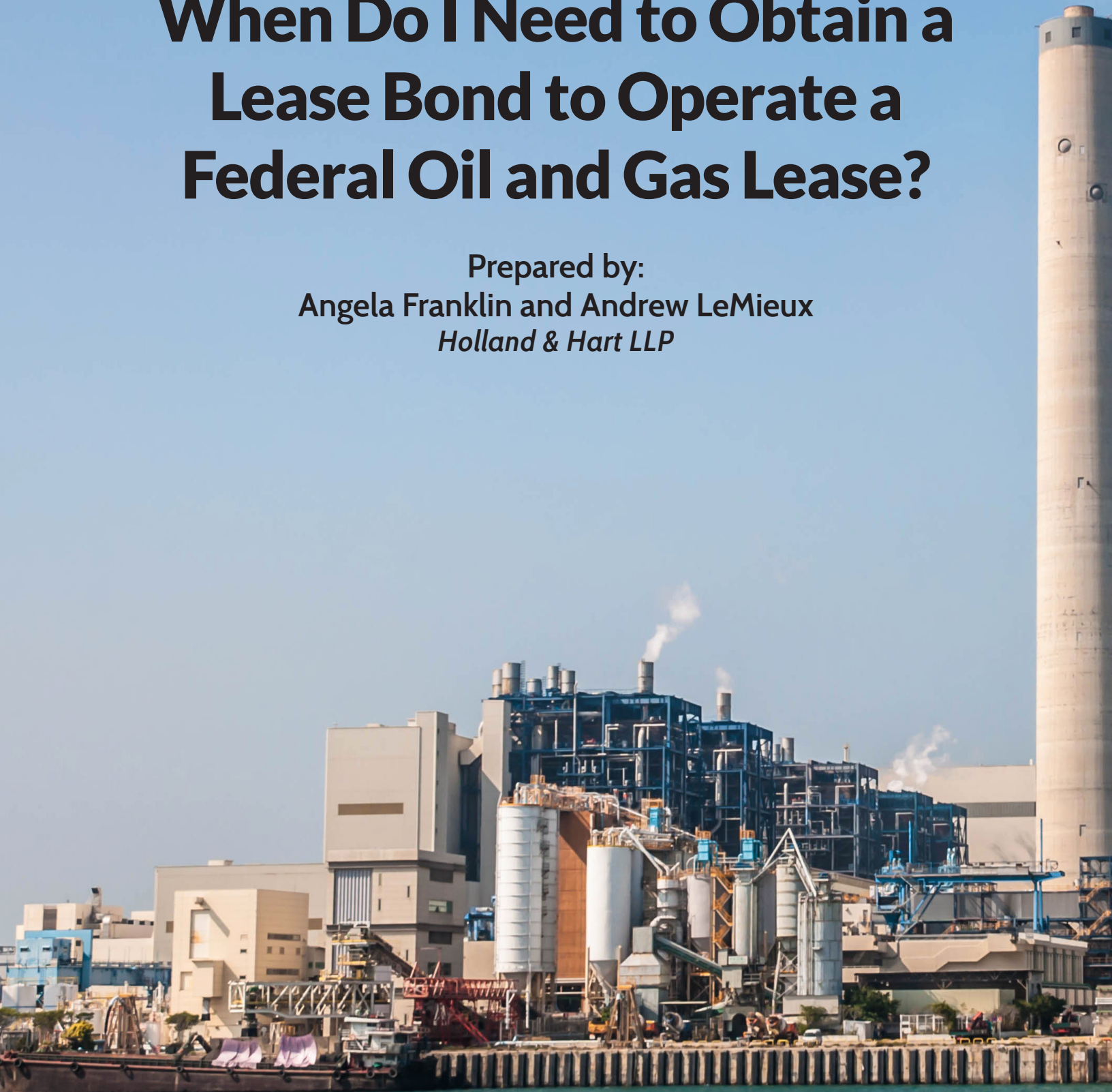


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WHEN DO I NEED TO OBTAIN A LEASE BOND TO OPERATE ON A FEDERAL OIL AND GAS LEASE?

Written by Angela Franklin and Andy LeMieux

Pursuant to the Federal Onshore Oil and Gas Leasing Reform Act of 1987 ("1987 Reform Act"), when operating on federal lands, an adequate bond (or other financial assurance) must be posted (1) before commencement of any surface disturbing activities related to drilling to ensure reclamation of lands and waters adversely affected by oil and gas operations ("lease bonds"); (2) before entry and commencement of geophysical exploration or surface-disturbing operations and for parties other than lessees before conducting geophysical exploration operations; and (3) before any surface disturbing activities for surface protection.^[1] This article focuses on lease bonds.

Lease Bonds Generally

A lease bond in an amount not less than \$10,000 for each federal oil and gas lease is required before commencement of any surface disturbing activities related to drilling operations on the lease. The bond is to ensure complete and timely plugging of the well(s), reclamation of the lands, and restoration and reclamation of the lands and surface waters adversely affected by oil and gas operations after abandonment or cessation of oil and gas operations on the

lease(s).^[2] Although the triggering event, “commencement of drilling operations,” is not defined in the regulations, in practice, the approval of an Application for Permit to Drill (“APD”) by the Bureau of Land Management (“BLM”) requires evidence of bond coverage.^[3]

The bond may be posted by the lessee (record title owner), sublessee (operating rights owner), operator, or unit operator (if applicable).^[4] An “operator” includes anyone who has assumed responsibility, in writing to the BLM, for operations conducted under a lease.^[5] The operator on the ground must have a bond in its own name as principal or be covered by a bond in the name of the lessee or sublessee, but this latter option requires the consent of the surety or obligor on the bond.^[6] A lease bond can be a surety bond^[7] or pledge backed by cash, negotiable securities, a certificate of deposit, or a letter of credit.^[8] If at least two principals have interests in different formations or portions of a lease, either separate bonds can be posted or lease operations may be covered by one bond.^[9]

