to be in violation of the order requiring corrective action. This gives the operator the opportunity to present testimony and argument on the issue of whether the operator is in fact in violation of the existing order. Only when a second order is issued is the operator's "good standing" affected, and then only if a stay is not issued on the order.

Although this provision appears to be of limited reach, it will be useful to the Division. For example, an order is issued requiring ABC Company to complete an abatement plan. ABC Company fails to comply. The Division, after notice and hearing, issues an order finding ABC Company to be in violation of the order requiring corrective action. ABC Company leaves the state, making it difficult, if not impossible, to obtain compliance. But because ABC Company is no longer in "good standing," under proposed rule 19.15.3.100 NMAC (the operator registration rule) it will not be able come back to New Mexico and acquire new wells. In addition, the officers, directors and partners of ABC Company will not be allowed to operate wells in New Mexico under a new company.

**A(3)** states that the operator must not have a penalty assessment unpaid more than 70 days after issuance of the order assessing the penalty. If an operator wants to contest an order assessing a penalty, the seventy days will allow him time to file an appeal and obtain a stay of the order assessing the penalty. The unpaid penalty assessment will not affect the operator's good standing during that 70-day waiting period, and will not affect his good standing if a stay is entered.

**A(4)** states that the operator has no more than a certain number of wells out of compliance with 19.15.4.201 NMAC [Rule 201]. That rule requires the plugging and abandonment of any well that has been inactive for a continuous period of one year plus 90 days, and is not on approved temporary abandonment status. Note that wells in

violation of Rule 201 that are subject to an agreed compliance order under which the operator agrees to bring the wells into compliance under an approved schedule enforced with penalties will not be regarded as out of compliance with Rule 201 when determining whether an operator is in "good standing." Wells subject to an order issued after notice and hearing will still affect an operator's "good standing." The Division will recognize and reward the operator's commitment to comply through an agreed compliance order, but if the operator is ordered to comply after notice and hearing, those wells will be taken off the list only when the operator actually brings those wells into compliance.

The Division proposes that an operator with more that 2 wells out of compliance is not in "good standing" if the operator operates fewer than 100 wells; and an operator with more than 5 wells out of compliance is not in "good standing" if the operator operates 100 wells or more. Note that this does not mean that an operator is allowed to have 2 or 5 wells out of compliance. It just means that the "good standing" concept will not apply, and the Division will need to use traditional enforcement methods to obtain compliance.

**Paragraph B** requires that the Division post on its website a list of operators who are not in compliance with the financial assurance requirements of Rule 101, and update the list weekly. Note that the Division's proposed changes to Rule 101 will broaden financial assurance requirements and increase the amounts of one-well financial assurances. As discussed below, those changes will be phased in, and until January 1, 2008 the proposed changes will only affect newly drilled or newly acquired wells.

**Paragraph C** requires the Division to post on its website a list of operators who are not in compliance with an order finding them to be in violation of an order requiring corrective action. The list will be updated as such orders are issued.

Paragraph C also provides that an order that is stayed pending appeal does not affect an operator's good standing. And the rule describes how an operator who is subject to an order affecting his good standing may restore his good standing: the operator may file a motion with the order's issuer (either the Division or the Commission) to have the order declared satisfied. The issuer may grant the motion administratively, or set the matter for hearing. It will be up to the issuer of the order to determine if the order has been satisfied.

**Paragraph D** requires the Division to post on its website a list of operators who have a penalty assessment unpaid more than 70 days after issuance of the order assessing the penalty. The list will be updated as needed. Again, an operator who contests the order may appeal and seek a stay of the order. An order that is stayed pending appeal does not affect an operator's good standing.

