

PROGRESS REPORT: STATE EFFORTS TO ADDRESS ORPHANED OIL AND GAS WELLS

**OFFICE OF CONSERVATION –
DEPARTMENT OF ENERGY AND NATURAL
RESOURCES**

PERFORMANCE AUDIT SERVICES

October 24, 2024

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October 24, 2024

The Honorable J. Cameron Henry, Jr.
President of the Senate
The Honorable Phillip R. DeVillier,
Speaker of the House of Representatives

Dear Senator Henry and Representative DeVillier:

This report provides the results of our evaluation of the Office of Conservation's (OC) progress in addressing issues identified in two previous performance audits that focused on the regulation of oil and gas wells and the management of orphaned wells.

We found that while more oil and gas wells are covered by financial security since OC removed most exemptions, the financial security amounts are still not enough to cover the cost of plugging orphaned wells.

We also found that the Oilfield Site Restoration Program (OSR) and the Louisiana Oilfield Restoration Association (LORA) plugged 976 orphaned wells in fiscal years 2020 through 2023. At the same time, the number of orphaned wells continued to grow. Between fiscal years 2020 and 2023, the number of wells plugged rose from 153 to 533. However, the number of orphaned wells decreased 0.9% from January 2020 to October 2023, and then rose 12.4% by April 2024.

In addition, we found that OC is unable to expand the OSR Program to plug more orphaned wells because state law limits the program's ability to collect adequate funding. We estimated that it will take approximately \$542.9 million to address the current population of orphaned wells; however, state law requires that collection of oil and gas production fees be suspended if the OSR fund exceeds \$14 million.

Further, the number of inactive wells, which have a higher risk of being orphaned, increased 21.7% from August 2019 to April 2024. Although OC recently updated regulations to increase the annual inactive well fee based on the time each well has been inactive, it does not place as many restrictions on inactive wells as other states. For example, some states require proof of a well's future utility, higher financial security amounts, or mechanical integrity tests to allow the well to remain inactive past a certain timeframe.

Michael J. "Mike" Waguespack

October 24, 2024

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The report contains our findings, conclusions, and recommendations. I hope it will benefit you in your legislative decision-making process.

We would like to express our appreciation to the Office of Conservation for its assistance during this audit.

Respectfully submitted,



Michael J. "Mike" Waguespack, CPA
Legislative Auditor

MJW/aa

ORPHANWELLS

Louisiana Legislative Auditor

Michael J. "Mike" Waguespack, CPA



Progress Report: State Efforts to Address Orphaned Oil Wells Office of Conservation – Department of Energy and Natural Resources

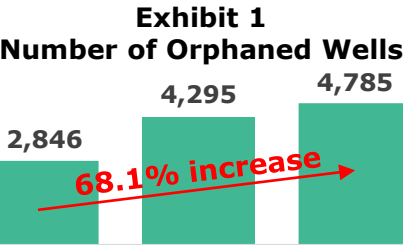
October 2024

Audit Control # 40230018

Introduction

We evaluated the Department of Energy and Natural Resources (DENR) - Office of Conservation's (OC) progress toward addressing issues identified in our May 2014¹ and March 2020² performance audits on OC's regulation of oil and gas wells and management of orphaned wells during fiscal years 2020 through 2023. These audits found that OC did not always effectively manage the current population of orphaned wells, and it faced several challenges in addressing the growing population of

Orphaned wells are abandoned oil and gas wells for which no responsible operator can be located or such operator has failed to maintain the well site in accordance with state regulations. These wells deteriorate over time and become susceptible to releasing oil, gas, and saltwater, which can pose threats to public safety and the environment.



July 2013 Jan. 2020 April 2024

Source: Prepared by legislative auditor's staff using SONRIS data obtained from OC.

orphaned wells. This is one of two reports on how the state is addressing the growing population of orphaned wells. The other report³ focuses on OC's oversight of the Louisiana Oilfield Restoration Association in its efforts to provide affordable financial security and assistance with plugging orphaned wells.

Despite an average of 257 orphaned wells being plugged⁴ per year from fiscal years 2020 through 2023,⁵ the number of orphaned wells has

¹ Louisiana Legislative Auditor (LLA), "[Regulation of Oil and Gas Wells and Management of Orphaned Wells: Office of Conservation – Department of Natural Resources](#)", May 2014.

² LLA, "[Progress Report: Regulation of Oil and Gas Wells and Management of Orphaned Wells: Office of Conservation – Department of Natural Resources](#)", March 2020.

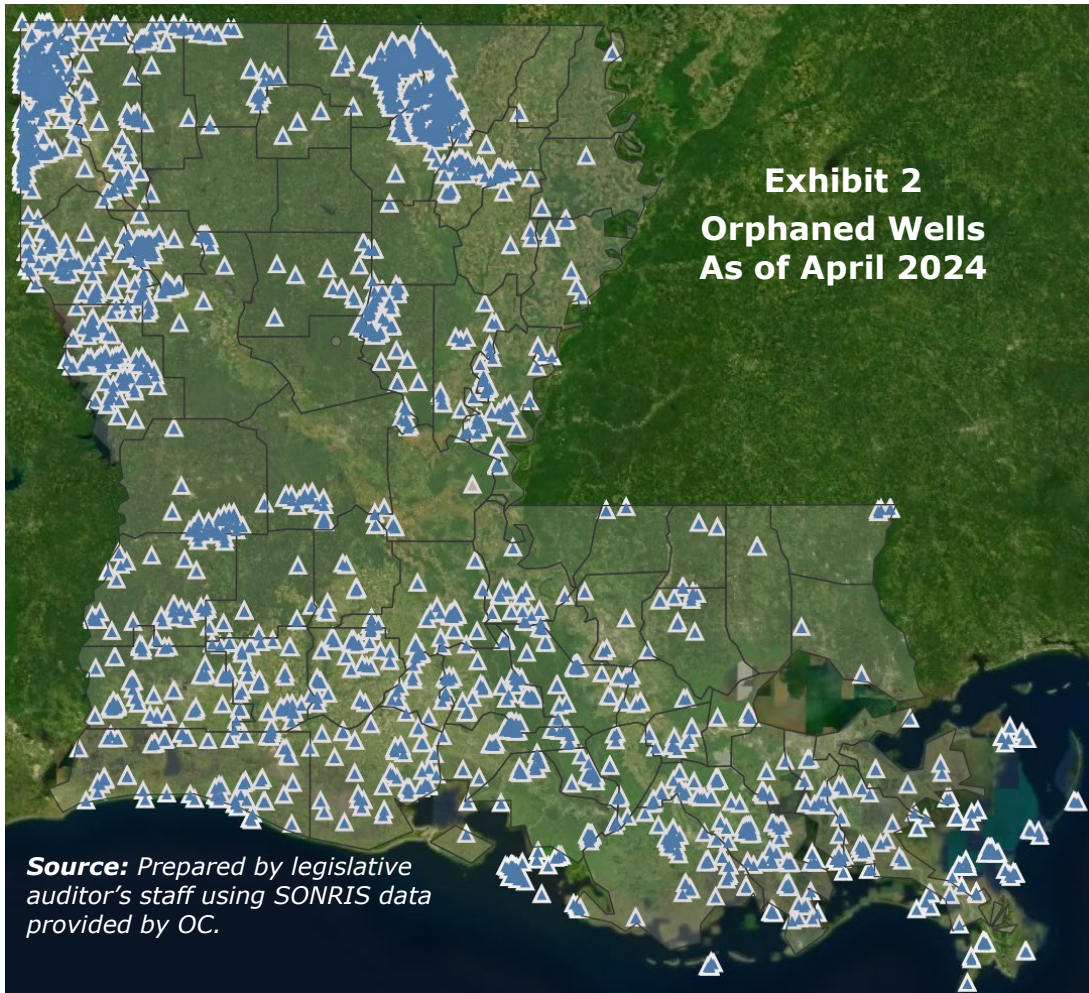
³ LLA, "[Oversight of the Louisiana Oilfield Restoration Association's \(LORA\) Efforts to Address Orphaned Oil and Gas Wells: Office of Conservation – Department of Energy and Natural Resources](#)", October 2024

⁴ As used in this report, "plugging" encompasses all required oilfield site restoration activities, including plugging wells, pit closure, site remediation, and removal of oilfield equipment.

⁵ Includes orphaned wells plugged by OC's Oilfield Site Restoration Program, federal grants, the Louisiana Oilfield Restoration Association, and any other party.

continued to increase. Exhibit 1 shows that the number of orphaned wells increased 68.1% between July 2013 (our first audit) and April 2024.

OC regulates operators and wells through its permitting, monitoring, and enforcement processes to ensure compliance with regulations and identify and address environmental and public safety risks. If operators abandon any of their wells or do not maintain all of their wells in compliance with regulations, OC will orphan all of the operator's wells. Exhibit 2 shows a map of orphaned wells as of April 2024.



OC efforts to address orphaned wells include:

Requiring Financial Security. During our 2014 audit, OC regulations did not require all operators to have financial security; however, OC revised its regulations in May 2015 to remove most exemptions. Financial security is now required for all new permits to drill, amended permits to change operators, and most inactive wells.

Financial security is similar to insurance in that it provides the state with funds to plug secured wells if they are orphaned due to operator abandonment or noncompliance.

Plugging Orphaned Wells. OC’s Oilfield Site Restoration (OSR) Program was created in 1993 to properly plug and abandon orphaned wells and to restore sites to approximate pre-wellsite conditions. OSR bids out plugging projects to oilfield contractors. No funding is used from the state general fund, as OSR generates revenue from fees on oil and gas production paid quarterly by Louisiana oil and gas operators. In fiscal years 2020 through 2023, production fees generated an average of approximately \$11.5 million annually to fund the cost of OSR projects not covered by financial security. In addition, DENR was awarded grant funding of \$25 million through the U.S. Department of the Interior and \$12.7 million through the U.S. Fish and Wildlife Service in August 2022 from the Infrastructure, Investment, and Jobs Act (IIJA) to augment OSR’s efforts to address orphaned wells. As of June 2024, DENR had used \$33.8 million of these funds to plug orphaned wells. OC anticipates receiving \$180 million in additional grant funds over the next five to ten years.

Requiring Inactive Well Fees. Our 2014 audit found that OC allowed operators to place wells in inactive status for extended periods of time to avoid plugging them. However, our 2020 audit found that OC developed processes to better identify and address inactive wells. For example, OC updated regulations in 2015 to require operators to pay an annual fee per inactive well, and updated regulations again in October 2023 to increase this fee based on the amount of time each well has been inactive. In fiscal year 2023, OC received a total of \$2.2 million in inactive well fees, half of which are dedicated by statute to be deposited in the OSR Fund. The remainder is placed in the Oil and Gas Regulatory Dedicated Fund Account, which OC uses for regulation of the oil and gas industry and other industries under its jurisdiction.