Rather than a lease bond for an individual federal oil and gas lease(s), most operators post a nationwide bond in an amount not less than \$150,000 or statewide bond in an amount not less than \$25,000 covering all their operations on federal oil and gas leases in the United States or a particular state.^[10] Lease and statewide bonds and riders should be filed in the BLM State Office for the lands using Form 3000-4 (June 1988) Oil and Gas or Geothermal Lease Bond (“Form 3000-4 Lease Bond”).^[11] Nationwide bonds may be filed in any BLM State Office.^[12]

Assignments and Bonding Requirements

An assignee^[13] of a record title or operating rights interest in a lease must certify compliance with 43 CFR Subpart 3102 regarding qualifications to own an interest in a federal oil and gas lease and post any required bond.^[14] If the assignor has a lease bond and bond coverage is required, the assignee must either post a new lease bond in the assignee's name or the consent of the surety or obligor under the existing bond to become a co-principal on such bond if the assignor's bond does not already include such consent.^[15] If the assignor remains a record title owner, the assignor remains responsible for all lease obligations, including bonding requirements.^[16] If bond coverage is necessary for approval of the assignment and the assignee has a statewide or nationwide bond, no additional bond is needed but the BLM may increase the amount of the bond.

Several conditions appear in the Form 3000-4 Lease Bond. For example, Condition 2 provides a way for the BLM to increase the scope of the bond to cover subsequently acquired leases,^[17] interests, and activities of the principal as operator. Conditions 3 and 4 provide for continuing coverage of the bond notwithstanding an assignment of an undivided interest, in which event the assignee is considered a co-principal on an individual bond, or assignment of all the interest in some of the leased lands, in which event the bond remains in effect as to those lands retained by the assignor.

Until approval by the BLM of an assignment, the assignor and its surety are responsible for performance under the lease and are liable for all lease obligations.^[18] Even after the BLM approves an assignment, the assignor remains responsible for lease obligations

accruing before the approval date of the assignment, whether or not those obligations were identified before the assignment date. Those obligations include, but are not limited to, responsibility for plugging wells and abandoning facilities that the assignor drilled, installed, or used before the effective date of the assignment. In cases where the assignor is not the operator, bond coverage may be maintained by the operator.

As to any bonds maintained by the operator and a successor operator is appointed, the new operator is required to provide a replacement bond in its own name or provide evidence that the surety under the existing bond has consented to the new operator's becoming a co-principal with the prior operator under that bond.^[19] Each operator is liable to the full extent of the leasehold.^[20] Condition 6 of the Form 3000-4 Lease Bond further addresses the operator's liability for those obligations.

Bond coverage is not required for producing leases that do not contain a well but are merely receiving allocated production.

Unit Operator's Bonds

A unit operator^[21] may, but is not required to, furnish a unit operator's bond for operations on all federal oil and gas leases that have been committed to a unit agreement. The unit operator's bond is in place of, not in addition to, individual lease, statewide or nationwide bonds. The BLM determines the amount of a unit operator's bond on a case-by-case basis. If the unit operator already has a statewide or nationwide bond, coverage for the unit may be provided by a rider to that bond.^[22] The rider must specifically cover the unit and the BLM

may increase the amount of the bond. When the unit terminates, or a non-unit well is drilled (*i.e.* a well not capable of producing unitized substances in paying quantities), a lease bond must be obtained.

Conclusion

The bottom line is any drilling operations or producing wells on a federal oil and gas lease must be covered by a bond posted with the BLM. However, the principal may be the lessee record title owner, sublessee operating rights owner, or the operator, or a combination depending on the ownership in the lease and the operator of the drilling and production operations.

[1] Prior to the 1987 Reform Act, competitive leases required a bond at time of issuance and noncompetitive leases required a bond upon classification as being within a known geologic structure or prior to entry.

[2] 43 CFR § 3104.1.

[3] See Rocky Mountain Mineral Law Foundation, *Law of Federal Oil and Gas Leases*, § 17.03.

[4] 43 CFR §§ 3104.2, 3104.4.

[5] *Id.* § 3100.0-5.

[6] *Id.* § 3104.2; *Law of Federal Oil and Gas Leases*, § 17.03.

[7] A list of sureties approved by the federal government is available at https://www.fiscal.treasury.gov/fsreports/ref/suretyBnd/c570_a-z.htm.

[8] 43 CFR § 3104.1.

[9] *Id.* § 3104.2.

[10] *Id.* § 3104.3

[11] This form is currently available at <https://www.blm.gov/services/electronic-forms> in the category "Fluid and Solid Minerals, Mining Claims."

[12] 43 CFR § 3104.6.

[13] In this article, the terms "assignor," "assignee," and "assignment" include "transferor," "transferee," and "transfer."

[14] 43 CFR § 3106.2.

[15] *Id.* § 3106.6-1.

[16] See *Western States International, Inc.*, 187 IBLA 365 (2016).

[17] Except as to individual lease bond.

[18] *Id.* § 3106.7-2.

[19] 43 CFR § 3106.6-1.

[20] *Law of Federal Oil and Gas Leases*, § 17.03.

[21] "Unit operator" is defined as the person authorized under a unit agreement approved by the BLM to conduct operations on unitized lands as specified in the unit agreement. 43 CFR 3100.0-5(b).

[22] 43 CFR § 3104.4.

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