



Federal Financial Responsibility Demonstrations for Owners or Operators of Class II Oil- and Gas-Related Injection Wells

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Purpose and Disclaimer

The Safe Drinking Water Act (SDWA) provisions and U.S. Environmental Protection Agency (EPA) regulations cited in this document contain legally binding requirements. This guidance is intended to provide information and suggestions that may be helpful for implementation of such requirements. In several chapters, this guidance document makes suggestions and offers alternatives that go beyond the minimum requirements indicated by the Class II UIC regulations, although consistent with the discretion accorded therein. Such suggestions are prefaced by “may” or “should” and are to be considered advisory. They are not required elements of the rule. Therefore, this document does not substitute for those provisions or regulations, nor is it a regulation itself, so it does not impose legally binding requirements on the EPA, states, or the regulated community. The recommendations herein may not be applicable to each and every situation.

While the EPA has made every effort to ensure the accuracy of the discussion in this document, the obligations of the regulated community are determined by statutes, regulations or other legally binding requirements. In the event of a conflict between the discussion in this document and any statute or regulation, legally binding requirements take precedence.

1. Introduction

The U.S. Environmental Protection Agency (EPA) established the Underground Injection Control (UIC) program under the authority of the Safe Drinking Water Act of 1974 (SDWA). For states, tribes, or territories that have not been authorized to administer the program, the EPA is required by the SDWA to implement it. As part of this program, the owners or operators of Class II injection wells associated with oil and gas production must "maintain financial responsibility and resources to close, plug, and abandon the underground injection operation in a manner prescribed by the Director" (40 CFR 144.28(d) and 144.52(a)(7)).¹ Setting aside financial resources is intended to ensure adequate protection of underground sources of drinking water and prevent the general public from bearing the costs of plugging abandoned injection wells.

In the states, tribes, and territories where the EPA administers the program, Class II well owners or operators must satisfy the financial responsibility requirement by submitting proof of a financial instrument that meets the approval of the UIC Program Director. For UIC Programs administered by the EPA, the UIC Program Director is the EPA Regional Administrator or his/her delegate. Owners or operators may be eligible to use one of several types of instruments to maintain adequate financial resources to properly close, plug, and abandon an injection well. Options may include surety bonds, trust funds, letters of credit, independent third-party insurance, and other cash-based accounts, as well as self insurance.

This guidance is a revision to the original Class II Financial Responsibility Guidance document issued in 1990. The guidance was primarily revised to address the Miscellaneous Receipts Act requirements by removing the EPA from financial instruments as beneficiary. Additionally this revised guidance provides information and recommendations for establishing financial responsibility demonstrations that are more consistent with updated knowledge and expertise in the area, and that place new emphasis on financial stability of third party providers. Any financial demonstrations that are established or renewed after the issuance of this document should follow the recommendations herein.

This introduction describes the audience for and purpose of the guidance and introduces options available to owners or operators to demonstrate financial responsibility.

A. Who Should Read This Guidance?

This guidance only pertains to the owners or operators of Class II injection wells in states, territories and Indian lands where the EPA administers the UIC program. These programs are termed "direct implementation" programs.² (A list of direct implementation states is presented in Appendix A.) Owners or operators of both rule-authorized and permitted wells must meet financial responsibility requirements.

¹ The UIC program regulations are found in Parts [124](#), [144](#), [145](#), [146](#), and [147](#) of Title 40 of the Code of Federal Regulations (CFR). For the UIC regulations related to Class II financial responsibility see Appendix C.

² The authority to run a state program is called "primacy." States that have such authority are called "primacy states."

The EPA prepared this guidance to help Class II injection well owners or operators in direct implementation states comply with the UIC program's financial responsibility demonstration requirements. The guidance discusses:

- Financial responsibility options,
- Types of financial instruments,
- Selection of a financial responsibility instrument,
- Conditions of coverage, and
- Submission requirements.

In addition, the guidance explains the criteria and guidelines the EPA uses to evaluate the financial responsibility demonstrations that Class II well owners or operators may make. The EPA works closely with each applicant to evaluate each financial demonstration. Financial services providers may also find this guidance helpful in advising clients who own or operate Class II wells.

Owners or operators of hydraulic fracturing wells using diesel fuel should also review the section on financial responsibility in the guidance "Permitting Guidance for Oil and Gas Hydraulic Fracturing Activities Using Diesel Fuels."³ As Class II wells, hydraulic fracturing wells using diesel fuel are subject to the requirements established by 40 CFR 144.52, as established in permit conditions. Owners or operators may refer to the financial responsibility section of the above-referenced guidance for recommendations specific to hydraulic fracturing wells.

B. Financial Responsibility Options

To construct and operate a Class II well, an owner or operator must demonstrate and maintain financial responsibility, which should be equal to the cost of hiring an independent third-party firm to close, plug, and abandon the well (see Section 3.A "Estimate Plugging Costs"). There are several ways that owners or operators can meet the requirement to demonstrate financial responsibility for well closure. However, not every option may be open to all Class II injection well owners or operators depending on their individual circumstances and record of compliance with the EPA regulations.

The instruments used to demonstrate financial responsibility may be grouped into two categories: independent third-party financial instruments and self insurance (sometimes referred to as a financial statement demonstration).

- Independent third-party financial instruments are agreements such as surety bonds, letters of credit, and trust funds. They rely on a third party such as a bank or surety company to guarantee (1) that a specified amount of money will be available to plug and abandon wells when necessary, or (2) that the actual job of closure will be accomplished.

³ Underground Injection Control Program Guidance #84 on hydraulic fracturing is available online at <http://water.epa.gov/type/groundwater/uic/class2/hydraulicfracturing/hydraulic-fracturing.cfm>.