Inactive wells are wells that no longer produce oil or gas. They have a higher risk of becoming orphaned.

Collaborating with the Louisiana Oilfield Restoration Association. In November 2019, OC entered into a cooperative endeavor agreement (CEA) with the Louisiana Oilfield Restoration Association (LORA) to provide financial security at a reduced rate in order to help more operators obtain coverage. The CEA also requires LORA to use a portion of annual fees collected to assist with plugging orphaned wells. LORA is not a regulated financial institution. Our second report evaluates OC’s oversight of LORA.

To conduct this audit, we analyzed data from DENR’s Strategic Online Natural Resources Information System (SONRIS), as well as other financial information provided by OC. The objective of this audit was:

To evaluate OC's progress toward addressing orphaned oil and gas wells.

This audit examined OC’s performance during fiscal years 2020 through 2023. Our results are summarized on the next page and discussed in detail throughout the remainder of the report. Appendix A contains DENR’s response, and Appendix B contains our scope and methodology. Appendix C contains a table showing the current amounts of financial security required by OC regulation, and Appendix D shows the number of wells plugged by different entities.

Objective: To evaluate OC's progress toward addressing orphaned oil and gas wells.

Overall, we found the following:

- **Although more oil and gas wells are covered by financial security since OC removed most exemptions, financial security amounts are still not sufficient to cover the actual cost of plugging wells.** Securing more wells with site specific trust accounts (SSTAs) would help ensure that operators pay to plug orphaned wells instead of OSR. Unlike other financial security, SSTAs are based on an estimate of actual costs to plug wells. Although SSTAs can be used to fulfill financial security requirements, they are only allowed when operators sell a well, and only 3.9% of wells had SSTAs as of October 2023.
- **OSR and LORA plugged 976 orphaned wells in fiscal years 2020 through 2023, including 396 wells that were plugged using grants from the federal government. However, despite increased plugging efforts, the number of orphaned wells continues to grow.** The number of orphaned wells plugged per year increased 247.7%, from 153 in fiscal year 2020 to 533 in fiscal year 2023, due to assistance from LORA and federal IIJA funds. However, the number of orphaned wells only decreased 0.9%, from 4,295 in January 2020 to 4,258 as of October 2023, and then rose 12.4% to 4,785 by April 2024.
- **Funding limitations prevent OC from expanding the OSR Program's efforts to plug more orphaned wells, as state law limits OSR's ability to collect adequate funding to address the orphaned oil well population.** We estimated that it will take approximately \$542.9 million to address the current population of orphaned wells; however, state law currently requires that collection of oil and gas production fees be suspended if the OSR Fund exceeds \$14 million. In addition, no changes have been made to the rate of gas production fees since 2004, which accounted for 79.5% of OSR's revenue in fiscal years 2020 through 2023, and more than \$10 million of collected financial security had not been spent as of the end of fiscal year 2023 due to delays caused by factors such as OSR budget priorities.
- **The number of inactive wells, which have a higher risk of being orphaned, increased 21.7%, from 17,775 in August 2019 to 21,629 in April 2024.** Although OC recently updated regulations to increase the annual inactive well fees based on the time each well has been inactive, OC does not place as many restrictions on inactive wells

as some other states. For example, some other states require proof of a wells’ future utility, higher financial security amounts, or mechanical integrity tests for wells to remain inactive past a certain timeframe.

Our findings and recommendations are discussed in more detail in the sections below.

Although more oil and gas wells are covered by financial security since OC removed most exemptions, financial security amounts are still not sufficient to cover the actual cost of plugging wells.

Financial security is similar to insurance in that it provides the state with funds to plug secured wells if they are orphaned due to operator abandonment or noncompliance. If an operator abandons a well, the financial institution⁶ that provided financial security for the well would pay the Office of Conservation (OC) the secured amount to plug the well. Our 2014 audit found that only 14,432 (25.0%) of 57,819 wells in May 2014 had financial security because OC regulations⁷ allowed some operators to be exempt from providing financial security.⁸ However, OC revised its regulations in May 2015 to remove most exemptions. The 2020 audit found that due to these changes, 35,046 (66.3%) of 52,826 wells had financial security in November 2019. In addition, we found that, as of October 2023, 38,007 (74.0%) of 51,332 wells had financial security.⁹

Financial security amounts are still insufficient to cover the actual cost of plugging wells, particularly when wells are covered by blanket security. OC regulations require either individual or blanket financial security (*see box at right*). After our 2014 audit found that the required amounts were insufficient, OC revised its regulations in May

Individual Security: Covers one well and is based on the well depth and location (land, inland waters, or offshore).

Blanket Security: Covers multiple wells owned by a single operator and is based on the number of wells and their location.

⁶ All financial security is provided by regulated financial institutions, such as banks and insurance companies, except for financial security provided by LORA.
⁷ Louisiana Administrative Code (LAC) 43.XIX:104
⁸ During our 2014 audit, OC only required financial security if, in the previous four years, the operator started its first operations, had compliance issues, or was associated with an orphaned well (directly or as an officer).
⁹ Since financial security was not required prior to 2000, only wells permitted on or after July 1, 2000, or transferred to a different operator on or after November 1, 2001, are subject to financial security requirements. Other remaining exemptions include declared orphaned wells that are transferred to a new operator and wells whose operators received an exemption for plugging a similar well in depth and location (i.e., a plugging credit).

2015 to increase some individual¹⁰ and all blanket security amounts. Even with these changes, our 2020 audit found that financial security amounts were still insufficient. Appendix C summarizes the current financial security amounts, which have not been updated since our 2020 audit. Individual security amounts range from \$2 to \$12 per foot based on the well's depth and location, and blanket security policies range from \$50,000 to \$5,000,000 depending on the location and number of wells.

Based on our analysis of OSR plugging costs in calendar years 2022 and 2023, the median actual cost to plug land wells up to 3,000 feet deep was \$8 per foot, and the median cost to plug wells in inland waters was \$38 per foot. However, for individual security, OC regulations only require \$2 per foot and \$8 per foot, respectively. For blanket security, the discrepancies are even larger, as large numbers of wells can be grouped together under one amount. In addition, unlike individual security, blanket security does not account for well depth, which can significantly impact the plugging costs. As of October 2023, 35,818 (95.1%) of the 37,647 wells with financial security¹¹ had blanket financial security, with up to 3,811 wells being covered on the same blanket policy. Although OC regulations state that OC will periodically review and adjust individual and blanket financial security amounts to ensure they are reflective of plugging costs, OC has not established a schedule for performing these reviews.

Securing more wells with site specific trust accounts (SSTAs) would help ensure that operators pay to plug orphaned wells instead of OSR. Unlike other financial security, SSTAs are based on an estimate of actual costs to plug wells. Although SSTAs can be used to fulfill financial security requirements, they are only allowed when operators sell a well, and only 3.9% of wells had SSTAs as of October 2023. State law¹² allows an SSTA to be established when an operator sells a well to another operator to ensure that funds will later be available for plugging the transferred well.¹³ Since state law¹⁴ authorizes DENR to recover costs from prior operators of orphaned wells when OSR plugging costs exceed \$250,000, SSTAs are usually established because the previous operators do not want to be held liable if the wells are abandoned by the operator who last purchased the well. State law requires the amount of funding for an SSTA to be based on a site assessment conducted by an OC-approved contractor who estimates the actual plugging cost, which must be updated if the well is transferred again later.

¹⁰ OC originally increased individual financial security for land wells less than or equal to 3,000 feet from \$1.00 to \$7.00 per foot, but this was reduced to \$2.00 per foot by Act 634 of the 2016 Regular Legislative Session. According to OC, this was because many small operators could not afford the \$7.00 per foot amount and were at risk of orphaning their wells.

¹¹ This excludes wells secured through site-specific trust accounts, as their required amounts are calculated differently than individual and blanket security.

¹² Louisiana Revised Statutes (R.S.) 30:88

¹³ SSTA funding includes contributions to the account at the time of the transfer and at least quarterly payments to the account until it is fully funded. No financial security is required in addition to an SSTA once it is fully funded.

¹⁴ R.S. 30:93

SSTAs accounted for approximately \$223.8 million (64.7%) of the total amount of financial security as of October 2023. However, SSTAs only covered 1,494 (3.9%) of the 38,007 total wells covered by financial security. As recommended in our 2014 report, the legislature could encourage more operators to establish SSTAs by reducing the minimum site restoration recovery cost from \$250,000 to a lower amount that is more in line with actual plugging costs for most wells. For example, only 17 (10.1%) of the 168 wells that OSR plugged in calendar years 2022 and 2023 had costs greater than \$250,000. The number of SSTAs may also increase if state law was expanded to allow operators to establish SSTAs in other situations than just transfers, such as when initially permitting a new well.

Matter for Legislative Consideration 1: In order to increase the number of SSTAs established, the legislature may wish to consider revising state law to lower the minimum site restoration recovery cost and/or to allow SSTAs to be established in other situations than transfer to a new operator, such as when initially permitting new wells.

Recommendation 1: DENR¹⁵ should establish set time periods for review of the individual and blanket financial security amounts required by regulation to provide updated information on the discrepancy in costs and encourage increases to the required amounts at minimum to cover inflation.

Summary of Management’s Response: DENR agrees with this recommendation and stated that the Natural Resources Trust Authority recently created within the department will perform continuous review of financial security amounts. See Appendix A for OC’s full response.

OSR and LORA plugged 976 orphaned wells in fiscal years 2020 through 2023, including 396 wells that were plugged using grants from the federal government. However, despite increased plugging efforts, the number of orphaned wells continues to grow.

The OSR Program was created within OC in 1993 to properly plug and abandon orphaned wells and to restore sites to approximate pre-wellsite conditions. If an operator abandons a well without financial security, OC is authorized to use funds from the OSR Fund to plug the well. In addition, OSR’s efforts to plug orphaned wells were supplemented using federal IJJA grant funds beginning in January 2023, in addition to LORA beginning to plug wells in January 2022.

¹⁵ We addressed our recommendations to DENR instead of OC because Act 727 of the 2024 regular legislative session and Executive Order JML 24-13 require reorganization of DENR, which could change OC’s responsibilities.

