



RAILROAD COMMISSION OF TEXAS

OIL AND GAS DIVISION

OIL AND GAS REGULATION AND CLEANUP PROGRAM ANNUAL REPORT - FISCAL YEAR 2012





RAILROAD COMMISSION OF TEXAS

OIL AND GAS DIVISION

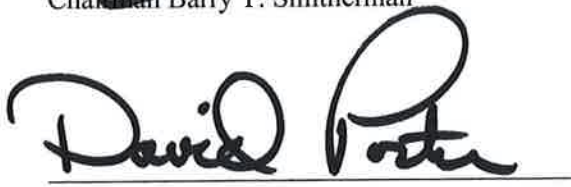
January 29, 2013

To The Legislature:

S.B. 1103, 72nd Legislature, 1991 and S.B. 310, 77th Legislature, 2001 and S.B. 1, 82nd Legislature, 2011 (§91.112(b), Natural Resources Code) requires the Railroad Commission to submit an Annual Report to the Legislature on the Oil Field Cleanup Program. The information required by S.B. 1103 and as amended by S.B. 310 and S.B. 1 is contained in this report. This report covers the period from September 1, 2011 through August 31, 2012.

The Railroad Commission remains committed to the success of the Oil and Gas Regulation and Cleanup Program and to the protection of the State's land and water resources through activities funded by the Oil and Gas Regulation and Cleanup Fund. This report is posted on the Commission's website; however, should you have any questions about the material presented, please contact Ramon Fernandez, Deputy Director of the Commission's Oil & Gas Division, Field Operations Section, at 463-6830; Peter Pope, Assistant Director of the Commission's Oil and Gas Division, Site Remediation Section, at 463-8202; Reese Copeland, Director of the Commission's Office of General Counsel, Enforcement Section, at 463-8951; or Araminta Everton, Director of the Commission's Administration Division, at 463-5881.


Chairman Barry T. Smitherman


Commissioner David Porter

Attest:


Secretary


Commissioner Christi Craddick

RAILROAD COMMISSION OF TEXAS

OIL AND GAS REGULATION AND CLEANUP PROGRAM

ANNUAL REPORT - FISCAL YEAR 2012

INTRODUCTION:

The Oil and Gas Regulation and Cleanup Fund was created by the adoption of Senate Bill (S.B.) 1 (82nd Legislature, 2011). S.B. 1 replaced the previous Oil Field Cleanup Fund that was created by the adoption of Senate Bill (S.B.) 1103 (72nd Legislature, 1991) and modified by the adoption of S.B. 310 (77th Legislature, 2001). Under S.B. 1103, the State of Texas, through the Railroad Commission (hereinafter “Commission”), increased its financial ability to plug abandoned, orphaned oil and gas wells and to remediate abandoned, orphaned oil field sites throughout the State. S.B. 1103 replaced the previous Well Plugging Fund with the Oil Field Cleanup Fund and set the fund balance cap at \$10 million. S.B. 310 increased the production tax on oil and gas and several existing fees associated with oil and gas industry activity and increased the Oil Field Cleanup Fund balance cap from \$10 million to \$20 million.

The impact of the Oil and Gas Regulation and Cleanup Fund is clearly demonstrated by the increase in the number of orphaned wells plugged and sites remediated. From fiscal year 1984 to fiscal year 1991, the Commission plugged 4,078 wells at a cost of \$16,171,406 under the previous Well Plugging Fund. From fiscal year 1992 through fiscal year 2012, the Commission plugged 29,004 wells at a cost of \$188,311,929 (33,082 wells since fiscal year 1984 at a total cost of \$204.4 million) and cleaned up, assessed, or investigated 4,950 sites at a cost of \$60,534,744 using the Oil and Gas Regulation and Cleanup Fund and other state and federal sources of funds.

As of August 2012, the Commission was tracking 398,252 wells compared to 396,355 in August 2011. Of this number, 109,737 were inactive, shut-in oil and gas wells. Of the 109,737 wells, 30,449 were compliant inactive wells that had been shut-in less than 12 months and 66,899 were compliant inactive wells that were shut-in for more than 12 months, but belonged to operators with an active Organization Report (Form P-5) on file with the Commission and have filed the required financial assurance, a bond or letter of credit, and qualified for a plugging extension. The remaining 12,389 wells were non-compliant inactive wells that were in violation of the Commission’s plugging rule. Of the 12,389 non-complaint wells, 4,913 wells belonged to operators with an active Form P-5 on file with the Commission and 7,476 wells belonged to operators with a delinquent Form P-5. The Commission defines these 7,476 wells as orphan wells. These figures are represented on a percentage basis in Figure 1 and the distribution of wells for August 2012 monitored by the Commission is shown in Figure 2.

The operators of record plug most of the compliant inactive wells and some of the non-compliant inactive wells as required by Commission rules and regulations. However, some currently compliant and many of the orphan wells eventually require plugging by the Commission with Oil and Gas Regulation and Cleanup funds and/or other state and federal funds.

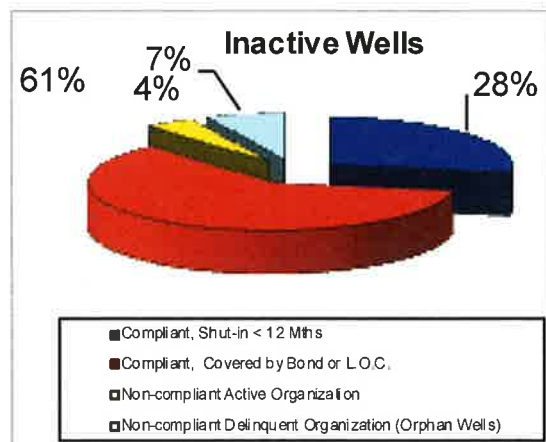


Figure 1

Distribution of Wells Monitored by the Railroad Commission

As of August 31, 2012

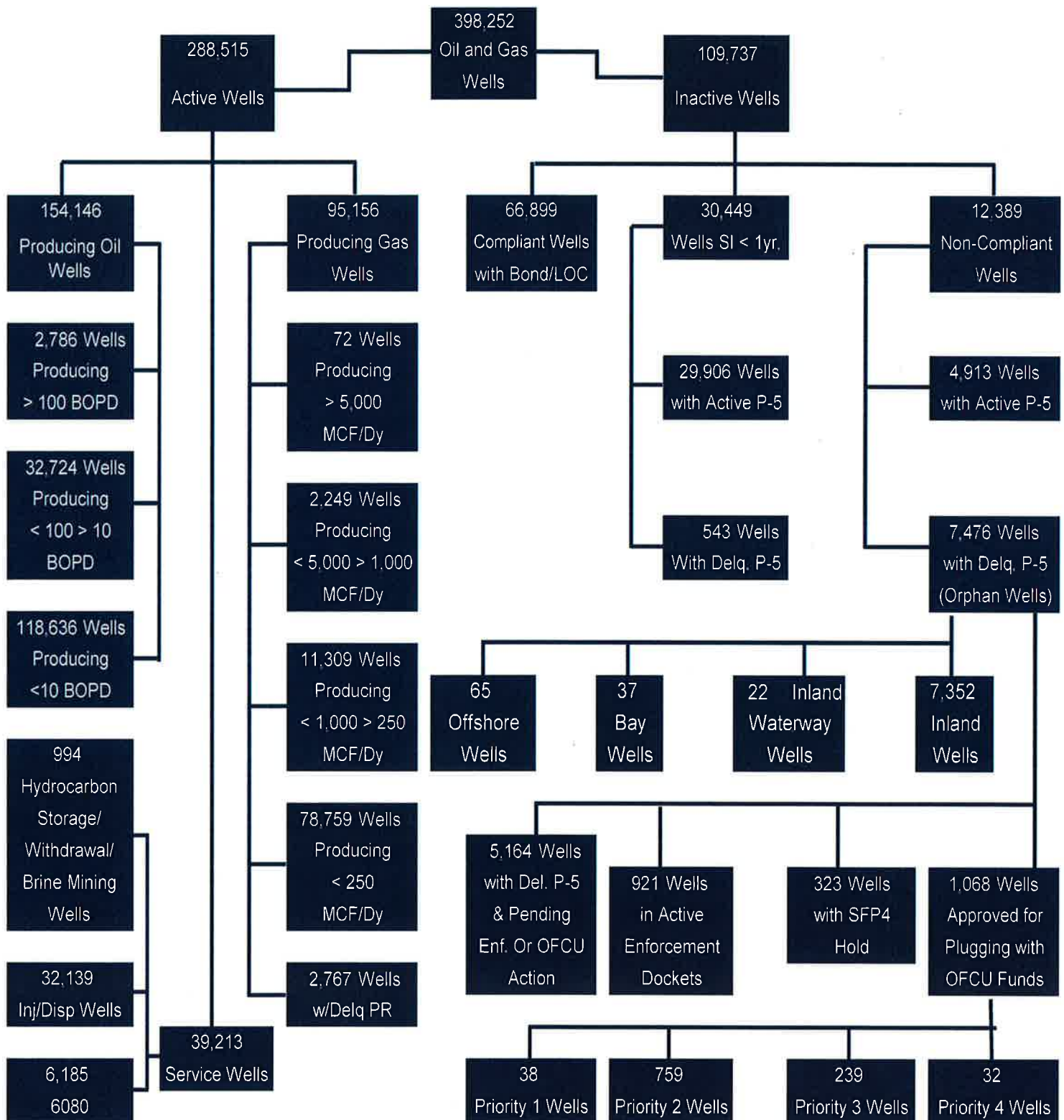


Figure 2

It is important to understand that the number of orphan wells is a dynamic number that changes daily, as wells are placed into and out of compliance. The Commission attempts to capture the dynamics occurring within the orphan well population on a monthly basis and depicts these changes during fiscal year 2012 in Table 1. Table 2 depicts the yearly dynamics beginning with fiscal year 2003 (September 1, 2002). The data in Table 1 illustrates that the number of orphan wells decreased by 393 in fiscal year 2012 and has decreased by 10,495 wells since September 2002 (Table 2). However, the make-up of the orphan wells has changed. A total of 8,690 wells (Plugged, Returned to Active Status, P-5 renewal, Other) were removed from the fiscal year 2012 beginning inventory, but 8,297 new wells were added to the population of orphan wells throughout the fiscal year (Table 1). Since the beginning of fiscal year 2003, 105,142 orphan wells have been removed from the inventory and 94,647 new orphan wells have been added to the inventory (Table 2). The Commission's regulatory goals are to eliminate the threat of pollution posed by orphaned unplugged wells and to minimize the number of orphan wells requiring plugging with Oil and Gas Regulation and Cleanup funds, or other state and federal funds. This decrease in the number of orphan wells is illustrated in Figure 3.