**Paragraph E** requires the Division to post on its website, and update daily, a list of non-compliant inactive wells, by operator. As Paragraph E(2) explains, the listing of a well creates a rebutable presumption that the well is out of compliance with Rule 201. And, as explained below, the list will tie to the Division's electronic permitting system, allowing the Division to refuse permits to operators who exceed the 2 or 5 well limit. Paragraph

E's list will not include all wells out of compliance with Rule 201. The list will be under-inclusive in two respects:

First, the list will not include a well if the wellbore is plugged but the site has not been cleaned in accordance with the requirements of 19.15.4.202 NMAC [Rule 202]. Once the wellbore is plugged, the rule allows the operator one year to clean the wellsite. So an operator may be out of compliance until he plugs the wellbore, and then in compliance for a year until the deadline for cleaning the site expires. The Department's computer database currently tracks the plugging of the wellbore, but does not track the expiration of the one year period for cleaning the wellsite. Therefore the list will exclude a well if the wellbore is plugged, even if the well is out of compliance because more than a year has passed and the wellsite has not been cleaned. This compliance issue will be handled by traditional enforcement methods.

Second, the list also excludes wells that are subject to an agreed compliance order under which the operator has agreed to a schedule for bringing the wells into compliance and penalties if the operator meets that schedule.

## 5. 19.15.3.102 NOTICE OF INTENTION TO DRILL

The substantive change the division proposes to Rule 102 is the addition of a "good standing" requirement: the Division may not approve a permit to drill, deepen or plug back if the applicant is not in good standing pursuant to Rule 37. Note that the rule is written with "may," rather than "shall," giving the Division some discretion in the use of this enforcement tool.

In practice, most operators apply for permits electronically. If the operator is out of good standing based on the lists kept by the Division, the computer will notify the operator that his permit cannot be approved electronically, and he will need to contact his district office. Depending on the circumstances, the district office may choose to issue the permit, but warn the operator that he must regain "good standing" prior to receiving authority to produce and transport from the well. If the operator is out of compliance due to an unacceptable number of inactive wells, the district office may propose an agreed compliance order setting a schedule for bringing the wells into compliance and providing for penalties if the schedule is not met. If the operator and the Division enter into such an agreed compliance order, the wells covered by the order will be removed from the list, and the operator will regain his "good standing."

If the division's lists show that an operator is not in "good standing," the operator may be able to provide evidence that he is in "good standing," and obtain the permit. For example, if the Division's list shows that the operator has an unpaid penalty, and the operator produces a cancelled check showing payment, the Division will remove the operator's name from the list. If the operator believes he is in "good standing," but the Division does not agree, the operator may challenge his listing, or the denial of the permit, through the hearing process.

The Division also proposes a number of style and organizational changes to Rule 102. It proposes changing the title of Rule 102 to match the title of its companion rule, 19.15.13.1101 NMAC [Rule 1101], and the title of the form used to apply for permits. The title change also changes the emphasis from the operator's intention to the need for the operator to obtain a permit.

**Paragraph A** sets out the heart of the rule: the need for a permit, and the activities for which a permit is required. The current rule does not identify the need for a permit for activities other than drilling; those requirements are found in the companion Rule 1101 and the form.

**Paragraph B** describes the application process and the requirements the applicant must meet. Subparagraph B(3) recognizes that an operator seeking a permit to operate a well in a spacing or proration unit containing an existing well or wells operated by another operator must comply with 19.15.3.104.E(2) NMAC [Rule 104.E(2)], which was recently adopted by the Commission. The proposed rule keeps the existing requirement regarding notification to other operator in the same quarter-quarter section, because it is possible that Rule 104.E(2) will not apply to all operators in that circumstance.

**Paragraph C** imposes the "good standing" requirement.

**Paragraph D** recognizes that the Division may impose conditions on a permit to drill, deepen or plug back. Imposing such conditions is the current practice.

**Paragraph E** states the existing requirement that operators keep a copy of the approved form C-101 at the well site during drilling operations.

## 6. 19.15.13.1101 APPLICATION FOR PERMIT TO DRILL, DEEPEN OR PLUG BACK (Form C-101)

The 1100 series of the Division's rules describes the requirements of the forms used by the Division. Rule 1101 is the companion rule to Rule 102, and sets out the requirements for the form C-101 that is used to obtain a permit to drill, deepen or plug back.