The number of orphaned wells plugged per year increased 247.7%, from 153 in fiscal year 2020 to 533 in fiscal year 2023, due to assistance from LORA and IIJA funds.¹⁶ However, the number of orphaned wells only decreased 0.9%, from 4,295 in January 2020 to 4,258 as of October 2023, and then rose 12.4% to 4,785 by April 2024. DENR spent \$11.5 million in IIJA funds from January to June 2023 on two contracts for plugging large groups¹⁷ of land wells in northwest and northeast Louisiana in order to maximize the number of wells plugged with those funds.¹⁸ This allowed OSR to prioritize plugging a smaller number of more expensive high-risk wells with its typical allocated funding beginning in fiscal year 2023.¹⁹ LORA also plugged 90²⁰ orphaned wells between January 2022 and June 2023. However, the orphaned well population continues to grow. As shown in Exhibit 3, after spiking in fiscal year 2017, the number of new orphaned wells per year decreased, but still remained higher than before fiscal year 2017.²¹ Appendix D shows the number of orphaned wells plugged by OSR, LORA, and with IIJA funds in fiscal years 2020 through 2023.

¹⁶ These numbers and those in Exhibit 3 include 51 orphaned wells plugged by parties other than OSR or LORA, such as the Environmental Protection Agency, U.S. Coast Guard, or one of the well's prior operators.

¹⁷ By contrast, OSR bids out contracts to plug individual wells. OC stated that it is researching whether legislative or regulatory changes would be needed to use the bid model from the IIJA projects for OSR projects, as this would be more efficient for large groups of similar wells.

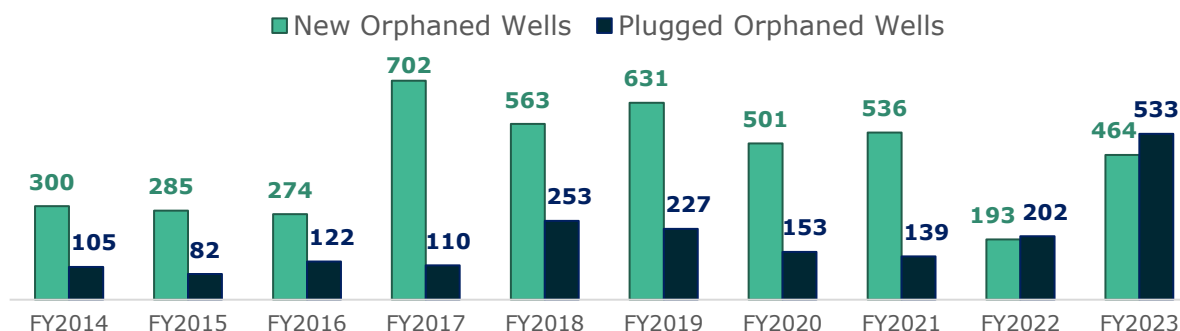
¹⁸ This only includes IIJA funds spent to plug wells through June 2023. OC had spent a total of \$33.8 million in IIJA funds to plug orphaned wells as of June 2024. Some IIJA funds were also spent on activities including conducting methane measurement and developing tools for tracking IIJA metrics.

¹⁹ The grants were received and administered through DENR, but OSR staff were involved in coordinating the federal projects.

²⁰ This includes six wells plugged by the LORA foundation, a charitable organization formed by LORA to request donations from oil and gas companies to plug orphaned wells. According to LORA, the only donor so far is its management company (Arkus Management Services), which LORA contracts to perform all LORA operations, as LORA does not have any employees of its own.

²¹ Fiscal year 2022 was the exception. According to OC, new orphaned wells dropped in that year due to the COVID-19 pandemic, as OC granted extensions to many operators, the compliance order process was delayed, and inspectors did not visit wells as often.

Exhibit 3 New Orphaned Wells and Plugged Orphan Wells Fiscal Years 2014 through 2023*



* Numbers may not match previous reports because OC updated its reporting method to be more accurate.

Source: Prepared by legislative auditor's staff using SONRIS data provided by OC.

In order to address the existing population of orphaned wells and keep pace with the number of new wells being orphaned each year, OC needs to proactively seek ways to permanently increase the OSR program's plugging capacity. According to OC, the state has mostly small operators and more than 25,000 inactive wells, and as a result, new wells are constantly being orphaned faster than existing orphaned wells can be plugged. For example, although the number of orphaned wells decreased slightly from 4,295 in January 2020 to 4,258 as of October 2023, it had already risen to 4,785 by April 2024. This was primarily due to 326 wells belonging to just one operator all being orphaned in February 2024. The operator did not have any financial security for these wells. OC stated that such rapid increases in the orphan population have been common and are likely to continue as more inactive wells are orphaned.

Louisiana also has an unknown number of **undocumented wells**, which are wells that were drilled and abandoned before regulatory programs were established. According to the Interstate Oil and Gas Compact Commission (IOGCC), undocumented wells often go undetected for years or decades.

Funding limitations prevent OC from expanding the OSR Program's efforts to plug more orphaned wells, as state law limits OSR's ability to collect adequate funding to address the orphaned oil well population.

Our 2014 and 2020 audits both found that the OSR program has insufficient funding to address the population of orphaned wells. OSR's total funding has increased 58.2%, from \$10.5 million in fiscal year 2020 to \$16.6 million in 2023, but insufficient funding remains a major challenge that prevents OSR from decreasing the growing population of orphaned wells. OC stated that if the OSR

program had more funds, it could immediately plug more wells.²² Exhibit 4 summarizes the different statutorily-mandated sources of revenue that OSR uses to plug orphaned wells. In addition to these revenue sources, DENR received IIJA grant funds beginning in fiscal year 2022.

| Exhibit 4 OSR Revenue Sources Fiscal Years 2020 to 2023 | | | | | | |
|--|---------------------|---------------------|---------------------|---------------------|---------------------|----------------|
| Revenue Source | FY 2020 | FY 2021 | FY 2022 | FY 2023 | Total (FY20-23) | Percent Change |
| Gas Production Fee | \$8,206,998 | \$9,462,151 | \$12,230,926 | \$13,186,578 | \$43,086,653 | 60.7% |
| Oil Production Fee | 1,039,263 | 589,155 | 447,943 | 813,287 | 2,889,648 | -21.7% |
| Financial Security Reimbursements | 169,585 | 687,651 | 1,582,065 | 1,421,953 | 3,861,254 | 738.5% |
| Inactive Well Assessment | 982,917 | 1,028,805 | 1,064,188 | 1,122,688 | 4,198,598 | 14.2% |
| Interest | 83,348 | 2,432 | 12,652 | 33,319 | 131,751 | -60.0% |
| Louisiana Oil and Gas Association | 1,800 | 4,196 | 3,852 | 5,781 | 15,629 | 221.2% |
| Total Funding | \$10,483,911 | \$11,774,390 | \$15,341,626 | \$16,583,606 | \$54,183,533 | 58.2% |
| Source: Prepared by legislative auditor staff using financial reports provided by OC. | | | | | | |

State law limits OSR’s ability to collect adequate funding to address the orphaned oil well population. We estimated that it will take approximately \$542.9 million to address the current population of orphaned wells, assuming no new wells become orphaned.²³ However, state law²⁴ currently requires that the collection of oil and gas production fees be suspended if the OSR Fund exceeds \$14 million. As a result, OSR is limited in its ability to collect adequate funding, which ultimately hinders how timely it can plug wells. According to this law, collection of production fees cannot resume until the OSR Fund balance decreases to \$10 million.

According to OC, when this law was put in place in 1993, the agency did not understand the magnitude of how many orphaned wells needed to be plugged. Although legislation in 2016²⁵ raised the original cap of \$10 million to \$14 million, this is still not sufficient to plug the current population of orphaned wells. OC also stated that removing the cap entirely or raising it to reflect the estimated cost to plug all orphaned wells would increase OSR’s capacity to plug more orphaned wells. This would prevent disruption of its primary funding source (production fees) and

²² During our 2020 audit, OSR’s plugging efforts were limited due to difficulty finding licensed contractors, so the agency could not have plugged more wells even if it had more funding. However, this is no longer an issue since Act 242 of the 2020 Louisiana regular legislative session removed statutory requirements for contractors to be licensed and obtain a performance bond.

²³ This is based on OSR’s average cost to plug a well (\$113,449) in calendar years 2022 and 2023 and the population of orphaned wells (4,785) as of April 2024.

²⁴ R.S. 30:86

²⁵ Act 666 of the 2016 Regular Legislative Session

would enable OC to also seek additional funding sources. OC stated that if the cap did remain, requiring it to be calculated based on annual production fee collections instead of the OSR Fund balance would help reduce administrative burden²⁶; however, this alternative would only be helpful if the cap was set much higher than anticipated revenue.

Although legislation in 2016 increased the rate of oil production fees, no changes have been made to the rate of gas production fees, which were last increased in 2004 and accounted for 93.7% of production fees collected in fiscal years 2020 through 2023. In an effort to increase funding for the OSR Fund, Act 666 of the 2016 Regular Legislative Session increased the fee on oil produced to \$.03 per barrel for any year where the average price of oil is above \$60 a barrel and \$.045 when the average price is above \$90 a barrel. In addition, Act 411 of the 2017 Regular Legislative Session eliminated the exemption²⁷ relative to severance taxes on horizontal wells, which helped increase funding to the OSR Fund. However, the majority of OSR's funding comes from the gas production fee, but legislation has not increased the gas production fee since 2004. Gas wells contributed approximately \$43.1 million (93.7%) of the \$46.0 million total production fees collected in fiscal years 2020 through 2023, which amounted to 79.5% of OSR's \$54.2 million in overall revenue. Gas production fees remain at the fixed rate of \$0.003 per thousand cubic feet of gas produced.

More than \$10 million of collected financial security had not been spent as of the end of fiscal year 2023, as spending these funds is often delayed by several factors, such as OSR budget priorities. When financial security is collected for an operator's orphaned wells, it is placed in an escrow account that can only be spent on plugging those specific wells. Since the escrow accounts are held by the Department of Treasury, OSR must first pay to plug the associated wells from the OSR Fund, which is then reimbursed from the escrow accounts. For fiscal years 2020 through 2023, we found that OC collected almost \$8.7 million in financial security; however, it only spent \$3.9 million of financial security funds on plugging wells in this period. At the end of fiscal year 2023, the balance in financial security escrow accounts was approximately \$10.3 million, a 68.0% increase from \$6.2 million at the end of fiscal year 2020.