- Owners or operators using self insurance submit data that demonstrate the financial strength of their companies; these demonstrations should include an auditor's opinion for confirmation.

Readers should note that financial instruments developed in response to state oil and gas requirements may not necessarily be sufficient to meet federal UIC financial demonstration requirements. Owners or operators should obtain the express approval of the EPA regional office in question in order to rely on such instruments. If owners or operators are unsure whether they must comply with these financial requirements or with the UIC regulations, they should contact the EPA office in the Region where their wells are located. Appendix B provides information on how to identify EPA's regional offices, their addresses, telephone numbers, and the states they oversee.

2. Financial Responsibility Demonstrations

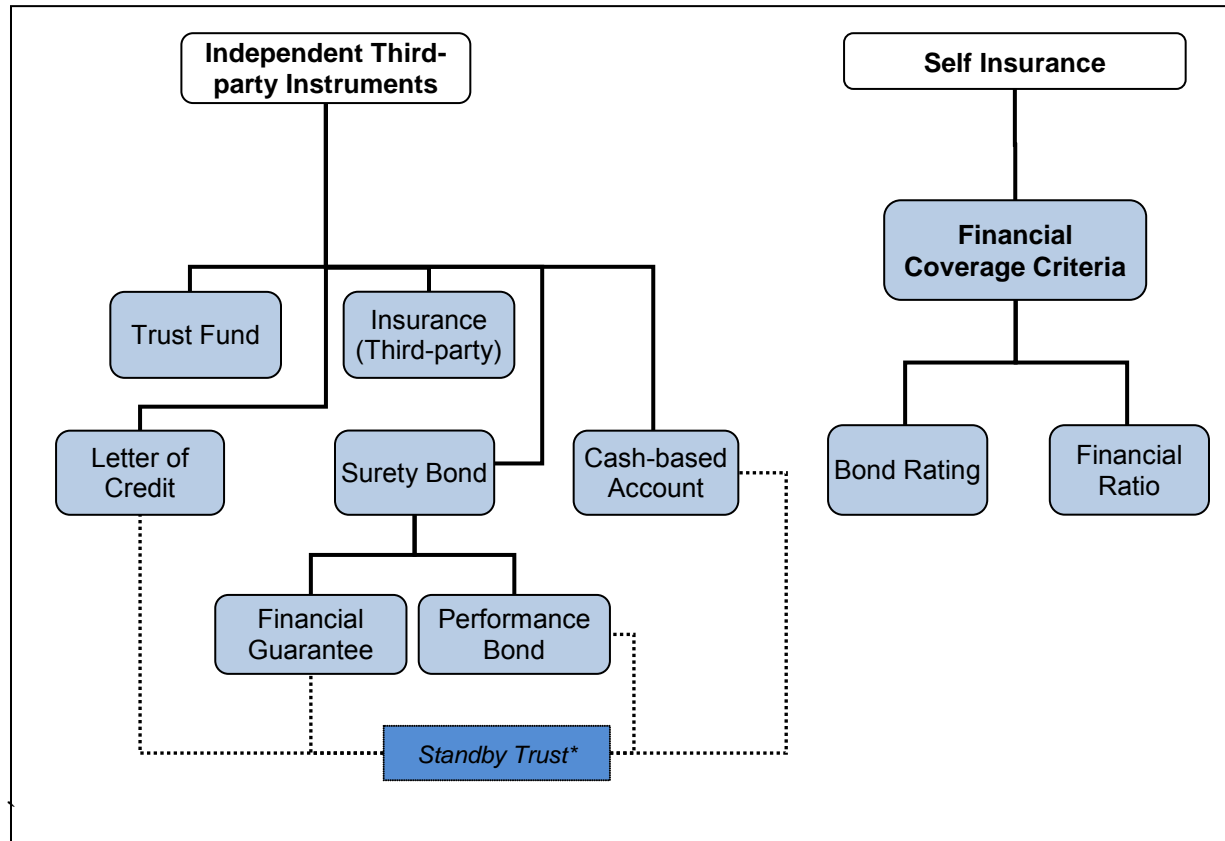
The federal regulations at 40 CFR 144.28(d) require that owners and operators demonstrate and maintain financial responsibility “in a manner prescribed by the Director.” As such, options for demonstrating financial responsibility may include third-party instruments or self insurance. However, some financial responsibility options might not be available or appropriate depending on the individual project.

1. Independent third-party instruments. These financial instruments rely on an independent third-party institution’s guarantee to provide funds sufficient to cover the total cost of hiring an independent third party to properly close, plug, and abandon injection wells or to directly perform such financial responsibility activities.
2. Self insurance. This financial instrument may be available to owners or operators if they pass the self insurance requirements described in Section 2.B “Self Insurance.” This option allows owners or operators to submit financial statements and other information that show they are likely to remain in operation, based on indicators of the economic health of the organization, and that they will be able to properly plug and abandon their wells.

The following sections provide details on EPA’s recommendations for financial instruments that can be used for specific coverage options. Section A “Independent Third-Party Financial Instruments” describes financial instruments that owners or operators can use in financial responsibility demonstrations. Section B “Self Insurance” describes EPA’s recommendations for qualifying for self insurance coverage. Section C “Use of a Financial Instrument for Multiple Facilities” describes EPA’s recommendations for qualifying for a single instrument to provide financial responsibility for multiple facilities. Finally, Section D “Other Qualifying Financial Instruments” describes other instruments that may qualify as methods for financial demonstration with the UIC Program Director’s approval.

Figure 1 “UIC Financial Responsibility Demonstrations” provides a graphical representation of the financial instruments that are potentially available to owners or operators.