The proposed changes to Rule 1101 reorganize the information in the existing rule, but make no substantive changes other than to remove the requirement for filing multiple copies of the application.

## 7. 19.15.9.701 INJECTION OF FLUIDS INTO RESERVOIRS

**Paragraph A** contains the most significant substantive change. The proposed rule will prohibit the Division from granting a permit for injection to an operator who is not in "good standing." The operator may challenge a denial through the hearing process. The proposed rule will also allow the Division to revoke an existing permit after notice and hearing if the operator is not in "good standing."

**Paragraph B(2)** expands the notice requirements for injection well applications, requiring the applicant to notify other "affected persons" within one-half mile of the well, in addition to each leasehold operator. "Affected persons" is defined by reference to 19.15.14.1210.A(2)(a) NMAC, a proposed rule currently before the Commission for approval.

## 8. 19.15.13.1104 REQUEST FOR ALLOWABLE AND AUTHORIZATION TO TRANSPORT OIL AND NATURAL GAS (Form C-104).

The substantive change to Rule 1104 is the addition of a "good standing" requirement: the Division may assign an allowable or issue an authorization to transport only if the operator is in "good standing." The operator may challenge a denial through the hearing process. Note that the proposed rule specifically mentions authorization to transport. As currently written, authorization to transport is mentioned in the title of the rule but not in the body of the rule.

The remaining changes to Rule 1104 are organizational. Paragraph A consolidates the requirements for obtaining an allowable or authorization to transport. Paragraph B describes the effective date for an allowable. References to filing multiple hard copies of the application are deleted because the applications are now made electronically.

## 9. [New] 19.15.3.100 OPERATOR REGISTRATION; CHANGE OF OPERATOR; CHANGE OF NAME

**General:** This new rule puts the requirements for registration, change of operator and change of name in one rule. Most of the provisions in the rule reflect current Division practice, but do not appear in any existing rules. The current rules only address change of operator, and that is a short discussion in the procedural rule for sundry notices. See 19.15.13.1103.J NMAC, which the Division proposes to delete. The proposed rule allows the Division to deny registration, or deny a change of operator, if the operator is not in "good standing."

**Paragraph A** requires every operator of a well or wells in New Mexico to register with the Division, and explains the registration process. The requirements reflect current practice: an OGRID number, a current address, registration with the Public Regulation Commission (if the applicant is a corporation), and registration with the Secretary of State (if the applicant is a partnership).

**Paragraph B** allows the Division to deny registration to an operator who is not in good standing. The Division may also deny registration if an officer, director or partner in the applicant, ~~or person with an interest in the applicant exceeding 5%, was an~~ officer, director, partner or person with an interest exceeding 5% in <u>another</u> entity that is not in good standing. And the Division may deny registration if the applicant itself is an officer, director, partner, or person with an interest exceeding 5% in another entity that is not in good standing. These provisions are modeled after Illinois' rules (Ill. Adm. Code 240.250) and are designed to prevent entities from avoiding the good standing

requirement by changing their name or forming a new entity. Example: "Well Operator, Inc." operates wells in New Mexico. "Well Operator, Inc." is found to be in violation of an order requiring remediation, and has $10,000 in unpaid penalty assessments. The officers of "Well Operator, Inc." decide to cease operations under that corporation, but form a new corporation, "Superior Well Operator, Inc." The Division may refuse to recognize "Superior Well Operator, Inc." as an operator in New Mexico.

**Paragraph C** requires operators to keep the Division informed of their current address. As discussed above, proposed Rule 1227 will allow the Division to use the most current address provided by the operator when giving the operator notice of compliance actions.

**Paragraph D** provides that the Division may require an operator or an applicant to identify its current and past officers, directors and partners, and its current and past ownership interest in other operators, so the Division will have the information necessary to determine whether to deny registration to an operator pursuant to Paragraph B.

**Paragraph E** describes what constitutes a change of operator, and explains that when an operator change occurs, the wells are moved from the prior operator's OGRID number to the new operator's OGRID number. Paragraph E also describes the new joint application process through the division's web-based online application, and provides an alternate process if the previous operator is not available.