Spending collected financial security may be delayed if the specific wells' plugging costs exceed the amount of financial security collected, as OSR has to wait to combine plugging them with other projects to help drive the cost down, or if OSR policy dictates plugging other wells with higher priority ratings first. In addition, spending these funds may be delayed due to the overall impact on OSR's budget. When OSR plugs wells with financial security, even though the OSR Fund is reimbursed from the escrow accounts, the amount of financial security spent is deducted from OSR's overall spending budget for the year. As a result, spending

²⁶ For the purpose of the cap, state law requires collected financial security, outstanding contractual obligations, and other ever-changing amounts tracked by separate OC divisions to be excluded from calculating the OSR Fund's cash balance.

²⁷ Wells that are exempt from severance taxes are also exempt from production fees.

financial security funds from the escrow accounts reduces the amount that OSR can spend from the OSR Fund (even though it has more funds available). Since collected financial security is not included in calculations of whether the OSR Fund balance exceeds the \$14 million cap, spending these funds can also impact OSR's ability to collect production fees.²⁸ According to OC, it could use financial security funds more timely if spending them did not impact its ability to generate and spend funds from other sources.

Since February 2020, we found that OC has not had significant new issues with financial institutions failing to honor their obligations to pay financial security when secured wells are orphaned. Our 2020 audit found that, as of February 2020, 12 financial institutions had not paid approximately \$5 million in financial security that OC had called²⁹ when wells were orphaned. However, of the \$9.7 million that OC called from February 2020 through September 2023,³⁰ OC was only unable to collect \$81,000 from four different financial institutions for varying reasons. According to OC, each time that lawsuits have resulted in it being unable to collect a financial instrument, it has updated its standard contract language or policies to ensure that the reason for non-collection will not be possible in the future.

One of the reasons that LORA was created was to address issues with financial security. When wells secured by LORA are orphaned, the CEA requires OC to give LORA the opportunity to plug the wells before requiring LORA to pay the financial security amount. We found that apart from one financial security instrument for \$50,000, LORA always opted to plug secured wells when they were orphaned. However, of the 175 wells secured by LORA that were orphaned through December 2023, 130 wells secured by nine financial security instruments totaling \$10.6 million had not been plugged as of July 2024. We address this in our second performance audit³¹ on how the state is addressing the growing population of orphaned wells, which focuses on OC's oversight of LORA.

Matter for Legislative Consideration 2: The legislature may wish to consider removing the \$14 million cap on the OSR Fund or increasing it based on the total estimated costs to plug orphaned wells, which would provide more adequate funding for addressing the growing orphaned well population.

²⁸ State law requires collection of production fees to be suspended if the OSR Fund balance reaches \$14 million. When orphaned wells without financial security are plugged using the OSR Fund, this decreases the balance. However, when OSR receives reimbursements from the escrow accounts for plugging wells with financial security, the OSR Fund balance goes back up, so these projects must be planned carefully to prevent the OSR Fund from reaching the \$14 million cap.

²⁹ "Calling" financial security refers to OC notifying the surety that they are obligated to pay OC the secured amount.

³⁰ This excludes \$2.9 million called for financial security provided by LORA during this period, as financial security provided by LORA was analyzed separately.

³¹ LLA, "[Oversight of the Louisiana Oilfield Restoration Association's \(LORA\) Efforts to Address Orphaned Oil and Gas Wells: Office of Conservation – Department of Energy and Natural Resources](#)", October 2024

Matter for Legislative Consideration 3: The legislature may wish to consider increasing the production fee for gas wells or establishing a variable fee based on the market price of gas, similar to the production fee for oil wells.

Matter for Legislative Consideration 4: The legislature may wish to consider providing the OSR program additional budget flexibility to allow OSR to spend collected financial security to plug wells without these expenditures decreasing the amount of revenue from other sources that OSR can spend.

The number of inactive wells, which have a higher risk of being orphaned, increased 21.7%, from 17,775 in August 2019 to 21,629 in April 2024. Although OC recently updated regulations to increase the annual inactive well fees based on the time each well has been inactive, OC does not place as many restrictions on inactive wells as some other states.

According to OC regulation, inactive wells are wells that have not produced oil or gas in more than six months.³² Operators must include these wells on semiannual inactive well reports to OC, including whether the well has future utility or no future utility. The future utility status allows operators to delay plugging inactive wells that still have potential for use, such as returning to production once market prices increase to profitable levels or converting it to a service well, waste fluid disposal, or gas storage. However, they can create environmental and public health hazards if not properly monitored and maintained.

Inactive wells are classified as either:

- (1) **Future Utility:** Wells currently not producing but may have some use in the future.
- (2) **No Future Utility:** Non-producing wells that are not expected to have any further use.

Our 2014 audit found that OC allowed operators to place inactive wells in future utility status for extended periods of time to avoid plugging them. As a result, OC revised its regulations³³ in May 2015 to require operators to either plug inactive wells with future utility within five years of becoming inactive or pay an annual fee of \$250 per well.³⁴ In addition, our 2014 audit found that OC did not have an effective process for identifying inactive wells, and only 12,181 inactive

³² The full definition in LAC 43 XIX:101 is “an unplugged well that has been spud or has been equipped with cemented casing and that has had no reported production, disposal, injection, or other permitted activity for a period of greater than six months and is not part of an approved production program.”

³³ LAC 43:XIX.137

³⁴ Operators were exempt from paying the fee if the well was included on an approved schedule of abandonment (SOA), which shows a timeline for when the operator planned to plug the well. However, the October 2023 rule change eliminated this exemption.

wells were recorded as of June 2013. However, our 2020 audit found that OC developed processes to better identify and address inactive wells, such as requiring electronic submission of inactive well reports. As a result, the number of recorded inactive wells increased 45.9% to 17,775 in August 2019.

The number of inactive wells increased 21.7%, from 17,775 in August 2019 to 21,629 in April 2024, which puts the state at risk that the orphaned well population may grow in the future. In a 2021 report,³⁵ the Interstate Oil and Gas Compact Commission (IOGCC)³⁶ states that inactive wells present an elevated risk of becoming orphaned and therefore imposing a liability on the state for plugging. We similarly found that inactive wells were more likely to be orphaned, as 2,199 (51.6%) of the 4,258 orphaned wells as of October 2023 had an inactive status prior to being orphaned. In addition, the IOGCC reports that if a high percentage of an operator's total wells are inactive, this may indicate an increased vulnerability to the state that the operator could become insolvent and leave orphaned wells. We found that, as of October 2023, more than half of the wells were inactive for 306 (33.9%) of the total operators in the state. In addition, 21,842 (42.5%) of the state's 51,430 wells overall³⁷ were inactive.

Exhibit 5 shows a comparison of the locations of orphaned and inactive wells as of October 2023, as well as how long they had remained in that status. The OSR program did not start until 1993, so the maximum time that a well could have been orphaned was approximately 30 years; however, 13.0% of inactive wells had been inactive for more than 30 years, with the longest being inactive for 86 years. The map also shows that 5,600 (25.6%) of the inactive wells were in offshore or inland water locations. By contrast, there were only 1,175 (4.0%) active wells in offshore or inland water locations as of October 2023. Operators may have greater incentive to allow wells in these locations to remain inactive because they typically cost more to plug than land wells.

³⁵ IOGCC, "[Idle and Orphan Oil and Gas Wells: State and Provincial Regulatory Strategies](#)," 2021.

³⁶ The IOGCC is a multi-state government agency chartered by the U.S. Congress in 1935. It promotes sound regulatory practices to help states prevent waste of natural resources vital to economic development and energy security while protecting health, safety, and the environment.

³⁷ This only includes wells with status codes that require financial security to remain consistent with our other analyses.

Exhibit 5 Orphaned and Inactive Wells by Time Since Status As of October 2023

Orphaned Wells (4,258 total)

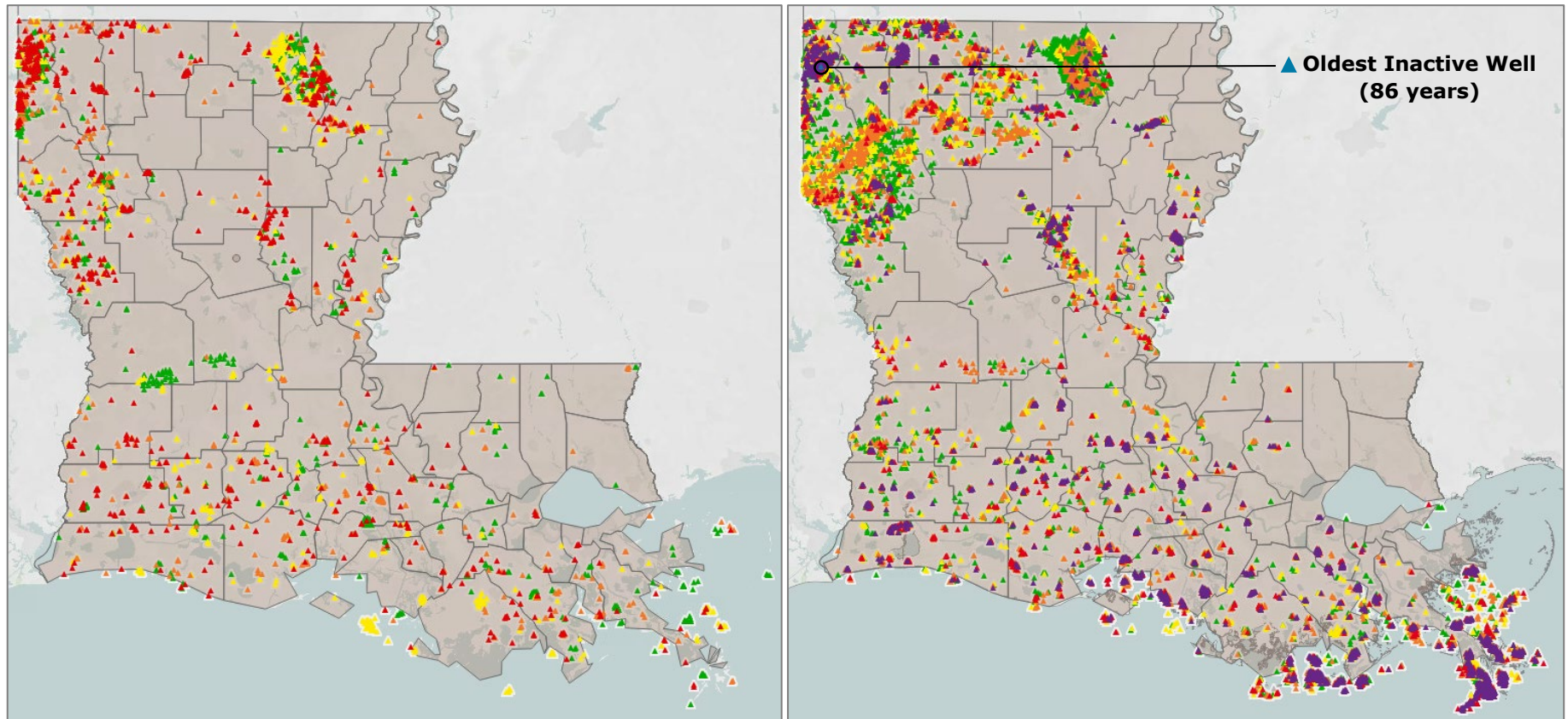
| |
|---------------|
| 1,433 (33.7%) |
| 1,031 (24.2%) |
| 647 (15.2%) |
| 1,147 (26.9%) |
| 0 (0.0%) |