Month of Activity	Sep-11	Oct-11	Nov-11	Dec-11	Jan-12	Feb-12	Mar-12	Apr-12	May-12	Jun-12	Jul-12	Aug-12	Total
Beginning Population (from previous month)	7,869	7,369	7,976	7,703	7,984	8,276	8,142	7,882	7,674	7,601	7,609	7,328	7,869
Plugged	(247)	(145)	(78)	(59)	(35)	(155)	(41)	(92)	(67)	(87)	(83)	(36)	(1,125)
Returned to Active Status	(3)	(6)	(5)	(4)	(5)	(7)	(15)	(5)	(24)	(5)	(7)	(8)	(94)
Operator Change	(33)	(20)	(67)	(51)	(27)	(53)	(61)	(47)	(77)	(88)	(57)	(125)	(706)
P-5 Renewal	(596)	(203)	(621)	(460)	(528)	(660)	(663)	(661)	(585)	(592)	(730)	(465)	(6,764)
Other Reasons	0	0	0	0	0	0	(1)	0	0	0	0	0	(1)
Wells Added to Population	379	981	498	855	887	741	521	597	680	780	596	782	8,297
Ending Population	7,369	7,976	7,703	7,984	8,276	8,142	7,882	7,674	7,601	7,609	7,328	7,476	7,476

Definitions:
Plugged = Plugged and abandoned.
Returned to Active Status = Active producing or service well.
Operator Change = P-4 Operator Change was filed and approved. An operator change will not be approved unless the new operator has sufficient bond amount on file to cover the new wells and has an active P-5.
P-5 Renewal = The operator of record renews their P-5.
Other Reasons = Supporting documentation filed to correct shut-in date, well activity, etc.
Wells Added to Population = Wells not considered orphaned at end of previous month, but considered orphaned at the end of this month.

Table 1

**RAILROAD COMMISSION OF TEXAS
OIL AND GAS REGULATION AND CLEANUP PROGRAM**

ANNUAL REPORT –FY 2012

Month of Activity	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012			Total
Beginning Population (from previous FY)	17,971	16,770	15,305	14,208	11,287	9,579	9,323	7,900	7,036	7,869			17,971
Plugged	(1,527)	(1,726)	(1,756)	(1,877)	(1,514)	(1,143)	(1,426)	(1,256)	(413)	(1,125)			(13,763)
Returned to Active Status	(646)	(160)	(177)	(196)	(118)	(119)	(35)	(47)	(187)	(94)			(1,779)
Operator Change	(3,110)	(1,777)	(2,506)	(1,483)	(1,361)	(1,546)	(856)	(934)	(668)	(706)			(14,947)
P-5 Renewal	(8,581)	(8,144)	(6,907)	(10,336)	(8,697)	(5,737)	(5,056)	(5,271)	(8,778)	(6,764)			(74,271)
Other Reasons	(281)	(23)	(19)	(12)	(5)	(6)	(4)	(9)	(22)	(1)			(382)
Wells Added to Population	12,944	10,365	10,268	10,983	9,987	8,295	5,954	6,653	10,901	8,297			94,647
Ending Population	16,770	15,305	14,208	11,287	9,579	9,323	7,900	7,036	7,869	7,476			7,476

Definitions:
Plugged = Plugged and abandoned.
Returned to Active Status = Active producing or service well.
Operator Change = P-4 Operator Change was filed and approved. An operator change will not be approved unless the new operator has sufficient bond amount on file to cover the new wells and has an active P-5.
P-5 Renewal = The operator of record renews their P-5.
Other Reasons = Supporting documentation filed to correct shut-in date, well activity, etc.
Wells Added to Population = Wells not considered orphaned at end of previous FY, but considered orphaned at the end of this FY.

Table 2

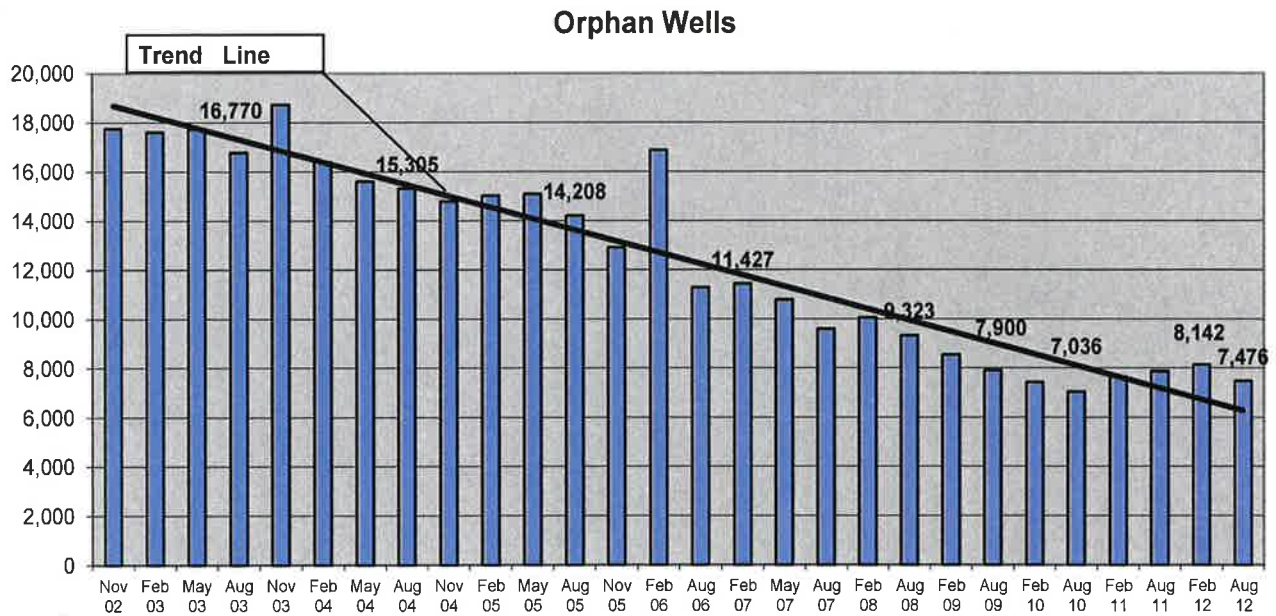


Figure 3

Revenue into the Oil and Gas Regulation and Cleanup Fund is derived primarily from production taxes and permitting fees paid by the oil and gas industry; but significant revenue is also contributed from enforcement penalties, reimbursements, proceeds from the sale of equipment and hydrocarbons salvaged from well plugging and site remediation operations, and interest on fund balances. Additionally, the Commission seeks other funding sources from state and federal agencies to supplement the activities of the Oil and Gas Regulation and Cleanup Program. Although the Oil and Gas Regulation and Cleanup Fund finances the majority of the Oil and Gas Cleanup and Regulation program activities, the wells plugged and sites remediated contained in this report were partially funded with federal monies received from the Coastal Impact Assistance Program (CIAP, and managed by the General Land Office (GLO).

The following information on the Oil and Gas Regulation and Cleanup Program is reported annually as required by S.B. 1.

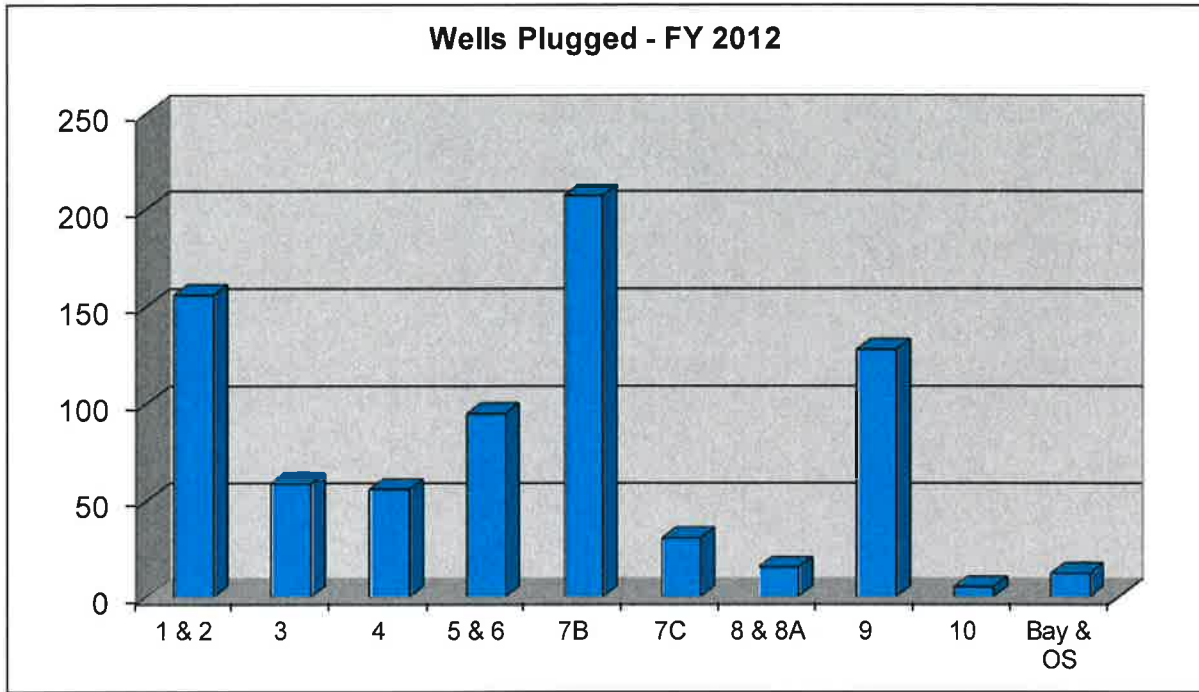
I. NUMBER OF WELLS PLUGGED BY DISTRICT:

In fiscal year 2012, the Commission plugged 764 wells with Oil and Gas Regulation and Cleanup funds. The total number of wells plugged represents those wells that are physically plugged and invoiced by the plugging contractors and files closed through August 31, 2012. Figure 4 illustrates the numbers of wells plugged by district during fiscal year 2012 and Figure 5 shows the number of wells plugged by fiscal year since the inception of the current Oil Field Cleanup Program, September 1, 1991.