Figure 1: UIC Financial Responsibility Demonstrations



**Not a stand-alone instrument. Dotted connection to standby trust from letter of credit, financial guarantee, performance bond, and cash-based accounts represents the recommendation for a standby trust when the EPA is the UIC Program Director.*

A. Independent Third-Party Financial Instruments

This section includes descriptions of qualifying third-party financial instruments as well as EPA's recommendations for each.

Trust Funds

An irrevocable trust fund is an instrument available to owners or operators to demonstrate financial responsibility. Trust funds are repositories of money set aside for a specific purpose. They are administered by a trustee designated by the grantor who establishes the trust. If an owner or operator uses a trust fund, the instrument should have a value equal to the full estimated cost of properly plugging the wells covered by the instrument. Income generated by the fund's investments is added to the trust.

The EPA has established recommendations for trust funds offered by Class II well owners or operators as demonstrations of their financial responsibility. These trusts should:

- Be established at a bank or other institution with authority to act as a trustee and whose trust activities are examined and regulated by a state or federal agency,⁴
- Contain funds equal to the estimated cost of plugging the wells covered by the trust (except when pay-in period plans are authorized by the UIC Program Director, as discussed on the following page),
- Specify the acceptable ways the trustee can invest the fund's money,
- Be accompanied by a "certificate of acknowledgement-" a notarized statement that attests that the trust was established at the direction of their corporation's board of directors or principal owners.

The financial institutions with which owners and operators normally do business with should be able to help establish a trust fund for plugging and abandonment, either serving as the trustee or directing owners or operators to another institution that can serve in that capacity. See Table 1 “Trustee Selection and Responsibilities” for EPA’s recommended guidelines for establishing a trustee.

Table 1: Trustee Selection and Responsibilities

Selecting a Trustee
<ul style="list-style-type: none"> • The selected trustee should be a neutral party whose connections to the owner or operator do not pose any potential for a conflict of interest. (The bank that the owner or operator normally does business with is an example of a neutral trustee.) • The trust should be established at a bank or other institution that has authority to act as a trustee. • Although some states authorize attorneys to serve as trustees, the attorney who represents the owner or operator could present a potential conflict of interest, and consequently, would not be an acceptable trustee.
Responsibilities of a Trustee
<p>As the grantor, the owner or operator should name a trustee whose responsibilities will include:</p> <ul style="list-style-type: none"> • Investing deposited funds with the owner or operator’s guidance and in accordance with provisions of the trust and applicable legal principles, • Providing the EPA with an annual valuation of the fund, and • Accepting additional deposits or releasing funds as the owner or operator drills new wells or plugs old ones with the approval of the EPA.

⁴ For the most up-to-date inventory of FDIC-insured banks nationwide, see <https://www.fdic.gov/>.

As wells are plugged, the UIC Program Director may approve payments from the fund to reimburse owners or operators for the cost of plugging, or the UIC Program Director may delay payments until all the wells covered by a trust are plugged and certified. The latter case is generally used if it appears, when plugging starts, that the entire operation may cost more than the trust fund contains. The EPA may also exercise its discretion to approve refunds if:

- The value of the trust fund exceeds the estimated plugging costs,
- The owner or operator substitutes another financial instrument for the trust fund, or
- Funds remain in the trust after the owner or operator has satisfactorily plugged the wells covered under the instrument.

Pay-in Period

Owners or operators who enter into administrative orders on consent with the EPA may have the option of developing payment plans under which they fund some instruments over a period of time, called a pay-in period. Some of the relevant instruments that use pay-in plans are trust funds and cash-based accounts. However, while longer pay-in periods reduce the up-front financial burden for the owner or operator, they also increase the risk that the instrument will fail if the owner or operator cannot meet its obligations.

To minimize risk of instrument failure, the EPA recommends that the UIC Program Director exercise his or her discretion in allowing a pay-in period that establishes the shortest pay-in periods possible. The UIC Program Director may also determine that a pay-in period is not desirable and may require that the trust fund or cash-based account be fully funded at its inception. Third-party providers of other instruments may also require up-front payment, completely foregoing pay-in periods. Further, the Director may also exercise its discretion to revoke the permit if the owner or operator does not meet the pay-in period schedule agreed upon. Owners or operators may be able to reduce the financial burden of shorter pay-in periods or up-front payments by obtaining third-party financing.

Standby Trust Funds

The EPA is subject to the Miscellaneous Receipts Act, 31 U.S.C. 3302, which requires the EPA to deposit money it receives into the U.S. Treasury unless a federal statute authorizes the EPA to retain the funds. The EPA must have statutory authorization to be the beneficiary of a trust or insurance policy. Because the SDWA does not give the EPA such authorization, financial instruments cannot be used to distribute funds directly to the EPA or name the EPA as the beneficiary of a trust or insurance policy. Therefore, if owners or operators choose to use a surety bond, letter of credit, or cash-based account to demonstrate their financial responsibility, they should also establish a standby trust fund.

A standby trust is different from a trust fund because the trust is unfunded (or in standby) until another financial instrument pays into it. Owners or operators may not use a standby trust as a standalone financial instrument. Instead, a standby trust fund exists solely as a mechanism to receive, on behalf of the EPA, the funds guaranteed if an owner or operator does not plug injection

well(s) properly. As a financial responsibility instrument, the standby trust allows the UIC Program Director to request the use of funds guaranteed by other instruments. For example, when funds are collected from letters of credit, surety bonds, and other cash-based accounts, they are moved to the standby trust, where they can be withdrawn and allocated to an independent third party to cover the costs associated with plugging and abandonment.