Paragraph E also contains two significant substantive changes. The Division may deny a change of operator if the new operator is not in good standing. (The prior operator's lack of good standing will not affect the transfer because the Division wishes to encourage good operators to take over operations from bad operators.) If the new operator is acquiring wells, facilities or sites subject to a compliance order requiring remediation or abatement, or compliance with Rule 201 (the inactive well rule) the Division may require the new operator to enter into an agreed compliance order setting out a schedule for compliance with the existing order before the division will approve the change.

**Paragraph F(1)** describes what constitutes a change of name, and explains that when a name change occurs, the OGRID number remains the same.

**Paragrah F(2)** sets out the procedure for obtaining a change of name, and specifies that the Division may require documentary proof that the change is a name change and not a change of operator. This puts operators on notice of the Division's current practice.

**Paragraph G** provides examples of change of operator, and change of name, to address some of the questions commonly asked by operators. The examples reflect the Division's current practice. Note that the examples also reflect the guideline available on the division's website, with one change. In subparagraphs G(3) and G(4) the Division clarifies its practice regarding mergers. A merger of a New Mexico operator and an operator who does not operate in New Mexico is treated as a change of name: the wells will remain under the existing New Mexico OGRID. If two New Mexico operators merge, both will have OGRIDS. Either one OGRID will survive the merger, or the

merged corporation will obtain a new OGRID. Wells transferred to the surviving or new OGRID will be transferred as a change of operator.

## 10. 15.13.1115 OPERATOR'S MONTHLY REPORT (Form C-115)

**Paragraph A** contains two clarification changes. The current rule requires a monthly report "on each producing lease and secondary or other enhanced recovery project or pressure maintenance project injection well." The proposed rule substitutes "each non-plugged well completion for which the division has approved a C-104 authorization to transport" for "each producing lease" to clarify that the reports are to be filed on a single well completion basis, and that only non-plugged wells holding approved C-104s are required to report. A well completion represents each well/pool combination approved on a C-105. One well can have multiple completions. The proposed rule also adds "or other injection well" to clarify that operators must file monthly reports for all injection wells, and not just for pressure maintenance project injection wells. Because the proposed rule clarifies that reports for all injection wells are filed on a form C-115, the proposed rule eliminates the need for filing a C-115 EDP. If the Commission adopts this change, the Division will propose eliminating references in other rules to the C-120-A, which previously was used for reporting salt water disposal.

**Paragraph B** instructs operators to file using the Division's web-based online application, and provides a procedure for obtaining an exemption from that requirement.

**Paragraph B(3)** changes the procedure for enforcing the monthly report requirements. Currently, the rule requires that the Division notify the operator of any deficiency within 30 days of the appropriate filing date. If the operator does not respond within 30 days, with a schedule to file the report and fix the error, the Division must notify the operator that he has failed to comply with the rule and may be subject to loss of authority to produce. If the operator "willfully" fails to respond to this second notice, the Division may notify the operator that authority to produce or inject will be cancelled in 30 days. If the operator does not respond to this third notice by requesting a hearing, the Division may then cancel the authorization.

The proposed rule streamlines the process. The Division must notify the operator within 60 days if an acceptable report has not been received, and put the operator on notice that if the operator does not file an acceptable report or request a hearing within 120 days of the original due date, the Division may cancel the operator's authority to transport or inject. Note that when the operator files electronically, he presses a "validate" button for his web submission of the C-115. The computer will alert the operator to all the errors that must be corrected, and that he should not submit the C-115 until all errors are resolved. ~~Therefore, the~~ operator knows immediately whether the ~~C-115 has been~~ accepted. If the operator nevertheless submits the report with errors, it will be rejected.

Please note an error in the proposed rule. The proposed rule eliminates subparagraphs B(1) and B(2) but leaves B(3) intact. The Division suggests that the Commission make

B(3) a separate paragraph C. If that is done, paragraph B will address the filing of reports, and paragraph C will address enforcement actions.