During fiscal year 2012, the Commission's well plugging expenditures totaled \$12,309,477. The average cost per well was \$16,112, which was \$4,598 more than the fiscal year 2011 average cost per well of \$11,514. The fiscal year 2012 adjusted average cost per well was \$13,600 compared to an adjusted average cost per well of \$8,932 per well for fiscal year 2010. The adjusted average cost excludes the costs to plug bay, offshore, and inland waterway wells. During fiscal year 2012 the Commission plugged twelve (12) bay wells at a total cost of \$2,081,920.

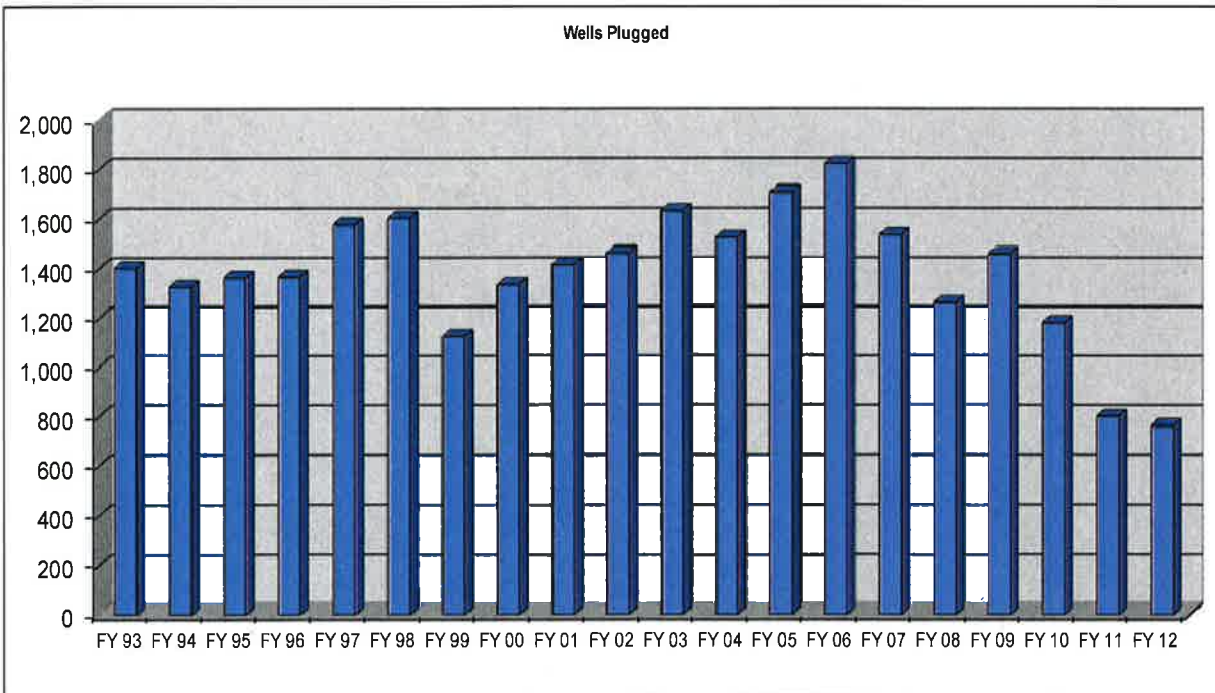
The Commission has approximately 193 well servicing companies with a P-5 Organization Report identified as an "Approved Plugger" and are authorized to plug wells in Texas. However, due to the increased level of activity in the oil and gas industry, competition for well plugging contractors is severely limiting the number of plugging contractors that bid on Commission contracts. As a result, fewer orphaned wells are being plugged by the Commission. During fiscal year 2012, the Commission awarded sixty-seven (67) contracts to twenty-four (24) well plugging contractors, of which, sixteen (16) had multiple bid awards. It is important to note that the current state of the industry is expected to continue for many years.





District Office	1 & 2	3	4	5 & 6	7B	7C	8 & 8A	9	10	Bay & OS	Total
Wells Plugged	156	59	56	95	207	31	15	128	5	12	764

Figure 4



Fiscal Year	FY 92	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98	FY 99	FY 00	FY 01	FY 02	FY 03	FY 04	FY 05	FY 06	FY 07
Wells Plugged	1,324	1,404	1,325	1,364	1,366	1,577	1,604	1,126	1,335	1,417	1,464	1,635	1,525	1,710	1,824	1,536
Fiscal Year	FY 08	FY 09	FY 10	FY 11	FY 12	Total										
Wells Plugged	1,261	1,460	1,182	801	764	29,004										

Figure 5

II. NUMBER OF ABANDONED WELLS BY DISTRICT:

As of August 2012, the number of abandoned, orphaned wells was **7,476**. The Commission defines these wells as orphan wells because they have been inactive for at least 12 months or more and the responsible operator’s Organization Report is delinquent. The number of orphan wells is a subset of the number of known inactive wells not currently in compliance with the Commission's plugging rule that is referenced in Section III of this report and illustrated in Figure 2. Figure 6, below, illustrates the number of orphan wells by district at the end of August 2012.

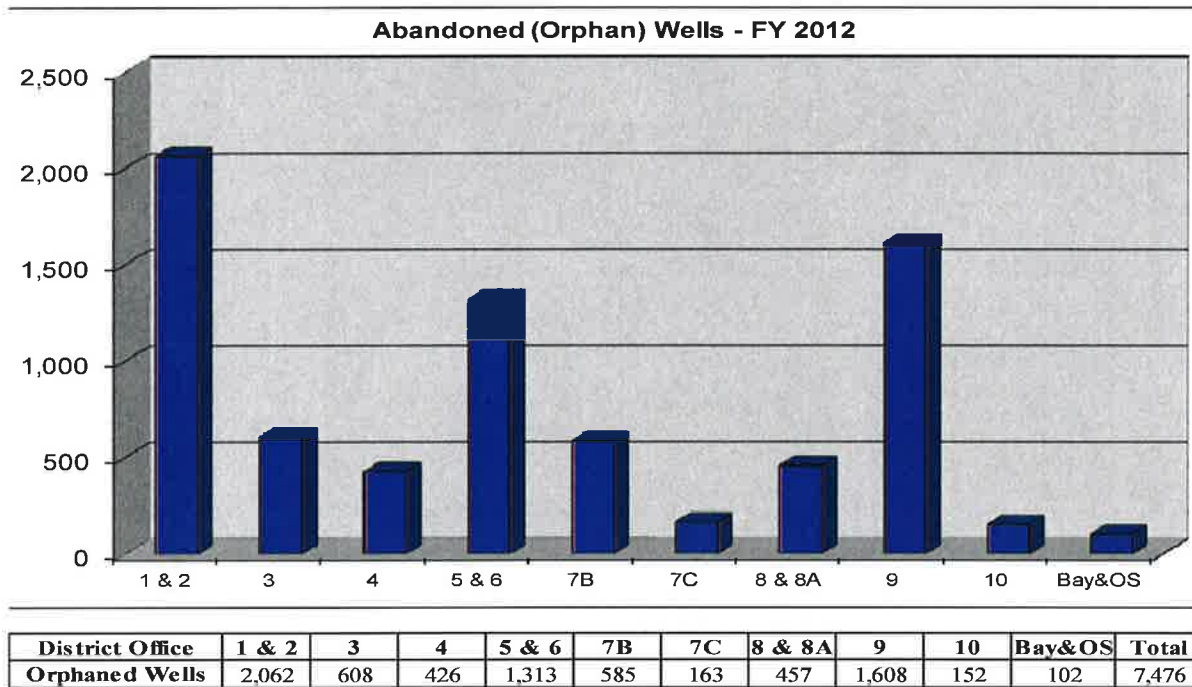


Figure 6

In addition to the 7,476 orphan wells, there are also an unknown number of old, unidentified wells in Texas, which have no records. As these wells are located, the Commission initiates plugging operations in accordance with the well plugging priority system, which is based on the threat the well poses to the environment and public safety. In fiscal year 2012, forty-seven (47) unidentified abandoned wells were plugged with Oil and Gas Regulation and Cleanup funds, which accounted for 6.2% of all wells plugged by the Commission in fiscal year 2012.

III. NUMBER OF NON-COMPLIANT INACTIVE WELLS BY DISTRICT:

The number of known inactive wells not in compliance with Commission rules as of August 2012 totals **12,389**. The number of known inactive wells not currently in compliance with the Commission's plugging rule is determined from the Commission’s computerized records. The number represents wells that remain shut-in beyond the initial 12 month shut-in period authorized by Commission Statewide Rule 14 and do not have a plugging extension, regardless of whether the operator’s Organization Report is active or delinquent. Wells that are shut-in for less than 12 months are deemed compliant inactive wells. Wells may remain inactive beyond the initial 12-month period and are eligible for plugging extensions if the operator has the required financial

assurance on file with the Commission, and the wells are in compliance with all Commission rules and regulations. Figure 7 shows the number of non-compliant wells by district at the end of August 2012. Figure 8 shows the number of non-compliant wells in August, at the end of each fiscal year since 1992. Like orphan wells (subset of the inactive non-compliant wells), the number of inactive non-compliant wells is a dynamic number that changes daily, as wells are placed into and out of compliance.