The standby trust agreements must be written such that the EPA, as the UIC Program Director, has the express authority to notify the trustee of the need for payments from the fund to cover the costs of activities covered under the agreement.⁵ Along with the standby trust agreement, owners or operators should provide a list of wells covered by the standby trust to the UIC Program Director. Owners or operators should revise the list of wells as necessary to accurately specify the wells covered by the standby trust. As with trust funds, trustees are required for standby trust funds and they have the responsibilities described in Table 1.

Surety Bond

A surety bond is a guarantee by a surety company that specified obligations, such as plugging and abandonment of Class II injection wells, will be fulfilled. There are two types of surety bonds: performance bonds and financial guarantee bonds. A performance bond guarantees the performance of the financial responsibility activities. For example, a performance bond might give the surety three options to guarantee and finance the completion of a project: completing the project itself, hiring a contractor to complete the project, or paying the amount of funds guaranteed by the bond. On the other hand, a financial guarantee bond, also commonly referred to as a payment bond, ensures that the surety company will pay the amount of funds guaranteed by the bond. Both types of surety bonds should have a standby trust to receive, on behalf of the UIC Program Director, any money that the surety company is required to pay to cover the cost of financial responsibility activities implemented by an independent third party.

Owners or operators who want to use either type of surety bond to demonstrate their financial responsibility should submit to the EPA both the bond and the standby trust agreement. In addition, the surety bond, whether it is a financial guarantee bond or a performance bond, should meet certain conditions. The bond should:

- Be issued by a surety company that has been tested and approved under the U.S. Department of the Treasury Circular 570 (<https://www.fiscal.treasury.gov/fsreports/ref/suretyBnd/c570.htm>). The EPA regional offices can provide a list of approved companies, and insurance brokers can also provide advice.
- Specify the wells that the bond covers. If owners or operators drill or acquire new wells, they must either post a new bond or amend the existing demonstration.
- Guarantee that, if an owner or operator fails to properly plug specified wells, the surety company will pay the amount of the bond into a standby trust fund.

⁵ When a state or tribe is the UIC Program Director, the surety bond may name a state, tribal, or local government as a recipient of funds or a beneficiary, if authorized by applicable law. In this case a standby trust may not be needed.

Depending on the permit's scope, owners or operators can secure a surety bond for either a single well (i.e., single well bonding) or a multi-well facility (i.e., multiple well bonding). In the case of multiple wells, the UIC Program Director may require that the face value of the bond reflect the sum of the costs of all the wells. Owners or operators should submit proof of the bond to the UIC Program Director. Typically, the cost of the surety bond depends on the cost estimate for the activity (e.g., one well or multiple wells) as well as the associated risk and the type of surety bond (performance or financial guarantee).⁶

Letter of Credit

A letter of credit guarantees that a set amount of money will be available to a specified party under certain conditions. The letter of credit should use a standby trust to facilitate the transfer of funds to complete the activity, and it must provide that funds will be paid into a standby trust if the UIC Program Director determines that it is necessary to draw upon the letter of credit. The actual letters of credit should be submitted as proof of financial responsibility and should:

- Be issued by a bank or other institution whose operations are regulated and examined by a state or federal agency. Most commercial banks and some savings and loan institutions and credit unions are the usual sources of this financial instrument. Owners or operators should also demonstrate the issuing institution's financial stability to the UIC Program Director.
- Identify, by their number and project name, the specific wells covered by the letter of credit. Owners or operators should revise the list of wells as necessary to accurately specify the wells covered by the letter of credit.
- Guarantee that, if the owner or operator fails to properly plug specified wells, the issuing institution will pay the amount of the letter of credit into a standby trust fund.
- Provide that the UIC Program Director may draw upon the letter of credit under the conditions specified in this guidance (see Section 4 "Conditions of Coverage and Specifications for Financial Responsibility Demonstrations").

Independent Third-Party Insurance

Independent third-party insurance is a contract between the insurer (typically an insurance company) and the insured (the Class II well owner or operator) written in the form of an insurance policy for plugging and abandonment activities. Independent third-party insurance demonstrations require that there is no ownership relationship between the insurance company and the insured party.⁷ Generally, the insurance company directly pays for an independent party to complete the activities covered by financial responsibility, as requested by the UIC Program Director. The terms of the insurance policy can vary among, and even within, states.

⁶ Since the EPA cannot liquidate property, such as equipment, to secure cash, "collateral bonds" are not accepted.

⁷ Captive insurance, an insurance policy underwritten by a subsidiary to insure its own parent company or a client of a parent company, is not considered a third-party insurance demonstration.

The independent third-party insurance demonstration should include a copy of the insurance policy and a signed certificate of insurance. The certificate of insurance should include, at a minimum, the following information:

- Name and address of the insurer and insured.
- A list of the injection wells covered by the policy and their respective the EPA identification number, name, and address. The list should also specify the amount of insurance required for each well, and these amounts for all injection wells covered should total the face amount of the insurance policy.
- The face value of the insurance policy, which should be at least equal to the independent estimate of the cost of plugging and abandoning the well(s) covered by the policy.
- The policy number and effective date.

Other Cash-Based Accounts (e.g., Certificate of Deposit and Escrow Accounts)

Other acceptable financial instruments include cash-based accounts, such as certificates of deposit (CDs) and escrow accounts. Due to the restrictions of the Miscellaneous Receipts Act, the owner or operator should also create a standby trust. If the obligations are not met, the funds will be paid to the standby trust for an independent third party, (i.e., an entity with no direct relationship with the owner or operator) to fulfill the obligations as requested by the UIC Program Director. CDs and escrow accounts set aside funds for a particular time period or to be used for an explicit purpose and can be used to deliver funds from one party to another.