Legend: Time Scale

| |
|--------------------------|
| 5 years or less |
| Over 5 years – 10 years |
| Over 10 years – 20 years |
| Over 20 years – 30 years |
| Over 30 years |

Inactive Wells* (21,842 total)

| |
|---------------|
| 8,421 (38.6%) |
| 4,446 (20.4%) |
| 3,366 (15.4%) |
| 2,366 (10.8%) |
| 2,843 (13.0%) |

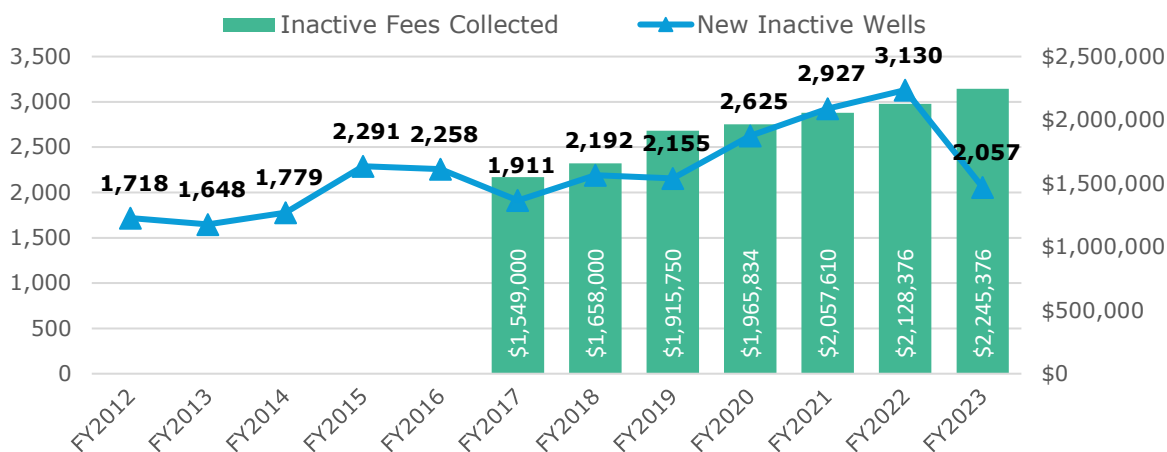


* Percentages do not add up to 100% because 400 (1.8%) inactive wells did not have latitude and longitude data available.

Source: Prepared by legislative auditor’s staff using SONRIS data provided by OC.

The rate of new inactive wells has not decreased since OC began collecting inactive well fees, which could indicate that the fees are not acting as a deterrent. OC began collecting inactive well fees in fiscal year 2017. As shown in Exhibit 6, in fiscal years 2012 through 2017, an average of 1,934 wells became inactive each year, compared to an average of 2,514 in fiscal years 2018 through 2023.

**Exhibit 6
New Inactive Wells and Inactive Fees Collected
Fiscal Years 2012 through 2023**



* This shows the total amount of inactive fees collected, which was split evenly between deposits to the OSR Fund and the Oil and Gas Regulatory Dedicated Fund Account.

Source: Prepared by legislative auditor's staff using OC financial reports and SONRIS data provided by OC.

The number of new inactive wells may not have decreased after OC began assessing inactive well fees because the combined cost of fees and financial security is still less than the cost to plug the wells. In addition to paying the fees, the amended OC regulations require operators to obtain financial security for inactive wells.³⁸ However, we found that the average financial security per well was \$3,248³⁹ as of October 2023, compared to the OSR average cost of \$113,449 to plug orphaned wells in calendar years 2022 and 2023.⁴⁰ Even when adding the annual inactive well fee to amounts paid to maintain financial security (which is usually a percentage of the amount secured paid periodically), this is still generally less than the cost to plug the well. In addition, OC did not always consistently require operators to pay the annual fees. OC granted some operators exceptions for inactive fees in fiscal years 2017 through 2024 for reasons such as financial hardship. However, OC does not have a formal policy describing reasons for which these exceptions may be granted or the amounts that fees should be reduced. According to OC, it plans to implement a consistent policy for granting these exceptions as part of its implementation of updated inactive fee regulations.

³⁸ The May 2015 update required financial security for future utility wells, and the October 2023 update added this requirement for no future utility wells.

³⁹ This excludes wells with SSTAs, which have higher amounts than other financial security. Including SSTAs, the average financial security per well was \$9,106.

⁴⁰ OSR's median plugging cost per well was \$17,675 during this period.

OC updated its regulations in October 2023 to increase inactive well fees for older and deeper wells; however, this update also removed the requirement to plug inactive wells with no future utility within 90 days, meaning that all inactive wells can now remain unplugged indefinitely as long as operators pay the fees. When OC revised its regulations in May 2015 to introduce the option of paying inactive well fees for future utility wells not plugged within five years, these changes did not apply to inactive wells with no future utility, which were still required to be plugged within 90 days unless an extension was approved.⁴¹ However, our 2020 audit found that 444 (62.1%) of 715 wells with no future utility were not in compliance with these regulations because OC allowed their operators to pay the inactive well fee rather than plugging them. According to OC, it continued allowing this noncompliance until October 2023, when it updated regulations to match practice.

The updated regulations establish nearly the same requirements for all inactive wells: operators must pay annual inactive well fees for wells not plugged within the prescribed deadline, which is five years for wells with future utility and 90 days for wells with no future utility.⁴² In addition, OC replaced the flat \$250 fee per inactive well with a range of fees that increase based on each well’s depth and time inactive, as shown in Exhibit 7.⁴³ Based on Louisiana’s inactive well population as of October 2023, we found that OC could assess \$5.1 million in fees using the new variable rate, compared to just \$3.0 million using the previous \$250 rate – a 68.7% increase.⁴⁴

| Exhibit 7 Inactive Wells Fees Updated October 2023 | | |
|---|----------------------------|------------------|
| Total Depth (ft.) | Time Since Inactive | |
| | 5-10 years* | 10+ years |
| 0-3,000 | \$125 | \$188 |
| 3,001-9,999 | \$250 | \$375 |
| 10,000+ | \$500 | \$750 |
| * For wells with no future utility, fees in this range start at 90 days instead of 5 years. Source: Prepared by legislative auditor’s staff based on OC regulation. | | |

Since half of inactive well fees are deposited in the OSR Fund, this change will likely result in more funding for plugging orphaned wells.⁴⁵ Higher fees also increase an operator’s incentive to plug or find another use for inactive wells sooner. However, the updated regulations now allow all inactive wells, regardless of whether they have future utility, to remain inactive indefinitely as long as operators pay the annual fees and maintain financial security coverage as required. According to OC, setting a maximum time limit that wells can have any inactive status would cause some wells to be plugged that could have become valuable assets in the future; however, wells with no future utility by definition do not have that potential.

⁴¹ Extensions past 90 days were allowed if wells were on an approved SOA or granted an extension.

⁴² According to OC, before this rule change, it treated all inactive wells the same for fees, so it did not charge fees for no future utility wells until they had been inactive for five years.

⁴³ The October 2023 changes also implemented an incentive program to reduce an operator’s total inactive fees between \$375 to \$1,500 for each well plugged by the operator in the prior 12 months.

⁴⁴ This analysis also accounted for other changes in how fees were assessed, including wells on SOAs no longer being exempted and OC charging fees for wells with no future utility starting at 90 days.

⁴⁵ The remainder are placed in the Oil and Gas Regulatory Dedicated Fund Account, which OC uses for regulation of the oil and gas industry and other industries under its jurisdiction.

Some other states have implemented more restrictive policies to help manage inactive wells and prevent them from becoming orphaned. For example, unlike Louisiana, the IOGCC reported that most of the 32 states it surveyed require inactive wells with no future utility to be plugged. However, even if OC reinstated the deadline for no future utility wells, it would only apply to a small number of inactive wells, as only 460 (2.1%) inactive wells were classified as having no future utility as of October 2023. This could be because, in Louisiana, operators are the ones who classify whether wells have future utility,⁴⁶ and “future utility” is not defined in law, regulation, or policy. The IOGCC report provides examples⁴⁷ of how other states approach assessing wells’ future utility, as well as other inactive well restrictions that could be helpful in Louisiana:

- **Agency Approval of Inactive Status Based on Future Utility.** At least eight states require operators to submit information about a well’s future utility to get agency approval for the well to enter or remain in inactive status. For example, West Virginia⁴⁸ regulations require operators to submit information such as historic production data, estimated remaining recoverable reserves, estimated costs to convert the well to a different purpose, and a plan explaining how the operator will utilize the well in the future, including the estimated date that use will begin.
- **Additional Financial Security.** At least 11 states implement additional financial security requirements for inactive wells that account for higher risk of becoming orphaned. For example, some states require higher amounts for wells that have remained inactive past a certain time period, for inactive wells with greater depths or larger facilities, when operators have a history of noncompliance, or when operators have more than a certain number of inactive wells. In addition, some states limit whether inactive wells can be covered by blanket security policies.
- **Limiting Inactive Wells per Operator.** At least two states limit the number or percent of an operator’s wells that can be inactive. In New Mexico, operators can only have two to 10 inactive wells depending on how many they operate overall; and in Michigan, no more than 10% of an operator’s wells can be inactive at any time.
- **Monitoring Well Integrity.** Since inactive wells are not in operation, any deterioration and resulting environmental harm can remain unobserved for months or years. For example, in Louisiana, inactive wells are only inspected by OC once every five years. At least 14

⁴⁶ Operators indicate on their semi-annual inactive well reports whether the wells have future utility. LAC Title 43:XIX.137 states that the district manager will periodically review these classifications and may require operators to submit supporting information; however, it does not indicate how often this review will occur or what criteria must be met for future utility to be confirmed.