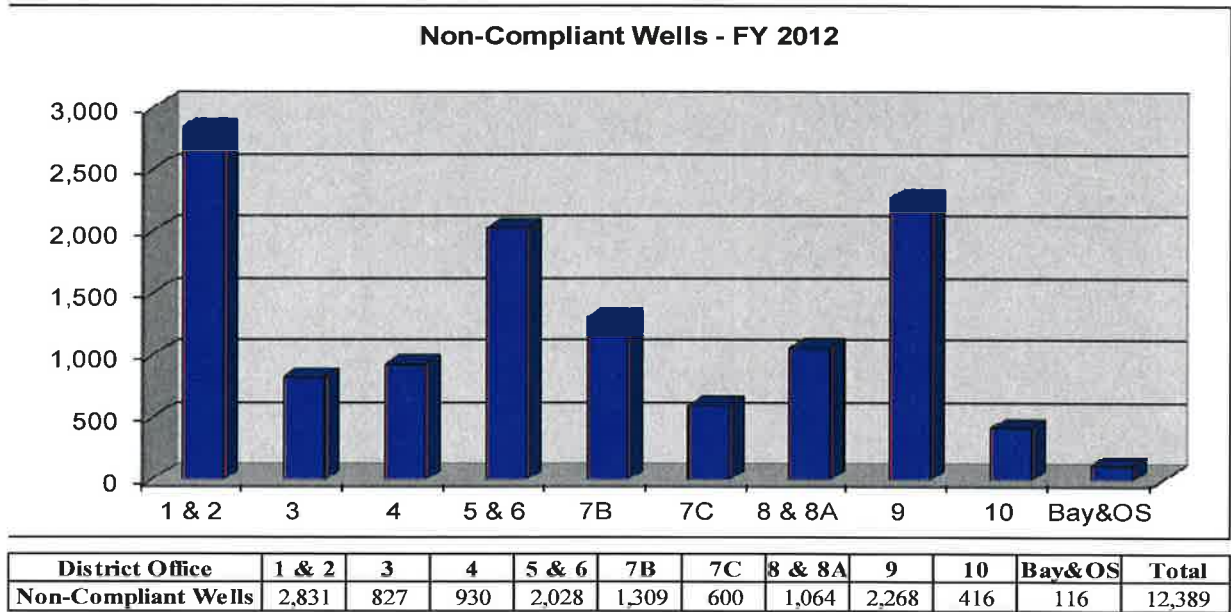


Figure 7

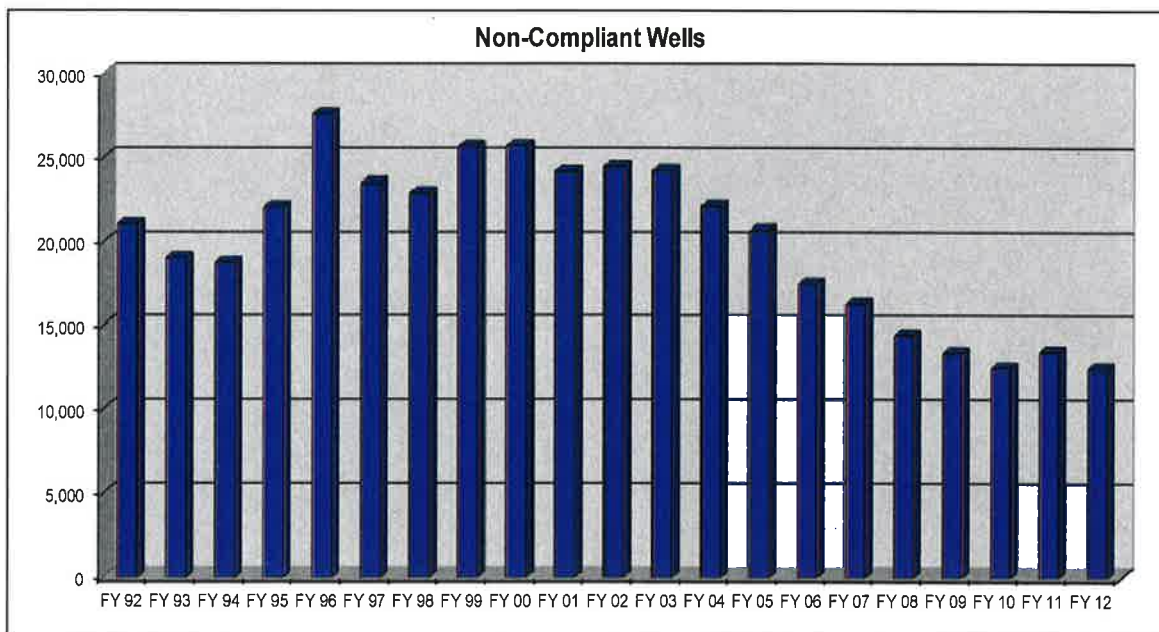


Figure 8

The operators of these wells are required by Commission rules to plug wells at their expense upon cessation of production but may be eligible for plugging extensions if they have the required financial assurance on file with the Commission and the wells are in compliance with all other rules and regulations. The operators may also be subject to enforcement action if violations are not corrected and the wells are not brought into compliance with Commission rules and regulations in a timely manner. If the Commission plugs these wells with monies from the Oil and Gas Regulation and Cleanup Fund or from other state or federal funds, the Office of the Attorney General may initiate legal action against the responsible operator for collection of the plugging costs and may assess civil penalties.

Operators plug the majority of all wells plugged each year. In fiscal year 2012, 8,055 wells (91% of all wells plugged) were plugged by the operators of record, without the use of Oil and Gas Regulation and Cleanup funds. Figure 9 depicts the number of wells plugged by operators since fiscal year 1992.

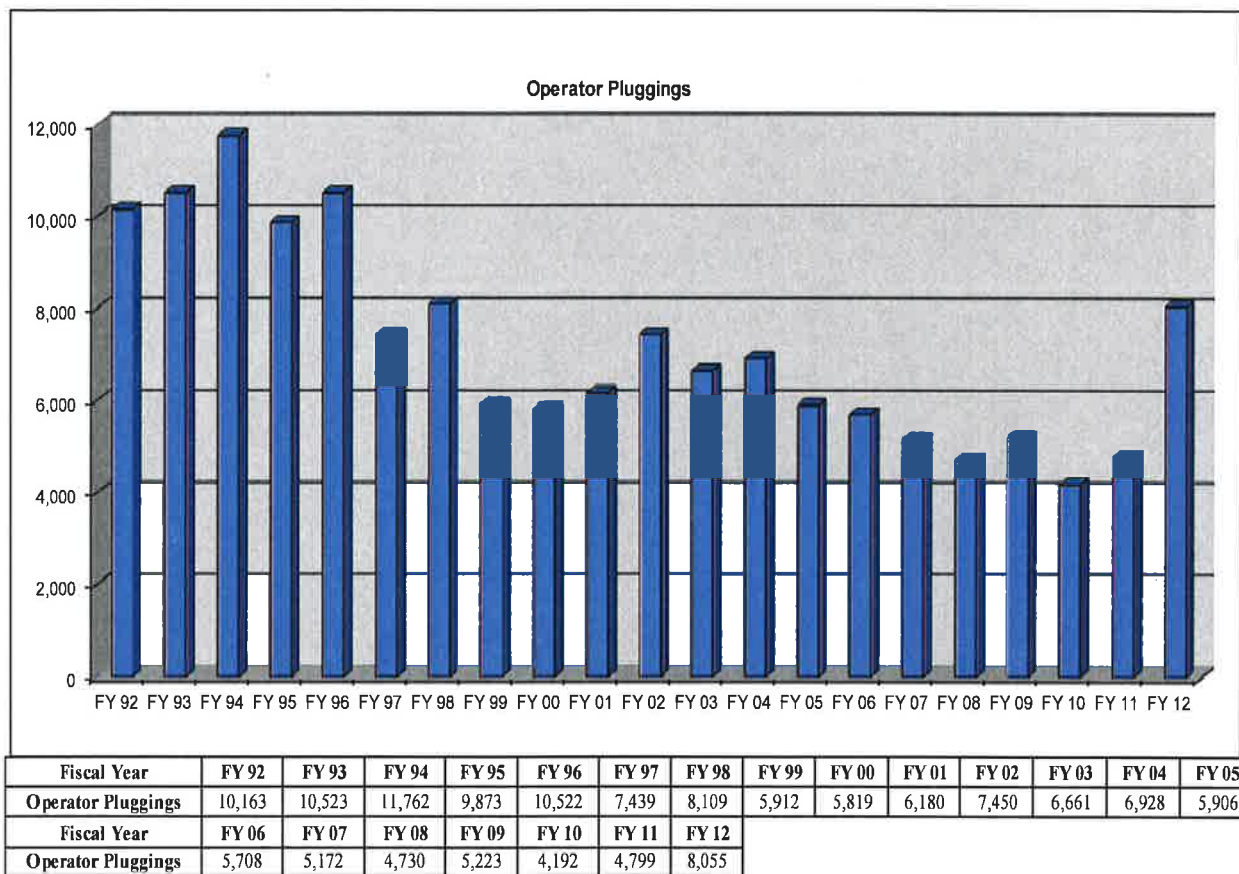


Figure 9

The Commission and industry have plugged between 5,000 and 12,000 wells per year since fiscal year 1992 (Figures 5 and 9). The number of orphan and non-compliant wells has decreased over the last five years (Figures 3 and 8). In fiscal year 2005, the number of known non-compliant inactive wells dropped below 21,000 for the first time since fiscal year 1994. Since a peak of 25,707 wells in fiscal year 2000, the number has declined to 12,389 in fiscal year 2012, a drop of 51%. The decrease in the number of orphan and non-compliant wells can be attributed to several

factors including the following: (1) In September 2001, the provisions of S. B. 310 required blanket bonds or letters of credit with an operator’s annual Organization Report (Form P-5) to cover the transfer of inactive wells from one operator to another; (2) In September 2004, universal bonding for all oil and gas operators became effective. At the end of fiscal year 2005, all inactive wells belonging to active operators were no longer eligible for a plugging extension by filing Form W-1X (Figure 2); and (3) the recent upturn in the oil and gas industry and sustained oil and gas prices have resulted in wells once deemed as uneconomic being returned to active production.