Cash-based accounts may yield interest over time. If interest is earned and the revised cost estimate for plugging and abandoning the well (including adjustments for inflation) shows that the amount held in the instrument exceeds the most recent estimated cost (assuming management fees due to the trustee have been paid), the owner or operator may request the UIC Program Director's approval for release of the excess funds. The UIC Program Director should not release funds from the instrument if the value of the account falls below the cost estimate.

The EPA recommends that the escrow agreement describe the acceptable ways that the escrow agent can invest the funds, show proof that the account was established at the direction of the owner or operator's board of directors or principal owners, and identify the conditions under which the escrow agent will release funds to fulfill required Class II activities. The EPA recommends that the agreement also stipulate that the escrow agent submit statements with the value of the escrow account (at least annually) to the UIC Program Director, invest the money in the fund according to the guidance provided in the agreement and applicable legal principles, and accept additional deposits or release funds with the approval of the UIC Program Director.

B. Self Insurance

Unlike independent third-party instruments, financial responsibility demonstrations with self insurance involve only the owner or operator (and the parent company in the case of a corporate guarantee). To use self insurance, owners or operators should receive approval from the UIC Program Director. In assessing whether an owner or operator may rely on self insurance to demonstrate financial responsibility, the UIC Program Director should consider the following two recommended factors for identifying financially healthy companies:

1. The owner or operator meets EPA’s coverage criteria identified in Table 2 “Financial Coverage Criteria” and
2. The owner or operator pass a financial test by meeting the criteria for either the bond rating alternative *or* the financial ratio alternative.

If the owner or operator fails to meet these recommended criteria or does not receive approval from the UIC Program Director, the owner or operator should submit to the EPA an alternative financial instrument to demonstrate financial responsibility.

The self insurance demonstration should be made on a form provided by the UIC Program Director. It should include the form letter, which the company’s chief financial officer (CFO) or another legally authorized person should provide, certifying that the company meets EPA's financial requirements for making a self insurance demonstration of responsibility. In addition, the owner or operator should verify to the EPA that the information contained in the CFO’s letter is accurate. Although there are many types of auditor’s analyses of financial data, the EPA recommends that the UIC Program Director accept only an auditor’s full opinion as confirmation of the accuracy of financial information and proof that a company passes this test. Reports that are based on full-scale audits are acceptable because the EPA considers them the functional equivalent to an auditor’s opinion. The EPA recommends that an owner or operator do this by providing one of the following:

- An auditor’s full opinion from an independent certified public accounting firm that verifies the accuracy of the financial data used in the letter,
- A "glossy" financial statement based on full-scale audits, such as those routinely prepared as reports to stockholders,
- A 10K report, which is submitted annually to the Securities and Exchange Commission (or a link to a 10K report if available online), or
- A Federal Energy Regulatory Commission (FERC) Form 2 Report.

Factor 1: Coverage Criteria

Table 2 describes the EPA’s recommended coverage criteria for determining if owners or operators qualify for the financial test. Owners or operators that meet all of the EPA's criteria in Table 2 may proceed to the bond rating alternative or the financial ratio alternative to determine whether they qualify to use self insurance to demonstrate financial responsibility.

Table 2: Financial Coverage Criteria

Criterion	Explanation
Has a good history of plugging wells and compliance with the EPA requirements	Has the owner or operator plugged wells in accordance with applicable regulations in the past and has the owner or operator maintained a good record of compliance with other EPA requirements? If so, the EPA believes the owner or operator is likely to do so in the future.
Has at least five years of remaining economic life of production fields or leases ⁸	Is the owner or operator producing from at least one field or does the owner or operator have at least one lease in the state or territory with an estimated remaining economic life of at least five years? If so, the EPA believes the owner or operator is likely to remain in business until the Agency conducts its periodic reviews.
Has been in business at least five years	Has the owner or operator been in the oil and gas business at least five years? The owner or operator's financial performance will have more significance if the answer is yes.
Operates multiple production fields	Is the owner or operator producing from more than one field in a state or territory? If so, then the owner or operator is less likely to deplete all his or her financial resources at the same time. Consequently, the owner or operator is more likely to be in business when the EPA conducts its periodic reviews.
Meets the requirement for minimum net worth ⁹	Does the owner or operator have a minimum net worth of \$2 million? If so, then the company may be eligible to use self insurance.

Factor 2: Financial Test

If the Director approves the financial coverage criteria submitted by the owner or operator, the Director should then evaluate the self insurance demonstration based on the bond rating alternative or a set of five financial ratios. In principle, this process confirms that the company presents a low risk because it is profitable, is not overly leveraged, and has sufficient liquidity.

Bond Rating Alternative

If the company has issued bonds to raise capital, its bond rating may be high enough to pass the EPA's recommended financial test. In order to pass, the most recent bond rating should be within the four highest categories of Standard and Poor's (AAA, AA, A, or BBB) or Moody's (Aaa, Aa, A, or Baa). If the company passes the bond rating standard and decides to use self insurance to demonstrate financial responsibility, it should submit annually to the EPA a statement of the operation's Standard and Poor's or Moody's bond rating using the model format of the CFO's letter provided by the UIC Program Director.

Financial Ratio Alternative

Table 3 describes the recommended financial ratio criteria for the company to pass this test.

⁸ The economic life of any asset (e.g., a production field or lease) is the length of time during which the present value of current and future benefits of the asset exceeds the present value of current and future costs.

⁹ The EPA increased the minimum net worth criterion from \$1 million to \$2 million to account for inflation since the issuance of the previous guidance in 1990. See: US Bureau of Labor Statistics http://www.bls.gov/data/inflation_calculator.htm

Table 3: EPA List of Financial Ratios and Thresholds

The EPA recommends that applicants meet the five ratios/thresholds (below) and the financial coverage criteria listed in Table 2.

