

July 16, 2020

The Honorable Gavin Newsom
Governor of California
State Capitol Building
Sacramento, California 95814

Submitted via fax to (916) 558-3160

Dear Governor Newsom:

We are writing on behalf of the Center for Biological Diversity and Sierra Club to urge you take immediate steps to protect the public and workers in the face of what is likely to be a wave of oil and gas company bankruptcies in the coming weeks and months. Any action by oil and gas producers to use bankruptcy proceedings and other cost-cutting and restructuring efforts to evade their environmental obligations will increase the risk that pollution from improperly secured or monitored oil and gas wells will cause environmental damage. Further, the current economics of the oil and gas industry increase the risk that the costs of plugging and cleaning up these wells ultimately will be unfairly passed to the taxpayers. Finally, oil and gas producers must not be allowed to evade their worker pension and healthcare obligations.

By taking the actions described below, you can prevent or mitigate these adverse outcomes. It is paramount that the state:

- 1) Participate directly in bankruptcy proceedings of oil and gas producers to ensure that the producers retain all environmental obligations and that cleanup costs remain the responsibility of the operators—not the public.
- 2) Pursue payment from prior well operators in cases where the current operator is unable to cover the costs of remediation.
- 3) Proactively increase and accelerate well plugging and abandonment requirements to reduce air and water pollution and create jobs. Prioritize remediation of wells in and near communities and in sensitive wildlife habitat.
- 4) Increase bond requirements to ensure that oil and gas companies set aside enough financial resources to cover the full costs of remediation even if they become insolvent.
- 5) Ensure that the oil and gas industry as a whole – not taxpayers – funds the remediation of truly “orphaned” wells, by increasing the administrative fee on well owners as needed.
- 6) Avoid the accrual of additional well cleanup costs by halting approvals and permits for new oil and gas activity, including new wells and fracking permits.
- 7) Take steps to ensure that oil and gas companies satisfy their obligations to workers by honoring their pension and healthcare commitments.

As you are aware, California Resources Corporation (CRC), one of the largest oil and gas producers in the state, has filed for Chapter 11 bankruptcy, leaving the fate of its approximately 18,500 active and idle oil and gas wells uncertain.¹ Properly plugging and abandoning these wells could cost over \$1.2 billion.² Although operators are obligated to plug and abandon their wells, CRC and its creditors will undoubtedly try to shed these substantial legal liabilities wherever possible.

CRC may try to offload its wells by either creating an underfunded subsidiary burdened with these high liability wells, or by transferring the permits to an undercapitalized buyer with even less ability to pay for remediation. CRC may also attempt to use its bankruptcy proceedings to shed its environmental obligations, leaving the state to undertake expensive plugging and abandonment procedures. Allowing CRC to walk away from its cleanup liabilities would be detrimental. It would increase the risk that unattended wells will cause environmental damage and increase the risk that taxpayers would ultimately be left to pay for remediation, despite the laws in place to prevent this.

But your regulators at the California Geologic Energy Management Division (CalGEM) can participate in bankruptcy proceedings to ensure that oil companies remain bound by their safety and environmental obligations.³ The state should advocate for the public during these bankruptcy proceedings by demanding that any reorganization plan set aside adequate resources to cover the cost of meeting CRC's legal obligation to clean up its wells.⁴ Failing to set aside sufficient financial resources—for either CRC itself or for any newly created subsidiary—would render the plan infeasible and therefore legally deficient because CRC or the new company may re-enter bankruptcy if these costs are not considered.⁵ The state should also insist that whenever any wells are transferred, the transferee provide bonding that covers the true full cost of remediating the wells. The state should also assist the bankruptcy court with evaluating whether CRC's reorganization plan meets the Bankruptcy Code's requirement that a plan comply with non-bankruptcy law. For CRC to meet this requirement, the reorganization plan would have to maintain and fully fund remediation requirements under state law.⁶

¹ Williams-Derry, William, "California Schemin": California Resources Corporation's Financial Distress Raises Questions About Cleanup—and What Occidental Petroleum Knew Before the CRC Spin-Off" Institute for Energy Economics and Financial Analysis (Feb. 2020), https://ieefa.org/wp-content/uploads/2020/02/California-Schemin_February-2020.pdf p. 7.

² *Id.*, p. 8.

³ Bankrupt companies are required to operate their businesses in full compliance with all applicable non-bankruptcy laws. 28 U.S.C. § 959(b).

⁴ When confirming a reorganization plan, the bankruptcy court must verify that the plan is consistent with all non-bankruptcy laws and is feasible so as to avoid additional financial reorganization in the future. 11 U.S.C. § 1129; *see also Midlantic Nat'l Bank v. N.J. Dep't of Env'tl. Prot.*, 474 U.S. 494, 507 (1986) (property cannot be abandoned if abandonment would contravene state laws designed to protect public health and safety).

⁵ 11 U.S.C., § 1129(a)(10) (requiring that "[c]onfirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan, unless such liquidation or reorganization is proposed in the plan.")

⁶ Compliance would include the requirement to properly plug and abandon wells in a manner that will "protect oil and gas zones, [] prevent degradation of usable waters, [] protect surface conditions, and for public health and safety purposes." (Cal. Code Regs. tit. 14, § 1723(a), *see also* Pub. Resources Code, § 3208; the mandate to "isolate all oil-bearing or gas-bearing strata encountered in the well and [] use every effort and endeavor to protect any

In addition, if CRC is ultimately unable to pay for well remediation after the bankruptcy proceedings, the state should pursue payment from previous well operators with more financial resources. In contrast to other states that have struggled to shift environmental clean-up responsibilities back onto coal mining companies that spun off underfunded subsidiaries, California has the express ability to hold previous operators that have financial resources accountable for properly abandoning and plugging wells. The state may pursue funds from prior operators as far back as 1996 to cover the cost of well remediation.⁷ In CRC's case, Occidental Petroleum operated many of CRC's wells until it spun off CRC as a separate entity in 2014.