IV. STATUS OF ENFORCEMENT PROCEEDINGS BY DISTRICT:

The following information represents wells, in violation of the Commission's plugging rule, which have been referred to the Office of General Counsel--Enforcement Section and/or the Office of the Attorney General (AG) and currently are in various stages of enforcement. Table 3 displays the information by district and Table 4 by fiscal year from fiscal year 07 to 12.

ENFORCEMENT PROCEEDINGS	1/2	3	4	5/6	7B	7C	8/8A	9	10	Total
STATUS										
<i>1. Awaiting RRC review</i>	120	43	26	153	222	12	15	111	13	715
<i>2. Awaiting Hearing</i>	27	2	7	3	33	16	1	31	0	120
<i>3. Awaiting Final Order</i>	26	13	3	1	13	3	1	25	3	88
<i>4. Final Order Served/Awaiting AG referral</i>	0	0	0	0	0	0	0	0	0	0
<i>5. Wells Referred to AG</i>	34	2	3	18	15	4	4	65	0	145
<i>Total Wells Still in Violation</i>	207	60	39	175	283	35	21	232	16	1,068
TIME PERIOD										
<i>6. In Enforcement < 2yrs</i>	78	27	24	146	179	30	12	55	2	553
<i>7. In Enforcement > 2yrs & < 5yrs</i>	95	32	10	9	77	0	5	81	14	323
<i>8. In Enforcement > 5yrs</i>	0	2	1	1	14	1	0	28	0	47
<i>Total Wells Still in Enforcement</i>	173	61	35	156	270	31	17	164	16	923

Table 3

**RAILROAD COMMISSION OF TEXAS
OIL AND GAS REGULATION AND CLEANUP PROGRAM**

ANNUAL REPORT –FY 2012

ENFORCEMENT PROCEEDINGS	FY 07	FY 08	FY 09	FY 10	FY 11	FY 12
STATUS						
<i>1. Awaiting RRC review</i>	369	244	103	766	568	715
<i>2. Awaiting Hearing</i>	349	469	844	382	496	120
<i>3. Awaiting Final Order</i>	284	374	80	138	153	88
<i>4. Final Order Served/Awaiting AG referral</i>	0	0	0	0	0	0
<i>5. Wells Referred to AG</i>	398	168	274	137	250	145
Total Wells Still in Violation	1,400	1,255	1,301	1,423	1,467	1,068
TIME PERIOD						
<i>6. In Enforcement < 2yrs</i>	1,257	1,082	1,130	1,091	916	553
<i>7. In Enforcement > 2yrs & < 5yrs</i>	143	167	171	193	464	323
<i>8. In Enforcement > 5yrs</i>	0	6	0	0	87	47
Total Wells Still in Enforcement	1,400	1,255	1,301	1,284	1,467	923
PENALTIES & REIMBURSEMENTS						
<i>9. Administrative Penalties Assessed by RRC</i>	\$2,331,640	\$2,038,190	\$2,273,825	\$1,161,613	\$1,317,326	\$1,965,020
TOTAL PENALTIES AND REIM. PAID TO RRC & AG	\$2,804,213	\$5,323,074	\$4,474,418	\$3,052,987	\$3,812,740	\$3,124,623

Table 4

V. NUMBER OF SURFACE LOCATIONS REMEDIATED BY DISTRICT:

During the year, 2,015 abandoned oilfield sites were identified as candidates for state-managed remediation. Additional abandoned sites are identified each year through routine activities such as lease inspections, complaint investigations, state-managed plugging operations, or spill responses.

During fiscal year 2012, the Commission conducted 253 cleanup activities (Figure 10). This total includes all remediation activities invoiced by contractors that were approved and processed by the Commission before August 31, 2012. State-managed remediation activities included the following:

1. 168 routine remediation operations,
2. 34 emergency operations,
3. 51 site assessment investigations,

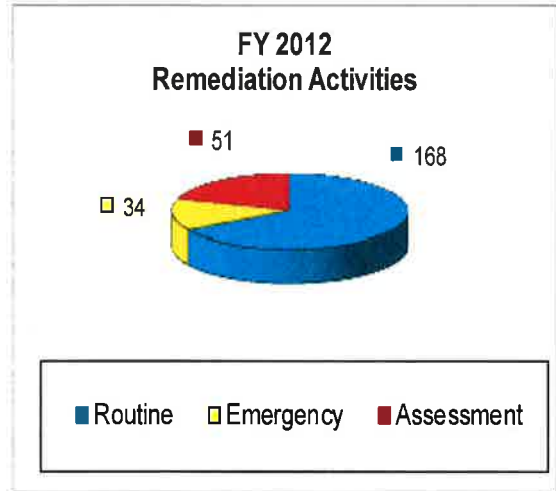
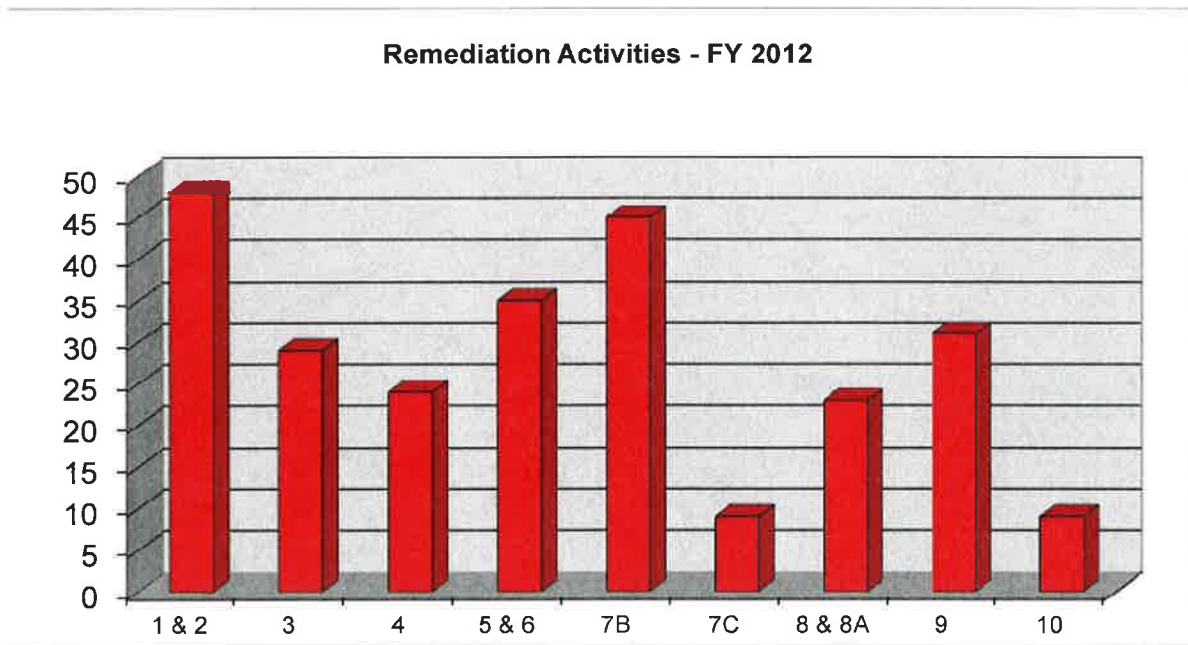


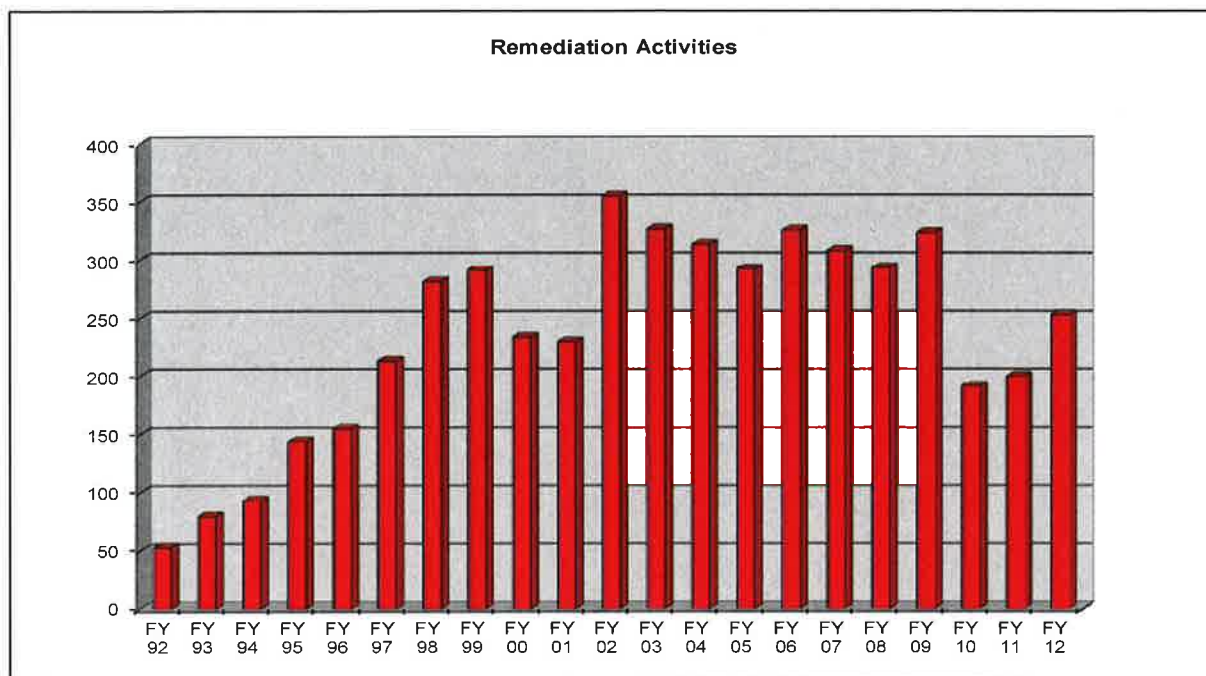
Figure 10

Figure 11 depicts these 253 sites by district for fiscal year 2012 and Figure 12 shows the sites cleaned up, assessed, or investigated by fiscal year since the inception of the program in September 1991.