Type of Ratio	Formula	Threshold
1) Debt-Equity Ratio	$\frac{\text{Current Liabilities}}{\text{Net Worth}}$	< 1.0
2) Debt-Equity	$\frac{\text{Long Term Liabilities}}{\text{Net Worth}}$	< 2.0
3) Liquidity	$\frac{(\text{Current Assets} - \text{Current Liabilities})}{\text{Total Assets}}$	> -0.10
4) Cash Return on Liabilities	$\frac{(\text{Net Income} + \text{Depreciation} + \text{Depletion} + \text{Amortization})}{\text{Total Liabilities}}$	> 0.10
5) Net Profit	Revenues – Expenses	> 0

Corporate Guarantee

A company that is a subsidiary should submit its parent company's financial statements for the coverage criteria and financial test only if the parent company guarantees to pay to plug its subsidiary's wells. The parent corporation should own at least 50 percent of the subsidiary's voting stock. For the financial responsibility demonstration, the parent company should provide a specific written guarantee made by a corporate officer authorized to legally bind the parent company that meets self insurance requirements. The written guarantee should explicitly state that the corporation will continue to honor the guarantee regardless of any ownership restructuring (e.g., sale of the owner or operator as an independent company). No company, except for the parent company, with a substantial business interest in the owner or operator's firm should provide a corporate guarantee. The EPA recommends that if a joint-ownership venture is formed among multiple firms or owners or operators, the financial responsibility demonstration and financial guarantee should be made by one party as the primary parent.

C. Use of a Financial Instrument for Multiple Facilities

Generally, an owner or operator can use a specified financial responsibility instrument for more than one injection well. The EPA recommends that evidence of financial responsibility submitted to the UIC Program Director include a list showing, for each injection well, the EPA identification number, name, address, and the amount of funds assured by the instrument. If the injection wells covered by the instrument are in more than one state or the EPA Region, the EPA recommends that identical evidence of financial responsibility be submitted to and maintained with the UIC Program Directors of all such states or Regions. The amount of funds available through the instrument should be no less than the sum of funds that would be available if a separate instrument had been established and maintained for each injection well. In directing funds available through the instrument for any of the injection wells covered by the instrument,

the UIC Program Director should direct only the amount of funds designated for that injection well, and if the designated funds are insufficient, the UIC Program Director can request that the owner or operator increase the value of financial assurance.

D. Other Qualifying Financial Instruments

The UIC Program Director may approve the use of financial instruments other than those specifically described in the guidance. Following the UIC Program Director's determination that the instrument is satisfactory, owners or operators can use these other qualifying instruments to demonstrate financial responsibility.

If approved by the UIC Program Director, owners or operators may also have the flexibility to use a combination of instruments to demonstrate financial responsibility. If an owner or operator uses a combination of instruments, the sum of the coverage provided by these instruments should be at least equal to the current cost estimate for plugging and abandonment activities.

3. Preparing a Submission

To prepare a financial responsibility demonstration, owners or operators should:

- Estimate their total plugging costs (This is a requirement for the plugging and abandonment plan under 40 CFR 144.28(c) for rule-authorized wells.),
- Select the financial instruments best suited to their operations, and
- Obtain and submit the appropriate information and financial instruments.

The following sections describe each of these steps.

A. *Estimate Plugging Costs*

Prior to obtaining financial responsibility, an owner or operator should submit the required plugging and abandonment plan for all wells¹⁰, including an estimate of the cost to plug and abandon the wells, and receive EPA's approval. To determine the appropriate level of financial responsibility for the plugging and abandonment plan, an owner or operator should obtain a cost estimate from an independent third-party firm in the business of plugging wells. The estimates should be based on a "turn key" plugging operation and should include the costs of all the materials and activities necessary to pay an independent third-party contractor to completely plug and abandon a well. The value of the financial instrument should meet the estimated cost of plugging the well(s) given in the owner or operator's EPA-approved plugging and abandonment plan (EPA Form 7520-14). The UIC Program Director may require periodic updates of the cost estimate as well as a revised demonstration of financial responsibility to reflect higher plugging and abandonment costs or the addition of new wells (40 CFR 144.28(d)(3) for rule-authorized wells and 144.52(a)(7)(ii) for permitted wells).

B. *Choosing a Financial Instrument*

After obtaining an estimate of the cost to plug and abandon the covered wells, owners or operators should select a financial responsibility instrument for which they believe they can qualify. At this point, owners or operators may want to review the various instruments available to them and consult with various providers of financial instruments such as banks and surety companies. These providers can help identify the most cost-effective instrument. Owners' or operators' insurance agents should have information about surety bonds including their availability, cost, and collateral requirements, if any.¹¹ Banks, savings and loans, and similar institutions can inform owners or operators about letters of credit and trust funds.

The cost of financial instruments varies depending on a number of factors. As owners or operators evaluate different instruments, they should keep in mind these cost elements: fees or premiums, collateral requirements, tax consequences, possible effects on their credit rating, and opportunity cost. Issuing institutions may require the payment of premiums annually, monthly,

¹⁰ EPA Form 7520-14; available at <http://water.epa.gov/type/groundwater/uic/reportingforms.cfm>

¹¹ Since the EPA cannot liquidate property such as equipment to secure cash, "collateral bonds" are not accepted.

or, in some instances, entirely up front before coverage begins. The cost of instruments will also depend on the issuing institution's evaluation of the risks involved with the operations.

If owners or operators request permission to use self insurance, they should prove to the EPA with the appropriate documentation that they meet the financial coverage criteria and the financial test described in Section 2.B ("Self Insurance") to the satisfaction of the UIC Program Director. The UIC Program Director may also allow the use of a single financial responsibility instrument for multiple facilities, but owners or operators should meet the recommendations outlined in Section 2.C ("Use of a Financial Instrument for Multiple Facilities").