⁴⁷ All examples are from the IOGCC report unless otherwise specified.

⁴⁸ West Virginia Code of State Rules 35-5-3 and 35-5-4

states require mechanical integrity tests⁴⁹ for inactive wells, which helps to prevent undetected hazards.

States also implemented several other restrictions for inactive wells, such as prohibiting operators with any outstanding compliance violations from having inactive wells and specifying minimum production levels before a well can return to active status.⁵⁰ Ultimately, OC should research these and any other practices used by other states to help determine what combination of additional restrictions could most effectively manage Louisiana’s growing population of inactive wells and prevent as many as possible from becoming orphaned.

Recommendation 2: DENR should implement a consistent policy for granting exceptions for inactive well fees, including reasons that exceptions can be granted and the amount that fees will be reduced for each reason.

Summary of Management’s Response: DENR agrees with this recommendation and stated that the Natural Resources Trust Authority will develop a strategic plan including measures specifically designed to address the financial challenges associated with inactive wells. See Appendix A for OC’s full response.

Recommendation 3: DENR should consider implementing additional restrictions on inactive wells to prevent them from remaining inactive indefinitely, such as a maximum amount of time that wells with no future utility may remain inactive, requiring review and approval of wells’ classification as having future utility, requiring additional risk-based financial security for inactive wells, monitoring inactive wells’ mechanical integrity, or limiting the number or percent of inactive wells that an operator can have at the same time.

Summary of Management’s Response: DENR agrees with this recommendation and stated that it will look toward identifying appropriate forms of risk analysis to better direct its efforts in regulating inactive wells and plugging obligations. See Appendix A for OC’s full response.

⁴⁹ MITs demonstrate the absence of significant leaks in a well. These tests show whether an inactive well is environmentally sound and capable of production, which could also be used to determine inactive wells’ future utility.

⁵⁰ For example, Texas regulations (16 Texas Administrative Code 3.15) set minimum production amounts that must be met before inactive wells can be reassigned an active status. In Louisiana, inactive wells can revert to active status if they produce any amount of oil or gas for three consecutive months, even if the amount is minimal. This creates a loophole for operators to interrupt wells’ inactive status (for example, before they have been inactive for five years) and avoid paying inactive well fees.

APPENDIX A: MANAGEMENT'S RESPONSE

TYLER PATRICK GRAY
SECRETARY

DUSTIN H. DAVIDSON
DEPUTY SECRETARY



MARK NORMAND, JR.
UNDERSECRETARY

MANNY ACOSTA
OIL SPILL COORDINATOR

KEITH O. LOVELL
ASSISTANT SECRETARY
COASTAL MANAGEMENT

AMANDA McCLINTON
ASSISTANT SECRETARY
ENERGY

ANDREW B. YOUNG
ASSISTANT SECRETARY
MINERAL RESOURCES

BENJAMIN C. BIENVENU
COMMISSIONER
CONSERVATION

DEPARTMENT OF ENERGY AND NATURAL RESOURCES

October 21, 2024

The Honorable Mike Waguespack
Louisiana Legislative Auditor
P.O. Box 94397
Baton Rouge, LA 70804-9397
C/O Gina V. Brown,
Performance Audit Manager
(Sent by Email: GBrown@lla.la.gov)

Re: Response to Performance Audit Reports

Dear Mr. Waguespack,

This response focuses directly on the Performance Audit Reports¹ associated with addressing orphaned oil and gas wells, yet it also expands to outline the challenges and proposed solutions regarding the management of orphaned wells in Louisiana. These are the third and fourth performance reports on orphaned wells since the initial report in 2014. The legislature and department have attempted to address this issue within their means over that same time frame. During the 2024 Regular Session, Rep. Bret Geymann proposed House Bill 810, now Act 727, creating the Natural Resources Trust Authority ("Trust Authority") within the department. One of the primary purposes of that entity is to address the exact issues raised in your office's reports.

While the Office of Conservation is responsible for the specific functions of regulating oil and gas operations and requiring related financial security, its undertaking of these functions in isolation has proven unsuccessful as outlined in your reports. This highlights, precisely why a more cohesive department is needed to adequately manage the proper plugging and abandonment of oil and gas wells. Proper funding is also needed to do so, which is a role the Trust Authority can, in part, fulfill with oversight from the existing Mineral and Energy Board that is already charged with marketing the state's resources and is thus equipped to engage on the issues in a public and transparent manner.

The Trust Authority is part of the larger DRIVE² initiative, which is designed to address the challenges currently faced by state government in managing its resources effectively. This includes the management of orphaned wells. The Trust Authority, created under Act 727, aims to

¹ Specifically, 2 reports: 1) Progress Report: State Efforts to Address Orphaned Oil and Gas Wells, and 2) Oversight of the Louisiana Oilfield Restoration Association (LORA) Efforts to Address Orphaned Oil and Gas Wells.

² On February 2, 2024, Governor Jeff Landry issued Executive Order JML 24-13, directing Department of Energy and Natural Resources to investigate consolidation and reorganization of the State's natural resources management regime. DENR pursued legislation during the 2024 regular session to prepare the groundwork for reorganization. This project is named the, "Departmental Review for Innovation and Visionary Enhancement."

develop a strategic approach to address the financial risk analysis related to energy and natural resources projects, including the risks associated with plugging and abandoning oil and gas wells in a manner that decreases the number of orphaned wells. The Mineral and Energy Board adopted a resolution at its October 9, 2024 meeting establishing an executive committee for the Trust Authority, supporting the department in its efforts to appoint a director for the Trust Authority, and requesting updates on Trust Authority's build out. DENR is currently interviewing for the Trust Authority director position and working the Trust Authority into next year's budget.

CHALLENGES AND RESPONSES

Challenge: *Lack of Funding for Plugging and Abandonment*

Response: To address this, after the Office of Conservation ("Conservation") sets appropriate financial obligations for operators, the Trust Authority, operating in conjunction with the State Bond Commission ("Bond Commission") and the Louisiana Department of Treasury ("Treasury") has the capability to secure and manage the funding, ensuring that the financial security amounts are adequate. By regulating substitutions and transfers necessary for meeting these obligations, the Trust Authority will create a more robust financial safety net. Moreover, by relying more heavily on financial security options that provide the department with direct custody of the funding, the Trust Authority will reduce the reliance on third parties. This direct management of funds will ensure that the available cash is more capable of meeting plugging obligations even as external factors such as inflation come into play.

Challenge: *Bureaucratic Hurdles and Fragmented Management*

Response: The restructuring under DRIVE will consolidate functions within DENR and enhance coordination among agencies. This will streamline the permitting, enforcement, and regulatory processes, thereby reducing bureaucratic hurdles and ensuring a more efficient approach to managing plugging risks and orphaned wells.

Challenge: *Inefficiencies in Current Management Practices*

Response: The establishment of the Natural Resources Trust Authority allows for the development of specific rules and regulations under the Administrative Procedure Act, as well as the adoption of standard operating procedures and internal policies. These rules and internal procedures will set clear guidelines for financial obligations, and policies for plugging and abandonment, ensuring consistency and efficiency in management practices.

Challenge: *Inadequate Emergency Response and Risk Management*

Response: The DRIVE initiative includes the establishment of an Emergency Response Section within DENR. This section will focus on preparedness and risk management, ensuring a swift and effective response to emergencies related to orphaned wells.

Challenge: *Overlapping Programs and Redundant Efforts*

Response: Overall, the enactment of Act 727 and the establishment of the Natural Resources Trust Authority mark significant steps toward addressing the challenges associated with the management of orphaned wells in Louisiana. Through enhanced coordination, strategic planning, and dedicated funding, the state aims to achieve a more efficient and effective approach to managing its natural resources. The DRIVE initiative further supports these efforts by streamlining processes and fostering collaboration among relevant agencies. By integrating the Louisiana Oil Spill Coordinator's Office into the Department, Act 727 aims to eliminate duplicative programs and allocate resources more effectively. This consolidation will allow for a holistic approach to well management, maximizing the physical reduction of abandoned wells and reducing overhead costs.

Responses to each Report and Result

REPORT 1 **PROGRESS REPORT: STATE EFFORTS TO ADDRESS ORPHANED OIL WELLS**

Objective: To evaluate OC's progress toward addressing orphaned wells.

Finding 1 *Although more wells are covered by financial security since OC removed most exemptions, financial security amounts are still not sufficient to cover the actual cost of plugging wells.*

Recommendation 1: DENR should establish set time periods for review of the individual and blanket financial security amounts required by regulation to provide updated information on the discrepancy in costs and encourage increases to the required amounts at minimum to cover inflation

Response

To expand the capability of the department to review financial security amounts with proper oversight, the Trust Authority under the oversight of the State Mineral and Energy Board, operating in conjunction with the Bond Commission and the Treasury will support Conservation by scrutinizing the amounts and financial obligations and by managing the resulting funding in the event a well becomes orphaned, all with the ultimate goal of ensuring that the financial security amounts are adequate. It is expected that review of financial security amounts and other

requirements will be continuous, with the added option of discussing such reviews at the regularly scheduled monthly public meetings of the State Mineral and Energy Board.

It is envisioned that by regulating substitutions and transfers necessary for meeting these obligations, the Trust Authority will create a more robust financial safety net. Moreover, relying more heavily on financial security options that provide the department with direct custody of the funding, the Trust Authority will reduce the reliance on third parties. Additionally, by working with existing governance structures better equipped to manage the State's interest, expanding its authority to engage in financial markets and capitalize on the tremendous value having custody of cash, under proper oversight, of the financial security instrument this direct management will ensure that the available cash is capable of meeting plugging obligations even as external factors such as inflation come into play.

Finding 2 *OSR and LORA plugged 976 orphaned wells in fiscal years 2020 through 2023, including 396 wells that were plugged using grants from the federal government. However, despite increased plugging efforts, the number of orphaned wells continues to grow.*

Response

The Trust Authority will serve as a counterbalance to Conservation's regulatory oversight of operations by properly assessing risk of the financial instruments required, which will help better manage the influx of new orphaned wells and ensuring that operators are financially responsible for plugging their wells. In addition, the subject matter expertise of financial markets, including custody of such funds at the Department of Treasury, reduces risk of loss or an inability to collect due to fraud or other unforeseen consequences. While developing a strategic plan to address financial challenges and goals is a top priority, a tactical approach to manage this immediate issue will be prioritized. Nonetheless, a process in which to establish a strategic plan is critical for effective management of inactive wells ensuring proper controls are in place to manage the regulatory obligations set forth by Conservation and that the funding will be available to execute. Lastly, through Executive Order JML 24-13, the department, and the Natural Resources Steering Commission, is exploring ways to integrate processes, procedures, and funding following the integration of Louisiana Oil Spill Coordinator's Office into the department per Act 727. The goal being a holistic approach to well management by integrating existing fees, eliminating duplicative programs, overlap, and mission creep to efficiently allocate funds maximizing the impact of each dollar and reducing the number of unfunded abandoned wells.