District Office	1 & 2	3	4	5 & 6	7B	7C	8 & 8A	9	10	Total
Activities	48	29	24	35	45	9	23	31	9	253

Figure 11



Fiscal Year	FY 92	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98	FY 99	FY 00	FY 01	FY 02	FY 03	FY 04	FY 05	FY 06	
Activities	53	79	93	144	155	213	281	291	233	229	355	326	313	292	325	
Fiscal Year	FY07	FY08	FY09	FY10	FY11	FY12	Total									
Activities	308	293	323	191	200	253	4,950									

Figure 12

Similar to the well plugging priority system, the abandoned oilfield sites are prioritized based on the present or possible future impact to the environment and public safety. With larger sites, the challenge is often determining if the source of pollution is natural or man-made, which potential operator is responsible, how to evaluate the site, and which remedial method is appropriate for the situation.

The Commission utilizes environmental engineering contracts to help address complex sites. In addition to producing detailed assessment reports, the environmental contractors develop alternative remedial recommendations and anticipated costs.



State-Managed Cleanup, Hutchinson County, Texas

VI. OIL AND GAS REGULATION AND CLEANUP FUND EXPENDITURES:

The Commission began fiscal year 2012 with a beginning fund balance in the Oil and Gas Regulation and Cleanup Fund of \$18,021,411 and ended with a fund balance of \$8,020,251. Total revenues for the fiscal year were \$44,463,882 and total expenditures and encumbrances were \$54,464,042. Fiscal year 2012 Oil and Gas Regulation and Cleanup Fund revenues and expenditures for well plugging operations, site remediation activities, and administration of the program are detailed in Table 5 and graphically displayed in Figures 13 and 14.

Prior Year Cash Balance as of August 31, 2012				\$ 18,021,411	
		Comptroller BRE	Current Qtr Collections	Year-To-Date Collections	
Revenues:					
Oil & Gas Well Drilling Permit		\$ 8,900,000	\$ 3,177,636	\$ 13,396,776	
P5 Organization Filing Fee		3,500,000	974,004	4,036,802	
Oil and Gas Regulatory Fees		7,049,000	1,448,095	7,423,745	
Other Revenue		2,962,000	2,457,520	6,850,181	
Sub-Total Revenue		\$ 22,411,000	\$ 8,057,255	\$ 31,707,504	
Surcharges		\$ -	\$ 7,151,369	\$ 9,214,958	
Interagency Contracts		-	-	3,541,420	
Total Revenues		\$ 22,411,000	\$ 15,208,624	\$ 44,463,882	
Expenditures & Encumbrances:					
	Budget				
	Original	Revised	Expenditures	Encumbrances	Total Exp & Enc
Well Plugging	\$ 18,033,680	\$ 25,887,455	\$ 16,589,059	\$ 4,632,961	\$ 21,222,020
Site Remediation	4,940,607	8,212,883	5,435,106	1,603,672	7,038,778
Monitoring and Inspections	11,353,780	11,018,437	10,569,029	196,676	10,765,705
Oil and Gas Permitting	6,488,998	6,737,168	6,278,799	142,389	6,421,188
Administration	10,316,097	10,190,392	8,747,201	269,150	9,016,351
Total Expenditures	\$ 51,133,162	\$ 62,046,335	\$ 47,619,194	\$ 6,844,848	\$ 54,464,042
Unobligated Oil and Gas Regulation and Cleanup Fund Balance - August 31, 2012				\$ 8,021,251	
Personnel:	Budgeted	Actual			
FTEs	435.40	396.06			