C. Demonstrating Financial Responsibility

Once owners or operators have selected a financial instrument, they should gather the necessary information and documents and submit them to the EPA. This step may require owners or operators to obtain a bond from a surety agent, request financial statement information from their accounting department, or obtain a letter of credit and standby trust agreement from a bank. For the Class VI financial responsibility guidance, the EPA developed sample forms and templates of third-party instruments that can also be used as templates for Class II financial responsibility demonstrations.¹² If the owner or operator cannot submit the information necessary to verify its qualification for the selected demonstration to the satisfaction of the UIC Program Director, the EPA may require the owner or operator to choose another option.

For third-party instruments, the EPA recommends that owners or operators demonstrate the financial stability of their third-party providers and provide proof of the issuing institution's financial strength. The EPA recommends that owners or operators submit the third party's credit rating or, if requested by the UIC Program Director, the third party's credit rating plus its most recent bond rating and calculated financial ratios, as presented in Table 3 ("EPA List of Financial Ratios and Thresholds"). The EPA recommends that owners or operators demonstrate that third-party providers have a credit rating or bond rating in the top four categories from either Standard & Poor's or Moody's (i.e., AAA, AA, A, or BBB for Standard & Poor's and Aaa, Aa, A, or Baa for Moody's) or from any nationally recognized statistical rating organization (NRSRO) as long as the owners or operators can demonstrate the equivalency of this rating with the recommended ratings.

The EPA regional office should not begin the evaluation of an owner or operator's submission until all the necessary certifications and representations are received. If submitted items and information meet EPA's criteria and receive the EPA's approval, then an owner or operator has met the obligation to demonstrate financial responsibility.

¹²These documents are listed under the heading "Recommended Financial Responsibility Instrument Language (Forms/Templates)" and are available on line at: <http://water.epa.gov/type/groundwater/uic/class6/gsguidedoc.cfm>.

4. Conditions of Coverage and Specifications for Financial Responsibility Demonstrations

This chapter describes the minimum conditions needed to assure that financial responsibility demonstrations will provide coverage for injection well plugging and abandonment. The EPA recommends that these conditions of coverage and specifications be discussed with the owner or operator's Chief Financial Officer (CFO) and with the various providers of financial instruments such as banks and surety companies, as appropriate.

A. Recommended Coverage Conditions for Instruments

Owners or operators should renew all financial instruments for the entire term of the project. The instruments may be automatically renewed as long as the owner or operator has the option of renewal at the face amount of the expiring instrument. To guarantee financial responsibility instrument coverage, the conditions of coverage should stipulate that a financial instrument may not cancel, terminate, or fail to renew except for failure to pay instrument overhead costs, such as premiums and annual fees. If there is a failure to pay overhead costs, the third-party financial institution may elect to cancel, terminate, or fail to renew the instrument by sending notice by certified mail to the owner or operator. The instrument, however, should establish that the cancellation not be final until 120 days after receipt of the cancellation notice by the UIC Program Director and the owner or operator. Within 90 days of the notice of cancellation, the owner or operator should provide an alternate financial responsibility demonstration. If an alternate financial responsibility demonstration acceptable to the UIC Program Director has not been established by the owner or operator by the end of the 90-day period, the UIC Program Director should provide notification that the funds be released to the instrument's standby trust. Any funds from the instrument being cancelled should be released within 30 days of notification by the UIC Program Director.

The EPA also recommends that the financial instrument(s) remain in full force and effect so that required Class II activities can be completed in the event that on or before the date of expiration the following circumstances arise:

- The UIC Program Director deems the facility abandoned,
- The permit is terminated or revoked or a new permit is denied,
- Closure is ordered by the UIC Program Director or a U.S. district court or other court of competent jurisdiction,
- The owner or operator is named as debtor in a voluntary or involuntary proceeding under Title 11 (Bankruptcy) of the U.S. Code, or
- The amount due is paid.

B. Conditions for Releasing or Partially Releasing a Financial Instrument

Owners or operators may cancel financial instruments only upon receipt of the UIC Program Director's written consent. There are several circumstances under which the EPA may fully or partially release certain instruments, pursuant to 40 CFR 144.28 (d)(1) for rule-authorized and 144.52(a)(7)(i) for permitted wells as follows:

- Wells are properly plugged and abandoned in accordance with an EPA-approved plugging and abandonment plan,
- Acceptable substitute demonstrations are made,
- Wells are converted out of the UIC program, or
- A transferee has demonstrated financial responsibility for the well.

Pursuant to 40 CFR 144.28(l) for rule-authorized wells and 144.38 for permitted wells, the transferor must provide the UIC Program Director notice at least 30 days in advance of the transfer in ownership or operational control for rule-authorized wells or the automatic permit transfers for permitted wells. The notice must include a written agreement between the transferor and the transferee, establishing a date for the transfer as well as a specific date by which the transferee will demonstrate financial responsibility. Under the regulations, the original owner/operator (the transferor) is required to maintain financial responsibility until the new owner or operator supplies an acceptable demonstration or is otherwise released from Class II financial responsibility requirements (e.g., the well is plugged and abandoned). See 40 CFR 144.28(d)(iii); 144.52(a)(7)(c).

C. EPA's Ability to Draw on a Financial Instrument

The UIC Program Director may draw upon a financial instrument under any of the following conditions:

- If an owner or operator fails to provide a substitute financial instrument no later than 30 days prior to the effective date of the issuing institution's non-renewal or cancellation of the existing instrument.
- If an owner or operator is unable or fails to plug the covered injection wells properly due to any reason, such as in the case that the owner or operator declares bankruptcy or does not have adequate funds available.

