MINUTE ITEM
This Calendar Item No. 42
was submitted for information
only, no action thereon
being necessary.

INFORMATIVE CALENDAR ITEM

3/24/83
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Forderer

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ASSIGNMENT OF TASK FORCE TO STUDY THE
VALIDITY OF PROTECTION OBTAINED FROM FIXED AMOUNT OF
PERFORMANCE BONDS

At its meeting of July 22, 1982, the Commissioners expressed concern over the validity of protection obtained from fixed amount performance bonds. Several of these bonds were secured many years ago and may not allow protection at current values. Following a discussion, the Commission requested staff to look into this matter.

Research by the task force indicated that presently bonds are not being used for the purpose of which they were designed. Originally, bonds were to guarantee faithful performance under the terms of the lease and the removal of any structures at the end of the lease. Existing bonds cover only a fraction of the actual cost to remove a structure or to cover royalty payments. Any increase in bonding to current removal costs could substantially increase company costs and could have an adverse impact on revenues.

The task force decided to address this issue by researching these effects on offshore oil and gas operations, surface lease management, and hard rock mineral leases.

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For future oil and gas operations (Point Conception area) a new lease document has been designed which provides for the establishment of a fund for the removal of structures. This fund is set up so that it will expense out a certain portion of the net profits and will be deposited over the life of the lease. At the end of the lease, there will be money available for the removal of the platform. This fund will be in tandem to some type of bond since there will not be any money available at the beginning of the program. This policy pertains to new oil and gas leases since existing leases cannot be retroactively/unilaterally changed. Since new offshore oil and gas leases are being handled separately, this area was not considered a primary issue of the task force.

Presently, the task force is exploring alternatives to current bonding practices for marina operations. One method of operation being further researched is to assess a surcharge per lease suggested at one-tenth of one percent of the annual rental rather than requiring the lessee to purchase a bond. This money would be put into a fund of which a certain amount would have to be left intact to cover the State's exposure. Any excess money could be used to operate a hazard removal program or possibly to perform channel dredging. The lessee would benefit by not having to indemnify the bonding company thereby tying up real property or other assets as collateral. The State would benefit from this as well by having a ready source of funding to remove navigational hazards consistent with the stewardship of the Public Trust. The task force is also investigating the ramifications of implementing this kind of program such as the possible effects on bonding companies, the response of marina operators, or any legal problems which might be incurred, etc.

The task force has yet to address the hard rock mineral issue.