Table 5

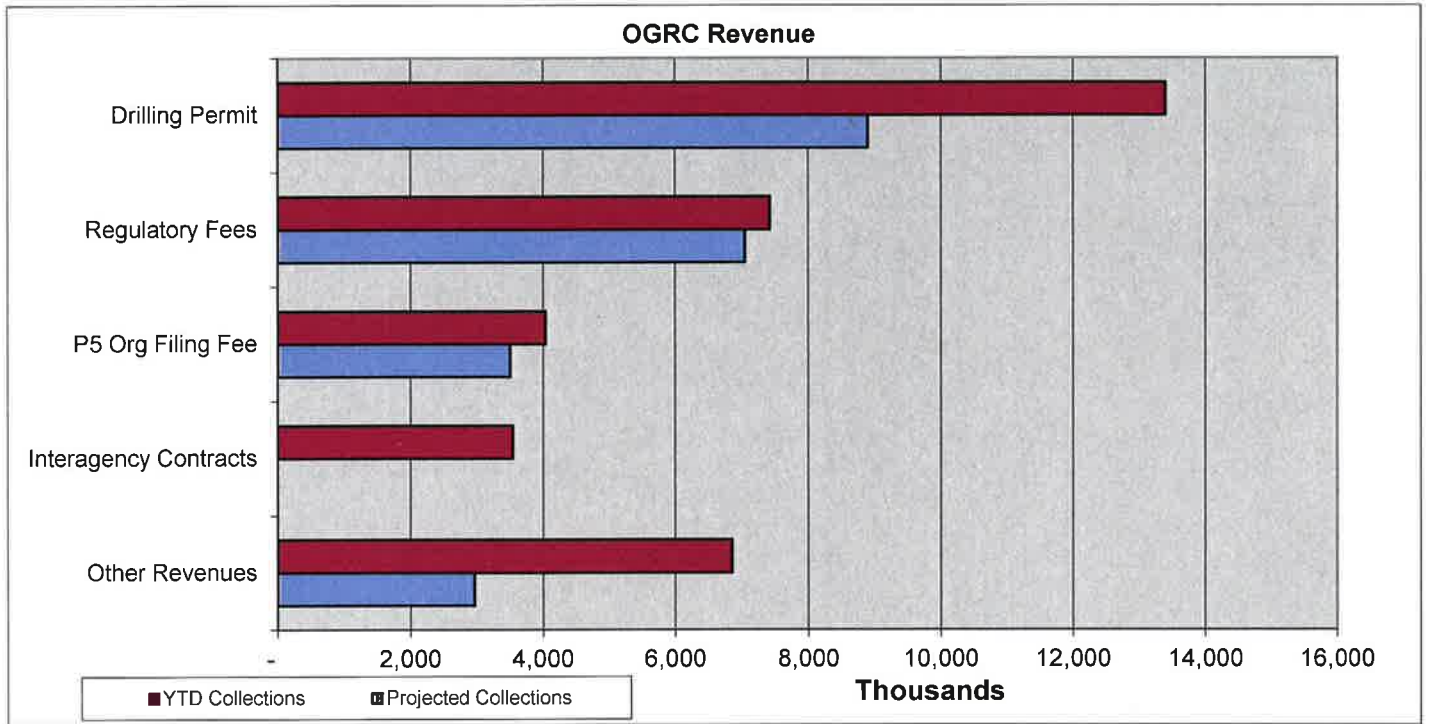


Figure 13

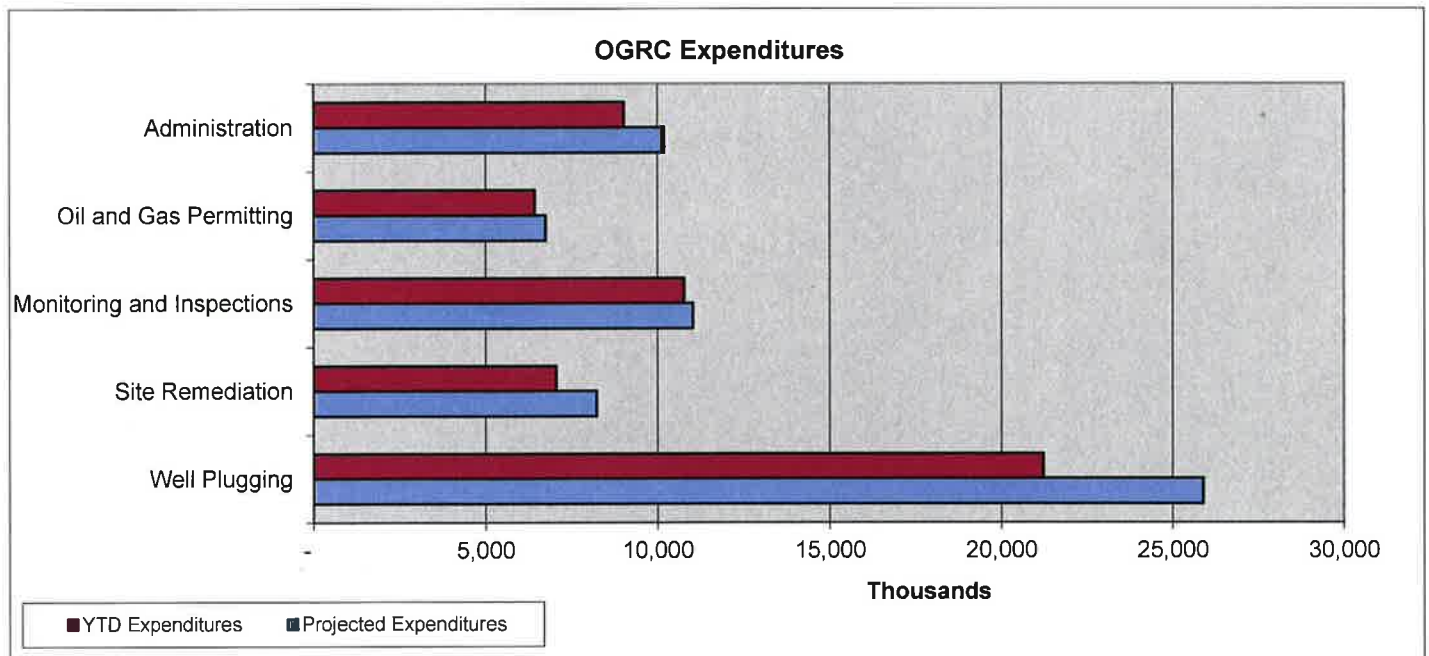


Figure 14

VII. WELL PLUGGING PRIORITY SYSTEM:

The Commission uses a priority methodology to rank wells for plugging to insure that those posing the greatest threat to public safety and the environment are plugged first. The priority system includes four factors relating to the threat a wellbore poses to public safety and the environment. The factors are titled “Well Completion”, “Wellbore Conditions”, “Well Location with respect to sensitive areas”, and “Unique Environmental, Safety, or Economic Concern.” The “**Well Completion**” factor has seven subcategories relating to the completion information on the well; type of formations penetrated, type of well, and age of the well, and has a maximum of forty (40) points. The “**Wellbore Conditions**” factor has seven subcategories relating to downhole conditions such as pressures on the well, fluid level in the well, and the mechanical integrity of the wellbore, and has a maximum of seventy-five (75) points. The “**Well Location**” factor has seven subcategories relating to the proximity to sensitive areas, and has a maximum of twenty (20) points. The remaining factor, “**Unique Environmental, Safety, or Economic Concern**” has five subcategories relating to proximity to active water floods or disposal wells, logistical concerns, wellbores with reentry problems, and the length of delinquency of the operator’s Organization Report, and has a maximum of twenty (20) points.

Only those factors, which apply, are considered. Each factor has been assigned a weight dependent on its potential to affect human health and the environment. The weights of the factors are summed to obtain a total weight. The total weight determines the priority a well receives. Wells receive a priority of 1, 2H, 2, 3, or 4, where 1 is the highest priority. The greater the total weight summed from all of the applicable factors, the higher the priority assigned. The priority system assigns leaking wells the highest priority (an automatic priority 1) and assigns an automatic priority 2 if the well fails a fluid level test. The current priority system is outlined below.

WELL PLUGGING PRIORITY SYSTEM

FACTOR		WEIGHT
1.	Well Completion	
A.	Unknown (no well records)	15
B.	No surface casing or set above base of deepest usable quality water	10
C.	Additional casing string not adequately cemented to isolate usable quality water	5
D.	Injection or Disposal Well	10
E.	Well penetrates salt/corrosive water bearing formation or abnormally pressured formation	5
F.	Well in H2S Field	5
G.	Age: well drilled ≥ 25 years ago	5
	Total (40 max)	

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2. Wellbore Conditions	
A. Well is pressured up at the surface (tbg or Prod csg)	10
B. Bradenhead pressure exists *	5
Auto 2H if UQW not protected, and fluid at BH is not UQW	
C. Measured fluid level:	
D. Fluid level at or above the base of deepest usable quality water.	50
E. Fluid level less than 250' below base of deepest usable quality water (na if 2D applies)	15
F. MIT failure	5
G. H-15 (MIT) never performed, or test greater than 5 years old (na if F applies)	3
H. Inadequate wellhead control/integrity	5
Total (75 max pts)	
3. Well location with respect to sensitive areas	
A. H2S well with Public area ROE ** Automatic Priority 2H	
B. In Marine Environment	10
C. Within 100' of river, lake, creek, or domestic use fresh water well (N/A if B applies)	5
D. Between 100' and ¼ mile of river, lake, creek, or domestic use fresh water well (N/A if C applies)	3
E. Located within agricultural area	2
F. Well located in known sensitive wildlife area	3
G. Well located within city or town site limits	10
Total (20 max pts)	
4. Unique environmental, Safety, or Economic Concern	
A. Adjacent to Active water flood or disposal well at or above completion interval.	5
B. Logistics (poor roads, encroaching public, etc)	5
C. Well Contains Junk	5
D. P-5 Delinquent > 5 years	5
E. Other (attach explanation)	1-20
Total (20 max pts)	
Total Weight	
Priority	
Priority 1 = Leaking Well (Based on Definition)	
Priority 2H = Higher Risk well (Based on Definition and/or total weight > +75)	
Priority 2 = Total Weight 50 - 75	
Priority 3 = Total Weight 25 - 49	
Priority 4 = Total Weight < 25	

* BH Pressure is sustained.

** 2H if public area could be impacted based on SWR 36 definition. Undetected/continuous leak possible.

Figures 15 and 16 and Table 6 below show the number of wells plugged with Oil and Gas Regulation and Cleanup funds by priority during fiscal year 2012 and between fiscal years 1992 and 2012. In September 2001, the Commission began concentrating its well plugging efforts on priority 1 and 2 wells as a result of implementation of the High Risk Well Testing Program established by S.B. 310 (77th Legislature, 2001). This continued through fiscal year 2012.

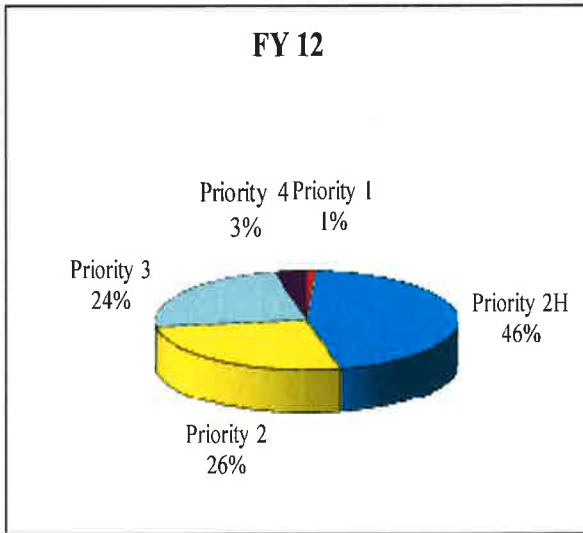


Figure 15

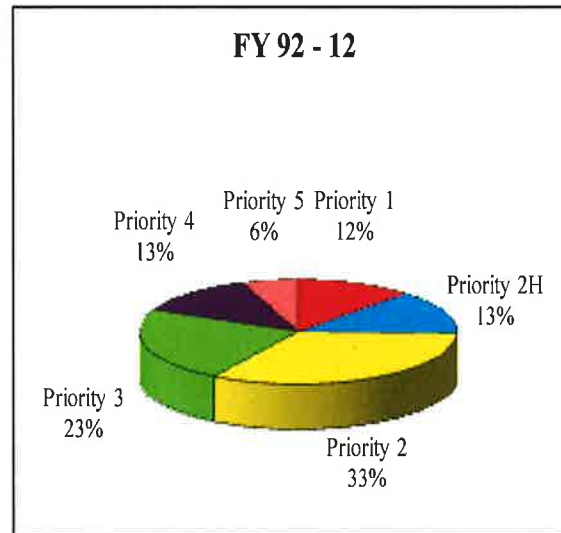


Figure 16

	Fiscal Year 2012	Fiscal Years 1992 – 2012
Priority 1	7	3,468
Priority 2H	348	3,924
Priority 2	202	9,666
Priority 3	181	6,656
Priority 4	26	3,639
Priority 5*	0	1,651
Total	764	29,004

Table 6

*No longer used (Priority 5 category eliminated in fiscal year 2001)

VIII. OIL AND GAS REGULATION AND CLEANUP FUNDS PROJECTION:

Oil and Gas Regulation and Cleanup fees projected in the Comptroller’s Biennial Revenue Estimate for the current biennium for plugging abandoned wells and remediating surface locations are as follows:

Fiscal Year 2012 = \$21,370,000

Fiscal Year 2013 = \$21,848,000

Figure 17 illustrates the actual revenues received into the Oil and Gas Regulation and Cleanup Fund. Neither the revenue projections nor the actual revenue receipts reflect revenues from federal sources.