## 11. 19.15.3.101 PLUGGING BONDS

The Act contemplates that operators are responsible for plugging their wells, and that the reclamation fund will be used only as a last resort. To that end, the Act requires all operators to post a $50,000 blanket financial assurance or one-well bonds in amounts sufficient to pay the cost of plugging. As wells reach the end of their productive lives, it becomes increasingly likely that the well will need to be plugged. The Act contemplates that after a well has been inactive for more than two years it should be covered by one-well financial assurances, so the state's costs will be covered if the state has to plug the well. If the state has to plug the well, it must forfeit the financial assurance and seek restitution from the operator for any costs not covered by the financial assurance. See NMSA 1978, §§ 70-2-14 and 70-2-38.

To better carry out this legislative scheme, the Division proposes three significant substantive changes to Rule 101:

1. The amended rule will require financial assurances on all oil, gas or service wells in New Mexico. The current rule requires financial assurances only for wells on privately-owned or state-owned lands.
2. The amended rule will require wells on temporary abandonment status for more than two years to be covered by a single-well financial assurance.
3. The amended rule increases the amount of one-well financial assurances to match the actual costs of well plugging by the state.

The Division proposes changing the title of the rule from "Plugging Bonds" to "Financial Assurances for Well Plugging" to reflect the fact that New Mexico recognizes letters of credit, as well as cash and surety bonds.

The Division proposes reorganizing the rule to make it easier to read and reduce confusion.

**New Paragraph A** outlines New Mexico's financial assurance requirements. The Act requires "Each person, firm, corporation or association who operates <u>any</u> oil, gas or service well within the state shall, as a condition precedent to drilling or producing the well, furnish financial assurance...." NMSA 1978, § 70-2-14(A)(emphasis added). The current rule exempts wells on federal or Indian land: "Any person, firm, corporation, or association who has drilled or acquired, is drilling, or proposes to drill or acquire any oil, <u>gas, or service well on privately owned or state owned lands within this</u> state" shall provide a financial assurance. Rule 101(A) (emphasis added). The Division proposes to delete "on privately owned or state owned lands," so that the financial assurance requirements apply to any oil, gas or service well in the state, as the legislature intended.

Currently, if an operator operates only wells on federal or tribal land, he does not need to post a financial assurance with the Division. If the proposed rule is adopted, that operator will need to post a financial assurance running to the benefit of the State.

Currently, an operator who operates wells on federal or tribal land and on state or fee land must post a financial assurance to cover the wells on state or fee land. The forms available on the Division's web site for blanket cash and surety bonds limit the coverage of those bonds to wells on "privately owned or state owned lands." If the proposed rule is adopted, an operator who posted a blanket cash or surety bond will need to replace that bond, or provide a rider to that bond, so that it covers all of the operator's wells. Alternatively, the operator could provide separate blanket or single-well financial assurances to cover the wells on federal or tribal land.

Some of the letters of credit currently on file with the Division do not limit coverage to wells on state or fee land. If the proposed rule is adopted, an operator who has posted a letter of credit that does not limit coverage will not need to change that financial assurance. Note that some older letters of credit may contain limiting language, and those will need to be replaced.

If the proposed rule is adopted, the Division will change the language in its forms for cash and surety bonds to reflect the extended coverage.

The proposed changes also clarify that the phrase "service well" includes injection wells.

The proposed changes also recognize letters of credit, which were added to NMSA 1978, § 70-2-14 by amendment in 2000. See Laws 2000, ch. 12, § 1.

**New Paragraph B** distinguishes between a one-well financial assurance and a blanket financial assurance. The rule provides that any well that has been in temporary abandonment status for more than two years must be covered by a one-well financial assurance, but provides an exception for wells that are shut in because of lack of pipeline connection. The rule provides that the Division may release the one-well financial assurance after the well is returned to production if the well is also covered by a blanket financial assurance. The authority for requiring one-well financial assurances for inactive wells is found at NMSA 1978, § 70-2-14(A) ("In addition to the blanket plugging financial assurance, the oil conservation division may require a one-well financial assurance on any well that has been held in a temporarily abandoned status for more than two years.")