Appendix B: USEPA Regional Offices and UIC Program Offices

For the most current regional contact information, consult the “Where You Live UIC Regional Contacts” page, available online at:

<http://water.epa.gov/type/groundwater/uic/whereyoulive.cfm>.

Appendix C: Regulatory Language for Financial Responsibility for Class II Wells

40 CFR §144.28: Requirements for Class I, II, and III wells authorized by rule.

(d) Financial responsibility.

(1) The owner, operator and/or, for EPA-administered programs, the transferor of a Class I, II or III well, is required to demonstrate and maintain financial responsibility and resources to close, plug and abandon the underground injection operation in a manner prescribed by the Director until:

(i) The well has been plugged and abandoned in accordance with an approved plugging and abandonment plan pursuant to §§144.28(c) and 146.10 and submission of a plugging and abandonment report has been made pursuant to § 144.28(k) ;

(ii) The well has been converted in compliance with the requirements of §144.28(j); or

(iii) For EPA-administered programs, the transferor has received notice from the Director that the transferee has demonstrated financial responsibility for the well. The owner or operator shall show evidence of such financial responsibility to the Director by the submission of a surety bond, or other adequate assurance, such as a financial statement.

(2) For EPA-administered programs, the owner or operator shall submit such evidence no later than one year after the effective date of the UIC program in the State. Where the ownership or operational control of the well is transferred more than one year after the effective date of the UIC program, the transferee shall submit such evidence no later than the date specified in the notice required pursuant to §144.28(1)(2).

(3) For EPA-administered programs, the Regional Administrator may require the owner or operator to submit a revised demonstration of financial responsibility if the Regional Administrator has reason to believe that the original demonstration is no longer adequate to cover the cost of closing, plugging and abandoning the well.

(4) For EPA-administered programs, the owner or operator of a well injecting hazardous waste must comply with the financial responsibility requirements of subpart F of this part.

(5) For EPA-administered programs, an owner or operator must notify the Regional Administrator by certified mail of the commencement of any voluntary or involuntary proceeding under Title 11 (Bankruptcy) of the United States Code which names the owner or operator as debtor, within 10 business days after the commencement of the proceeding. Any party acting as guarantor for the owner or operator for the purpose of

financial responsibility must so notify the Regional Administrator, if the guarantor is named as debtor in any such proceeding.

(6) In the event of commencement of a proceeding specified in paragraph (d)(5) of this section, an owner or operator who has furnished a financial statement for the purpose of demonstrating financial responsibility under this section shall be deemed to be in violation of this paragraph until an alternative financial assurance demonstration acceptable to the Regional Administrator is provided either by the owner or operator or by its trustee in bankruptcy, receiver, or other authorized party. All parties shall be prohibited from injecting into the well until such alternate financial assurance is provided.

(l) Change of ownership or operational control. For EPA-administered programs:

(1) The transferor of a Class I, II or III well authorized by rule shall notify the Regional Administrator of a transfer of ownership or operational control of the well at least 30 days in advance of the proposed transfer.

(2) The notice shall include a written agreement between the transferor and the transferee containing a specific date for transfer of ownership or operational control of the well; and a specific date when the financial responsibility demonstration of §144.28(d) will be met by the transferee.

(3) The transferee is authorized to inject unless he receives notification from the Director that the transferee has not demonstrated financial responsibility pursuant to §144.28(d).

§144.52 Establishing permit conditions.

(a) In addition to conditions required in §144.51, the Director shall establish conditions, as required on a case-by-case basis under §144.36 (duration of permits), §144.53(a) (schedules of compliance), §144.54 (monitoring), and for EPA permits only §144.53(b) (alternate schedules of compliance), and §144.4 (considerations under Federal law). Permits for owners or operators of hazardous waste injection wells shall include conditions meeting the requirements of §144.14 (requirements for wells injecting hazardous waste), paragraphs (a)(7) and (a)(9) of this section, and subpart G of part 146. Permits for owners or operators of Class VI injection wells shall include conditions meeting the requirements of subpart H of part 146. Permits for other wells shall contain the following requirements, when applicable.

(7) Financial responsibility.

(i) The permittee, including the transferor of a permit, is required to demonstrate and maintain financial responsibility and resources to close, plug, and abandon the underground injection operation in a manner prescribed by the Director until:

(A) The well has been plugged and abandoned in accordance with an approved plugging and abandonment plan pursuant to §§144.51(o),

146.10, and 146.92 of this chapter, and submitted a plugging and abandonment report pursuant to §144.51(p); or

(B) The well has been converted in compliance with the requirements of §144.51(n); or

(C) The transferor of a permit has received notice from the Director that the owner or operator receiving transfer of the permit, the new permittee, has demonstrated financial responsibility for the well.

(ii) The permittee shall show evidence of such financial responsibility to the Director by the submission of a surety bond, or other adequate assurance, such as a financial statement or other materials acceptable to the Director. For EPA-administered programs, the Regional Administrator may on a periodic basis require the holder of a lifetime permit to submit an estimate of the resources needed to plug and abandon the well revised to reflect inflation of such costs, and a revised demonstration of financial responsibility, if necessary. The owner or operator of a well injecting hazardous waste must comply with the financial responsibility requirements of subpart F of this part. For Class VI wells, the permittee shall show evidence of such financial responsibility to the Director by the submission of a qualifying instrument (see §146.85(a) of this chapter), such as a financial statement or other materials acceptable to the Director. The owner or operator of a Class VI well must comply with the financial responsibility requirements set forth in §146.85 of this chapter.