Finding 3 *Funding limitations prevent OC from expanding the OSR Program's efforts to plug more orphaned wells.*

Response

The Trust Authority will have the capability to solicit, accept, and expend grants, thus expanding the sources of funding available. Establishing new fees and other financial provisions through rules and regulations will create a sustainable model for plugging orphaned wells. Operating with oversight by the Mineral and Energy Board, the Trust Authority will address the issue in a public

and transparent manner with proper oversight, ensuring a consistent and reliable flow of funds for these efforts.

Finding 4 *The number of inactive wells, which have a higher risk of being orphaned, increased 21.7% from 17,775 in August 2019 to 21,629 in April 2024. Although OC recently updated regulations to increase the annual inactive well fee based on the time each well has been inactive, OC does not place as many restrictions on inactive wells as some other states.*

Recommendation 2: DENR should implement a consistent policy for granting exceptions for inactive well fees, including reasons that exceptions can be granted and the amount that fees will be reduced for each reason.

Response

By regulating financial instruments and ensuring better management of inactive wells, the Trust Authority will reduce the risk of these wells becoming orphaned and better cover costs if they do become orphaned. The strategic plan will include measures specifically designed to address the financial challenges associated with inactive wells. Furthermore, by reallocating funds efficiently and eliminating duplicate programs, the department aims to reduce overhead costs and focus resources on physically reducing the number of abandoned wells.

Recommendation 3: DENR should consider implementing additional restrictions on inactive wells to prevent them from remaining inactive indefinitely, such as a maximum amount of time that wells with no future utility may remain inactive, requiring review and approval of wells' classification as having future utility, requiring additional risk-based financial security for inactive wells, monitoring inactive wells' mechanical integrity, or limiting the number or percent of inactive wells that an operator can have at the same time.

Response

The department is looking at innovative ways to address the orphan well population currently and, in the future, including potential risk-based protocols, new requirements, and through increased funding to address those wells that do become orphaned. Due to the many complexities surrounding current and future value of existing wells, including those surrounding the confidential nature of certain economic and reserve data, the department will look towards identifying appropriate forms of risk analysis to better direct its efforts in regulating inactive wells and plugging obligations.

Report 2 Oversight of the Louisiana Oilfield Restoration Association's (LORA) Efforts to Address Orphaned Oil and Gas Wells

Objective: To evaluate the Office of Conservation's oversight of LORA.

Finding 1 *OC has sole oversight of LORA, but it does not conduct sufficient monitoring to protect operators and the state from the risk of LORA failing to fulfill its financial obligations. LORA is not subject to federal and/or state regulations that apply to financial institutions, so its operations and solvency are not monitored by the regulatory agencies that oversee other companies that provide financial security.*

Recommendation 1: DENR should ensure evaluation occurs of LORA's financial performance to date in order to make informed decisions that will support LORA's financial health in a holistic way. This could include using a third-party financial expert to develop standards for accepting risk tolerances, a detailed process for periodic monitoring of LORA's financial health and CEA compliance, and recommendations to strengthen the CEA to mitigate risks to the state.

Recommendation 2: DENR should develop a process to monitor LORA's solvency and CEA compliance that provides similar protections to the operators and the state that would be offered if LORA was regulated as a financial institution, and update the CEA as applicable.

Response

The Trust Authority will serve as the entry point in assessing risk in authorized financial security entities, such as LORA, as it relates to financial wherewithal and serving as the additional layer of financial oversight. Further, the Trust Authority is authorized to execute necessary contracts and instruments and enter into agreements for deductions and payments, enhancing oversight of financial security entities like LORA. It will also adopt rules to establish procedures and standards for evaluating the worthiness of applications and ensuring the compliance of financial security entities. This comprehensive oversight will align with the functions of the Mineral & Energy Board, providing a higher level of scrutiny and accountability. The Trust Authority will serve as the primary monitor for financial solvency and risk in authorizing entities, such as LORA, and will help identify any additional oversight and monitoring to protect the state and operators. Finally, the department will work towards identifying and requiring necessary updates to the CEA.

Finding 2 *Although LORA provides 45.3% of all financial security for Louisiana wells as of October of 2023, OC does not have a contingency plan to address financial and safety risks to the state if the CEA is terminated or LORA cannot cover its obligations.*

Recommendation 3: DENR should develop a plan to protect the state from financial risks if the CEA with LORA is terminated or LORA ceases

operations and ensure the current CEA is amended with comprehensive terms of termination.

Recommendation 4: DENR should consider whether LORA's current reserve amount is sufficient to mitigate the risk insolvency, and if not, ensure the CEA is amended to increase the required minimum and/or set it based on a percentage of the amount secured instead of a fixed amount.

Recommendation 5: DENR should ensure the CEA is amended to update terms, as appropriate, to mitigate risks related with LORA providing SSTAs, and/or evaluate whether operators with SSTAs through LORA should find alternative funding through regulated financial institutions.

Response

The strategic plan developed by the Trust Authority will include contingency measures to address financial and safety risks associated with the potential termination of agreements with entities like LORA. The authority will evaluate and adjust the minimum reserve requirements to ensure they are sufficient to cover financial responsibilities, thus mitigating risks and ensuring stability. Similarly the Trust Authority will evaluate and determine whether operators with SSTAs through LORA should find alternative funding through regulated financial institutions.

Finding 3 *Although OC has never exercised its authority to monitor LORA's actual administrative expenses to determine if the percent of fees allowed for this purpose is reasonable, OC allowed LORA to increase this percentage from 20% to 36% after the minimum reserve balance was met. As a result, LORA retained an additional \$1.1 million from June 2022, through December 2023 that could have been used to plug orphaned wells.*

Recommendation 6: DENR should ensure the CEA is amended to clarify what amount of fees LORA may retain for administrative expenses after the minimum reserve balance is met.

Recommendation 7: DENR should evaluate the actual amount of administrative expenses spent on LORA operations to determine if the amount allowed for this purpose is reasonable and, if necessary, ensure that the CEA with LORA is amended to change the allowable administrative amount or that another entity is identified to perform this function more efficiently.

Response

The Trust Authority will implement requirements to monitor and control administrative expenses, ensuring that funds are effectively utilized for plugging wells. By determining reasonable limits for administrative expenses and adjusting percentages as necessary, the Trust Authority will ensure

that more funds are directed toward the primary goal of reducing orphaned wells. This regulation will prevent financial mismanagement and ensure that administrative costs are kept in check.

Finding 4

OC did not include important provisions in its CEA with LORA to help ensure that LORA operates in the state's best interest. Specifically, the CEA does not address how LORA should spend investment income, does not establish measurable targets for evaluating LORA's performance, and does not contain an audit clause. Currently, OC allows LORA to keep all investment income from the reserve account or other funds accrued, which may incentivize it to delay plugging wells to increase interest earned.ⁱⁱⁱ

Recommendation 8: DENR should ensure that the CEA is amended to clarify what should happen to the investment income earned from the fees that LORA collects, such as whether these amounts should go into the reserve fund for the purpose of plugging orphaned wells.

Recommendation 9: DENR should ensure the CEA is amended to establish specific, measurable performance targets that can be monitored to evaluate LORA's performance, such as providing financial security to a certain number of high-risk operators, plugging a certain number of orphaned wells within a given time period, and spending its entire annual plugging budget within a specified time period after it is budgeted.

Recommendation 10: DENR should ensure the CEA is amended to allow full access to LORA's operations and financial records for the purpose of any audit conducted by the legislative auditor.

Response

The Trust Authority will specify how investment income should be utilized and help establish clear performance targets for financial security entities. Including audit clauses and performance metrics will ensure thorough monitoring and compliance with agreements, thereby aligning LORA's operations with the state's best interests.

Finding 5

OC did not ensure that LORA prioritized plugging its secured wells that were orphaned, as required in the CEA. Of the 175 wells secured by LORA that were orphaned through December 2023, 130 (74.3%) remained unaddressed as of October 2024. In addition, OC has not provided sufficient guidance to ensure LORA effectively used the option to transfer still-viable orphaned wells to new operators, which can also reduce the orphaned oil well population.

Recommendation 11: DENR should enforce the CEA requirement that LORA prioritize plugging its secured wells that are orphaned, for example by amending the CEA to establish a timeframe in which LORA must plug these wells and/or an approval process for LORA to plug unsecured orphaned wells. This would help ensure that LORA remains solvent long-term so that the state does not ultimately have to pay to plug LORA's secured orphaned wells.


Recommendation 12: DENR should ensure the CEA is amended to include criteria and processes related to determining secured orphaned wells' viability and facilitating their transfer to new operators, including requirements to monitor the accuracy of viability determinations and unnecessary delays to plugging unviable wells.

Recommendation 13: DENR should proactively reevaluate the relative benefits of spending or not spending reserve funds to plug orphaned wells when the reserve fund falls below \$5 million in order to prepare guidance for LORA that will protect its ability to fulfill long-term obligations but also prevent unnecessary delays to plugging secured orphaned wells.

Response

The Department, coordinating between its offices and the Trust Authority, will set clear timeframes and performance targets for plugging orphaned wells, ensuring timely and cost-effective actions. The strategic plan will include measures for ensuring that financial security entities like LORA prioritize and efficiently plug the orphaned wells they secure. Further the Trust Authority will evaluate the benefits of spending LORA's reserve funds and prepare guidance to protect its ability to fulfill long-term obligations and prevent unnecessary delays in plugging orphaned wells that LORA secures. By enforcing these requirements, the department will be able to better ensure that orphaned wells are addressed promptly and effectively.