**New Paragraph C** sets out the financial assurance amounts. The amount of a blanket financial assurance is set by statute at $50,000, and is unchanged. See NMSA 1978, § 70-2-14(A). The statute directs the Division provide for a one-well plugging financial assurance

> in amounts determined sufficient to reasonably pay the cost of plugging the wells covered by the financial assurance. In establishing categories of

financial assurance, the oil conservation division shall consider the depth of the well involved, the length of time since the well was produced, the cost of plugging similar wells and such other factors as the oil conservation division seems relevant.

NMSA 1978, § 70-2-14(A). Rule 101 currently distinguishes between wells in actively producing counties (Chaves, Eddy, Lea, McKinley, Rio Arriba, Roosevelt, Sandoval, and San Juan), and all other counties in the state. The Division proposes to keep that distinction, but raise the amounts for the two areas. Single-well financial assurances in the actively producing counties in the state are currently set at $5,000, $7,500 and $10,000, depending on the depth of the well. The division proposes to change the amount to $5000 plus $1 per foot projected depth of the proposed well or measured depth of existing well. Single well financial assurances in other counties are currently set at $7,500, $10,000 and $12,500, depending on the depth of the well. The Division proposes to change the amount to $10,000 plus $1 per foot.

**New Paragraph D** consolidates in one paragraph the general requirements for financial assurances. The requirement in subparagraph (1) and (2) are taken from the current rule. The requirement in subparagraph (3) is also taken from the current rule, with one change. The current rule provides, at paragraph L, that bonds are not to secure payment for damages to livestock, range, water, crops, tangible improvements, nor any other purpose." The proposed rule eliminates the word "water." The Division recognizes that financial assurances are not to secure payment to damages incurred by surface owners. But water is the property of the state, not the surface owner. And if a well damages water, the financial security may secure payment for that damage. The requirement in paragraph (4) that the Division may require proof that the individual signing for an entity on a financial assurance document or an amendment to a financial assurance document has the authority to obligate that entity is designed to prevent fraud, and is consistent with the Division's current practice.

**New Paragraph E** sets out additional requirements specific to surety bonds and cash bonds. These requirements exist in the current rule.

**New Paragraph F** sets out additional requirements for letters of credit. The existing rule does not address letters of credit. The new rule reflects existing Division practice of accepting letters of credit issued by national or state-chartered banking associations, and allowing the Division to forfeit and collect a letter of credit if not replaced by an approved financial assurance at least 30 days before the expiration date. Current practice is to allow letters of credit for terms of one year or more. The new rule will require terms of 5 years or more, unless the applicant shows good cause for a shorter time period. The five year requirement is consistent with the term applied to letters of credit for surface waste management facilities in 19.15.9.711.B(4)(b) NMAC. This longer term provides for ease of administration, as the Division will no longer have to notify operators of impending forfeiture every year and file forfeiture documents to protect the state.

**New Paragraph G** governs the release of a financial assurance, and reflects provisions in the current rule. Note one important change: Current paragraph J provides that "Upon approval of the bond and the Form C 103 or 104, the tranferror is released of plugging responsibility for the well..." The Division takes the position that a transfer should not absolve an operator from all responsibility for plugging the well, if the subsequent operator fails to plug the well. In an appropriate case the Division may seek corrective action or reimbursement from a prior operator. For example, Operator A pays Operator B to take over 50 wells that have cease production. Operator B has acquired 100 other non-productive wells under similar circumstances. All 150 of Operator B's wells are covered under a single $50,000 blanket bond, and the Division cannot require additional bonding from Operator B because none of his wells has been inactive for two years or more. Operator B leaves the state and cannot be located. Under the current rule, when the wells have been inactive for the prescribed period, the Division may pursue a plugging action against Operator B but cannot pursue any action against Operator A, or any of the other operators who profited from their wells before turning them over to Operator B to avoid plugging responsibility. Eliminating the language in the current rule that "the transferor is released of plugging responsibility" gives the Division the opportunity to argue that under these circumstances, Operator A should be held responsible for plugging the 50 wells he turned over to Operator B.