Given that CRC is likely the first of many oil and gas company bankruptcies that will occur in the coming weeks and months, state regulators should also protect the public by taking decisive action before oil and gas companies go bankrupt.

CalGEM can and should issue permit-specific orders requiring increased and accelerated well remediation now to increase the chances that operators will carry out this urgently needed work. Accelerated well remediation will benefit the environment and create jobs – and existing law requires the oil and gas operators to pay for it. CalGEM should also order operators to provide greater bonding amounts and life-of-well bonds on all existing wells to ensure that adequate financial resources for remediation are set aside before the company files for bankruptcy. In particular, the life-of-well bond requirement should apply to any entity that acquires wells from a bankrupted or near-bankrupt operator.

In addition, when wells do become orphaned, CalGEM must ensure that the industry as a whole pays for the necessary remediation, as required by existing law. The California Legislature has enshrined the “polluter pays” principle in multiple places in the Public Resource Code. Industry oversight is funded by well owner fees and it is “the policy of this state that the cost of carrying out [remediation of orphan wells] be charged to this state's producers of oil and gas.”⁸ State regulators must ensure that the industry pays for orphan well remediation through the fee on well owners (which is currently a mere 56.5 cents per barrel), through civil penalties, and through idle well management fees.⁹ Through these actions, you can ensure that the costs that must be borne by the responsible operators, and in the case of orphan wells, by the industry as a whole. It is absolutely unacceptable to allow these costs to be foisted upon the public.

Many fossil fuel companies have publicly resisted environmental responsibilities, using the threat of bankruptcy to discourage enforcement. But oil production in California is already in long-term decline. If a company cannot afford increased bonding necessary to protect the public, then it is likely already on a path towards insolvency and liquidation. Postponing the eventual just transition away from fossil fuels by propping up bankrupt companies will only worsen the

underground or surface water suitable for irrigation or domestic purposes from the infiltration or addition of any detrimental substances.” (Pub. Resources Code § 3228); and the mandate to restore the well site “to as near a natural state as practicable.” (Cal. Code Regs. Tit. 14, § 1776(a)).

⁷ Pub. Resources Code, § 3237(c).

⁸ Cal. Pub. Res. Code § 3250.

⁹ See generally, Letter to Wade Crowfoot, Secretary, California Natural Resources Agency and Uduak Ntuk, Supervisor, California Geologic Energy Management Division re: The Role of Oil Well Remediation in the State's Recovery and Economic Transition (dated June 23, 2020) (attached); Center for Biological Diversity, Well Remediation in California: Regulatory Authority and Funding Mechanisms (attached).

financial and environmental damage the state will have to face in the future. By contrast, well remediation presents a jobs opportunity and is an important piece of any just transition plan for impacted workers and communities.¹⁰ The same companies that have profited from oil and gas extraction must be held accountable for the costs of required environmental cleanup.

Finally, the state should stop issuing new drilling and fracking permits when so many operators are on the brink of bankruptcy. Continuing to expand oil and gas development only increases the number of wells that operators may walk away from.¹¹ State oil regulators have issued CRC and its affiliates permits to drill nearly 300 new wells so far this year, including 27 new permits in just the first week of July, all without conducting environmental review required by law, and knowing that bankruptcy was imminent. Approving new wells only digs the industry deeper into the hole for cleanup costs – new permits should cease immediately.

The public has subsidized the fossil fuel industry for long enough. We ask that you advocate for the public and workers before and during bankruptcy proceedings and ensure that polluters pay for the environmental degradation they caused and honor their worker pension and healthcare obligations.

Sincerely,

Kassie Siegel, Director, Climate Law Institute
Hollin Kretzmann, Senior Attorney
Center for Biological Diversity

Kathryn Phillips, Director, Sierra Club California
Nathan Matthews, Senior Attorney, Sierra Club

Cc: Wade Crowfoot, Secretary, California Natural Resources Agency
Uduak Ntuk, Supervisor, California Geologic Energy Management Division
Matthew Baker, Deputy Secretary, California Natural Resources Agency
Lisa Halko, Chief Counsel, California Department of Conservation

Enc: June 23, 2020 Letter from 30 public interest organizations with the Last Chance Alliance regarding accelerated remediation of oil and gas wells in California.

¹⁰ A recent national study estimated a total of 15.9 total jobs (direct, indirect, and induced) per million dollars spent on closing orphaned oil and gas wells. Pollin, Robert, and Shouvik Chakraborty, Job Creation Estimates Through Proposed Economic Stimulus Measures, Political Economy Research Institute (2020), <https://www.peri.umass.edu/component/k2/item/1297-job-creation-estimates-through-proposed-economic-stimulus-measures>.

¹¹ The California Council on Science and Technology estimates the total cost of oil and gas well plugging and abandonment to be over \$9.2 billion. (See CCST, Orphan Wells in California: An Initial Assessment of the State's Potential Liabilities (Jan. 2020), p. 28, Table 8, <https://ccst.us/reports/orphan-wells-in-california/publications/>)