Sincerely,



Tyler Patrick Gray, Secretary
Department of Energy
and Natural Resources



Benjamin Bienvenu,
Commissioner
Office of Conservation

Agency: Office of Conservation – Department of Energy and Natural Resources

Audit Title: Progress Report: State Efforts to Address Orphaned Oil and Gas Wells

Audit Report Number: 40230018

Instructions to Audited Agency: Please fill in the information below for each recommendation. A summary of your response for each recommendation will be included in the body of the report. The entire text of your response will be included as an appendix to the audit report.

| | |
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| Finding 1: Although more oil and gas wells are covered by financial security since OC removed most exemptions, financial security amounts are still not sufficient to cover the actual cost of plugging wells. | |
| <i>Recommendation 1: DENR should establish set time periods for review of the individual and blanket financial security amounts required by regulation to provide updated information on the discrepancy in costs and encourage increases to the required amounts at minimum to cover inflation.</i> | |
| Does Agency Agree with Recommendation? | <input checked="" type="checkbox"/> Agree <input type="checkbox"/> Disagree |
| Agency Contact Responsible for Recommendation: | |
| <i>Name/Title: Ha Louis/ Internal Auditor</i> | |
| <i>Address: 617 North Third Street</i> | |
| <i>City, State, Zip: Baton Rouge, LA 70802</i> | |
| <i>Phone Number: (225) 342-6768</i> | |
| <i>Email: ha.louis@la.gov</i> | |

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| Finding 2: OSR and LORA plugged 976 orphaned wells in fiscal years 2020 through 2023, including 396 wells that were plugged using grants from the federal government. However, despite increased plugging efforts, the number of orphaned wells continues to grow. |
| <i>There were no recommendations for DENR for this finding.</i> |

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| Finding 3: Funding limitations prevent OC from expanding the OSR Program’s efforts to plug more orphaned wells. |
| <i>There were no recommendations for DENR for this finding.</i> |

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| Finding 4: The number of inactive wells, which have a higher risk of being orphaned, increased 21.7% from 17,775 in August 2019 to 21,629 in April 2024. Although OC recently updated regulations to increase the annual inactive well |
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| fees based on the time each well has been inactive, OC does not place as many restrictions on inactive wells as some other states. | |
| <i>Recommendation 2: DENR should implement a consistent policy for granting exceptions for inactive well fees, including reasons that exceptions can be granted and the amount that fees will be reduced for each reason.</i> | |
| Does Agency Agree with Recommendation? | <input checked="" type="checkbox"/> Agree <input type="checkbox"/> Disagree |
| Agency Contact Responsible for Recommendation: | |
| <i>Name/Title: Ha Louis/ Internal Auditor</i> | |
| <i>Address: 617 North Third Street</i> | |
| <i>City, State, Zip: Baton Rouge, LA 70802</i> | |
| <i>Phone Number: (225) 342-6768</i> | |
| <i>Email: ha.louis@la.gov</i> | |
| <i>Recommendation 3: DENR should consider implementing additional restrictions on inactive wells to prevent them from remaining inactive indefinitely, such as a maximum amount of time that wells with no future utility may remain inactive, requiring review and approval of wells' classification as having future utility, requiring additional risk-based financial security for inactive wells, monitoring inactive wells' mechanical integrity, or limiting the number or percent of inactive wells that an operator can have at the same time.</i> | |
| Does Agency Agree with Recommendation? | <input checked="" type="checkbox"/> Agree <input type="checkbox"/> Disagree |
| Agency Contact Responsible for Recommendation: | |
| <i>Name/Title: Ha Louis/ Internal Auditor</i> | |
| <i>Address: 617 North Third Street</i> | |
| <i>City, State, Zip: Baton Rouge, LA 70802</i> | |
| <i>Phone Number: (225) 342-6768</i> | |
| <i>Email: ha.louis@la.gov</i> | |

APPENDIX B: SCOPE AND METHODOLOGY

This report provides the results of our performance audit of the Department of Energy and Natural Resources (DENR) - Office of Conservation's (OC) progress toward addressing issues identified in our 2014 and 2020 performance audits on the regulation of oil and gas wells and management of orphaned wells. We conducted this performance audit under the provisions of Title 24 of the Louisiana Revised Statutes of 1950, as amended. This audit covered July 1, 2019, through June 30, 2023, with the number of orphaned oil and gas wells as of April 2024. Our audit objective was:

To evaluate OC's progress toward addressing orphaned oil and gas wells.

We conducted this performance audit in accordance with generally-accepted *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

We obtained an understanding of internal control that is significant to our audit objectives and assessed the design and implementation of such internal control to the extent necessary to address our audit objective. We also obtained an understanding of legal provisions that are significant within the context of the audit objective, and we assessed the risk that illegal acts, including fraud, and violations of applicable contract, grant agreement, or other legal provisions could occur. Based on that risk assessment, we designed and performed procedures to provide reasonable assurance of detecting instances of noncompliance significant to those provisions.

To answer our objective, we performed the following audit steps:

- Reviewed the findings and recommendations of the 2014 Louisiana Legislative Auditor (LLA) performance audit of OC's management of orphaned oil and gas wells and the 2020 LLA performance audit that evaluated OC's progress toward addressing issues identified by the 2014 audit.
- Researched any updates to relevant state laws, regulations, and policies and procedures related to OC's legal authority, responsibilities, and processes for the regulation of oil/gas and orphaned wells.
- Met with OC leadership and staff to gain an understanding of its current policies and procedures related to its responsibilities for oil and

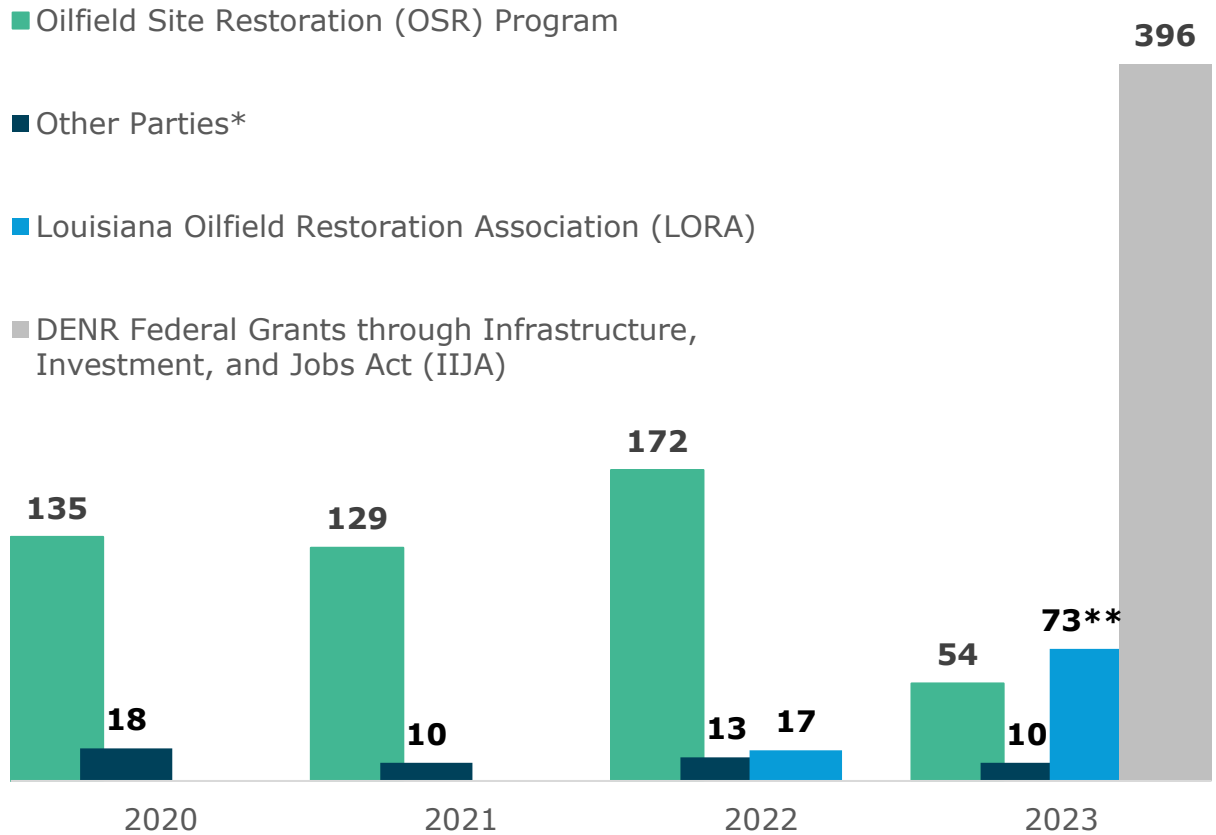
gas regulation and plugging orphaned wells through its Oilfield Site Restoration (OSR) program.

- Researched other states' practices for managing inactive wells.
- Obtained and analyzed reports from OC showing financial information, including OSR revenues and expenditures, the amounts of financial security called and collected, balances of escrow accounts with collected financial security, and annual inactive well fee invoices and payments.
- Obtained and analyzed OSR actual costs to plug orphaned wells in calendar years 2022 and 2023 to evaluate the sufficiency of OC's current financial security requirements.
- Obtained and analyzed data from DENR's Strategic Online Natural Resources Information System to evaluate active financial security; characteristics and locations of active, inactive, and orphaned wells; and the number of inactive, orphaned, and plugged orphaned wells over time.
- Conducted data reliability testing on data received from OC and found the information to be sufficiently reliable for the purposes of this audit.
- Provided our results to DENR management to review for accuracy and reasonableness and incorporated edits throughout the report as needed.

APPENDIX C: CURRENT INDIVIDUAL AND BLANKET FINANCIAL SECURITY REQUIREMENTS

| Well Depth/Number of Wells | On Land | Water (Inland Lakes and Bays) | Water (Offshore) |
|---|--------------|-------------------------------|------------------|
| Individual Financial Security Amounts Required | | | |
| Less than or Equal to 3,000 ft | \$2 per Foot | \$8 per Foot | \$12 per Foot |
| Between 3,001 - 10,000 ft | \$5 per Foot | \$8 per Foot | \$12 per Foot |
| Greater than 10,000 ft. | \$4 per Foot | \$8 per Foot | \$12 per Foot |
| Blanket Financial Security Amounts Required | | | |
| Less than or Equal to 10 Wells | \$50,000 | \$250,000 | \$500,000 |
| Between 11 - 99 Wells | \$250,000 | \$1,250,000 | \$2,500,000 |
| Greater than or Equal to 100 Wells | \$500,000 | \$2,500,000 | \$5,000,000 |
| Source: Prepared by legislative auditor staff based on OC regulations. | | | |

APPENDIX D: NUMBER OF ORPHANED WELLS PLUGGED, BY ENTITY FISCAL YEARS 2020 THROUGH 2023



* Other parties plugging orphaned wells could include the Environmental Protection Agency, U.S. Coast Guard, or one of the well's prior operators.

** This includes six wells plugged by the LORA Foundation, a charitable organization formed by LORA to request donations from oil and gas companies to plug orphaned wells.

Source: Prepared by legislative auditor's staff based on SONRIS data provided by OC.