**New Paragraph H** governs forfeiture of the financial assurance, and reflects provisions in the current rule. The proposed rule addresses how to handle situations in which the financial assurance either exceeds or is insufficient to cover the state's plugging costs. If proceeds exceed costs, the excess shall be returned to the operator or surety, as applicable. If the proceeds are less than the cost, the Division shall seek indemnification from the operator.

**New Paragraph I** sets out effective dates for the rule. The rule is effective immediately as to wells drilled or acquired after its effective date. But as to all other wells, the rule will be effective January 1, 2008. This will give operators of existing wells time to obtain financial assurances for wells on federal or tribal land. It will also give operators two years to decide what to do with their inactive wells. By plugging and abandoning those wells, or by returning those wells to production, operators can avoid having to post the one-well financial assurances that will be required under this rule.

## 12. 19.15.1.7 DEFINITIONS "TEMPORARY ABANDONMENT"

As discussed above, the Act provides that the Division may require a one-well financial assurance on any well "that has been held in a temporarily abandoned status" for more than two years. See NMSA 1978, § 70-2-14(A). The Division's current definition of temporary abandonment refers to a well that has been approved for temporary abandonment in accordance with Division rules. This definition leads to an anomaly that cannot have been intended by the legislature: the Division may require a one-well financial assurance on a well that is in compliance with Division temporary abandonment rules, but may not require a one-well financial assurance on an inactive well that is not in compliance with Division temporary abandonment rules. The Division proposes to

correct this anomaly by changing the definition of "temporary abandonment" to be the status of a well that is inactive.

## 13. 19.15.1.7 DEFINITIONS "APPROVED TEMPORARY ABANDONMENT"

The Division also proposes to add a new definition: approved temporary abandonment. This will refer to a well that is inactive and is in compliance with the Division's "approved temporary abandonment" rule.

## 14. 19.15.4.203 TEMPORARY ABANDONMENT

The Division proposes to amend the existing rule on temporary abandonment to reflect the new terminology of "approved temporary abandonment." In addition, the Division proposes the following substantive changes:

**Paragraph C(1)** revises the approved methods of demonstrating mechanical integrity. Subparagraphs (a) and (b) are clarified to require that wells be pressure tested to 500 pound per square inch surface pressure. Current subparagraph (c), which exempted certain wells from the requirement for a bridge plug or packer, is eliminated. Current subparagraph (d), which allowed operators to demonstrate mechanical integrity through submission of a casing log, is eliminated. New subparagraph (c) provides that an operator may demonstrate mechanical integrity by proof that the well has been completed for less than 5 years and has not been connected to a pipeline.

**Paragraph C(2) (3) and (4)** set out specific requirements for mechanical integrity tests and logs. Subparagraph (2) has not been substantively changed. Subparagraph (3) sets out new requirements for recording mechanical integrity tests: a chart recorder with a maximum two hour clock and maximum 1000 pound spring, calibrated within six months prior to the test, witnesses to the test sign the chart. Subparagraph (4) allows the Division to approve other casing tests if the operator demonstrates that the test will satisfy the requirements of Paragraph B(2).

## 15. 19.15.4.201 WELLS TO BE PROPERLY ABANDONED

The Division proposes to amend Rule 201 to reflect the new terminology of "approved temporary abandonment," and to amend Paragraph A to clarify that service wells include injection wells.

## 16. 19.15.13.1103 SUNDRY NOTICES AND REPORTS ON WELLS (Form C-103)

The Division proposes to amend Rule 103 to reflect the new terminology of "approved temporary abandonment," to delete references to filing multiple hard copies of forms that are now filed electronically, and to delete paragraph I regarding change of operators because that issue is now covered in proposed Rule 100.

## CONCLUSION

The Division respectfully requests that the Commission adopt the proposed rules at the conclusion of the hearing scheduled for October 13 and 14, 2005.

RESPECTFULLY SUBMITTED,

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