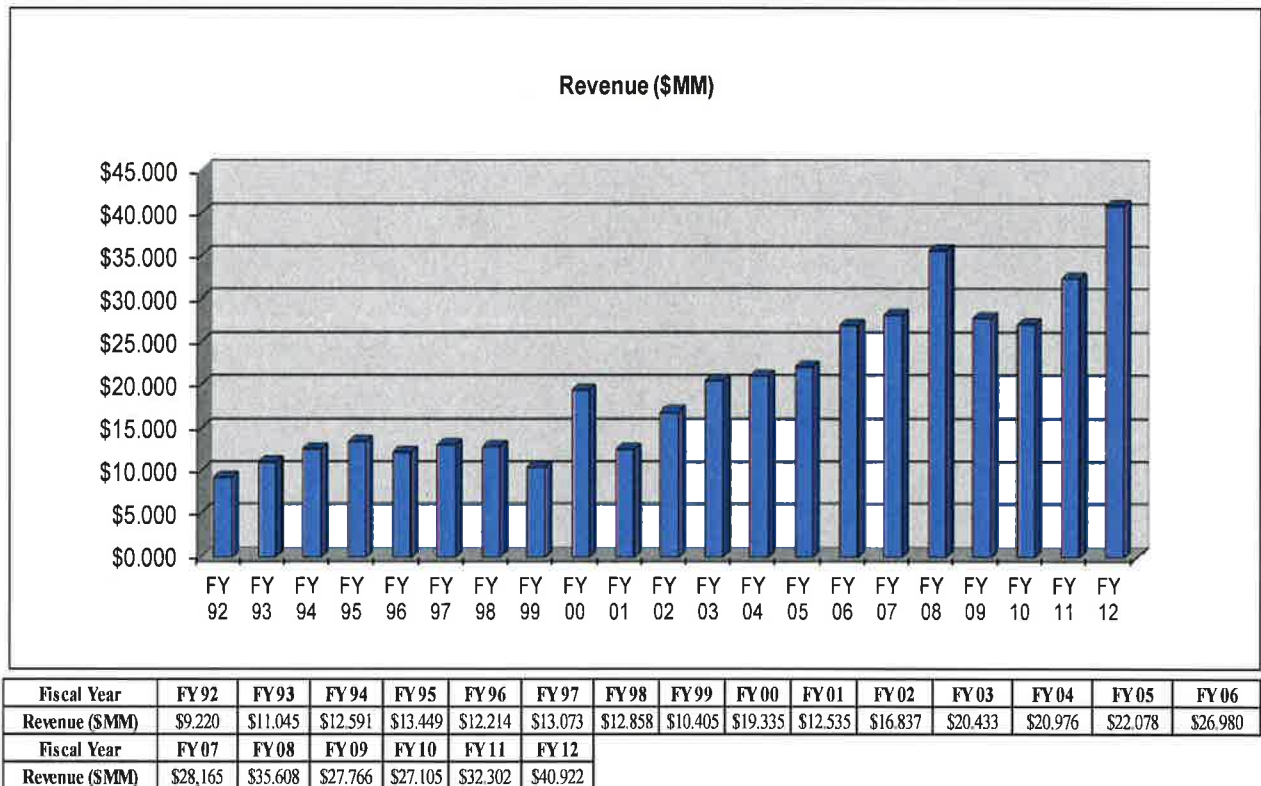


Figure 17

IX. STATUS OF SALVAGE OPERATIONS:

The Commission continues to benefit from the sale of salvageable equipment and hydrocarbons recovered from wells/leases plugged and sites remediated with Oil and Gas Regulation and Cleanup funds. In fiscal year 2012, the Commission derived **\$708,568** from the sale of salvageable equipment and hydrocarbons on **187** salvage operations and deposited these proceeds in the Oil and Gas Regulation and Cleanup Fund. The record for the sale of salvage was set in fiscal year 2006 with proceeds of \$1,637,051.

House Bill (H.B.) 2705 (73rd Legislature, 1993), which became effective January 1, 1994, streamlined the requirements and facilitated the process by which the Commission is able to sell salvageable equipment and hydrocarbons from wells plugged or sites remediated with Oil and Gas Regulation and Cleanup funds. While the bill eased the requirements to sell salvage, it continued to provide due process protection for interested or affected parties. Potential claimants of salvage proceeds have an indefinite period of time in which to file a claim against the Oil and Gas Regulation and Cleanup Fund for the proceeds from the sale of salvageable equipment and/or hydrocarbons. Additionally, H.B. 2613 (78th Legislature, 2003) clearly established the Commission’s ability to also sell stored hydrocarbons from abandoned sites remediated by the Commission.

Since the inception of the salvage program, the proceeds from the sale of salvageable equipment and hydrocarbons have totaled \$15,995,161 from 4,127 salvage operations. Figure 18 illustrates the salvage proceeds from the sale of equipment and hydrocarbons from fiscal year 1994 to the present.

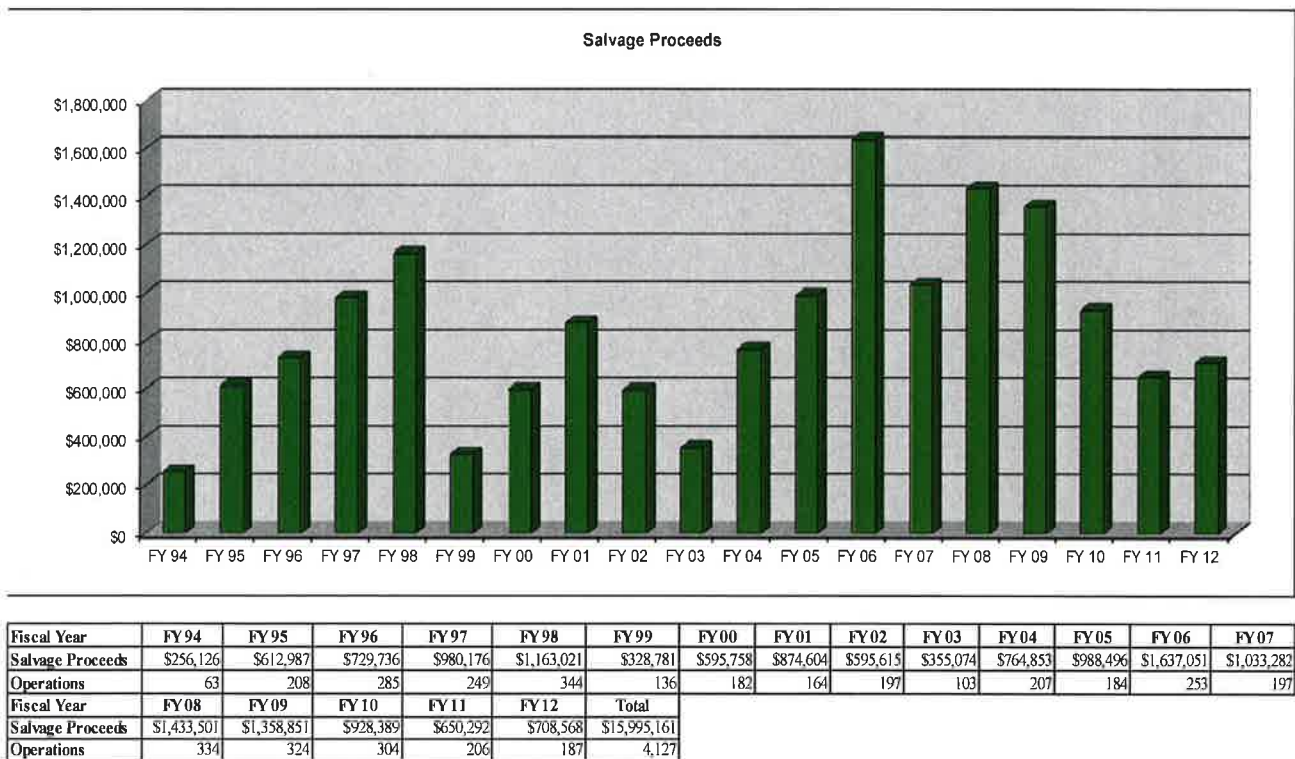


Figure 18

X. NUMBER OF SITES REMEDIATED UNDER THE VOLUNTARY CLEANUP PROGRAM BY DISTRICT:

Senate Bill 310, 77th Legislature (2001), amended Texas Natural Resources Code, Chapter 91, by adding new Subchapter O, specifically authorizing the Commission to establish a Voluntary Cleanup Program (VCP) that is self-funded through the collection of application and oversight fees and that these fees be deposited to the Oil Field Cleanup Fund. Railroad Commission rules regarding the VCP were adopted in June 2002 (16 TAC, Chapter 4, Subchapter D). The purpose of the VCP is to provide an incentive to lenders, developers, owners, and operators to remediate soil and water that have been environmentally impacted by activities over which the Commission exercises jurisdiction. The program removes the liability to the lenders, developers, owners, and operators who did not cause or contribute to contamination by offering a release of liability. In return for the release of liability, the State offsets oversight costs through the collection of fees, reduces the need for state-managed cleanup activities, and expedites the return of contaminated properties into productive use.

S.B. 310 structured the VCP in a sequential fashion: 1) an application (with application fee of \$1,000) and acceptance process, 2) agreement execution process, 3) cleanup with Commission oversight process, and finally 4) issuance of a VCP Certificate of Completion. The Commission oversight includes review of work plans and reports to ensure the protection of human health and the environment.

In fiscal year 2012 there were seven new VCP applications. As of August 31, 2012, there were 27 active VCP sites. Since program inception in the summer of FY02, 48 sites have been cleaned up and certificates of completion issued.

XI. OPERATOR CLEANUP PROGRAM:

Another important function of the Commission's Oil Field Cleanup Program is the management of the Operator Cleanup Program (OCP). Operator cleanups are complex assessment and remediation activities conducted by a responsible operator, usually at environmentally sensitive sites. The program ensures that pollution outside of SWR 91 non-sensitive area oil spill cleanup requirements and beyond routine SWR 8 cleanups and closures are addressed promptly and adequately. Oversight of OCP activities is usually by staff in Austin headquarters and District Office (DO) staff. The majority of the projects are long-term remediation projects that require specialized skills to review and manage.

Importantly, environmental cleanups in this program are funded by the responsible operator. As a result, prompt review and action by the Commission may keep some of these projects from becoming state-managed projects that would need Oil Field Cleanup funds to complete the clean up. While these projects do not impose actual assessment of cleanup costs to the Oil Field Cleanup Fund, they do require considerable staff resources of employees who are paid out of the fund.

Mergers, divestitures and acquisitions of oil field properties, which routinely involve environmental assessments for asset valuation, have also contributed to the increasing number of projects for the Operator Cleanup Program. It is not uncommon for operators to discover

contamination at sites during routine environmental assessment and to subsequently seek letters of “no further action” from the Commission after completion of clean up.

The Commission tracks approximately 540 complex operator cleanups. These projects involve frequent sampling, reporting, and evaluation to ensure final cleanup is protective of the public health, safety and the environment.

Figure 19 illustrates the number of sites in the Operator Cleanup program since 1998 as of the close of each fiscal year.

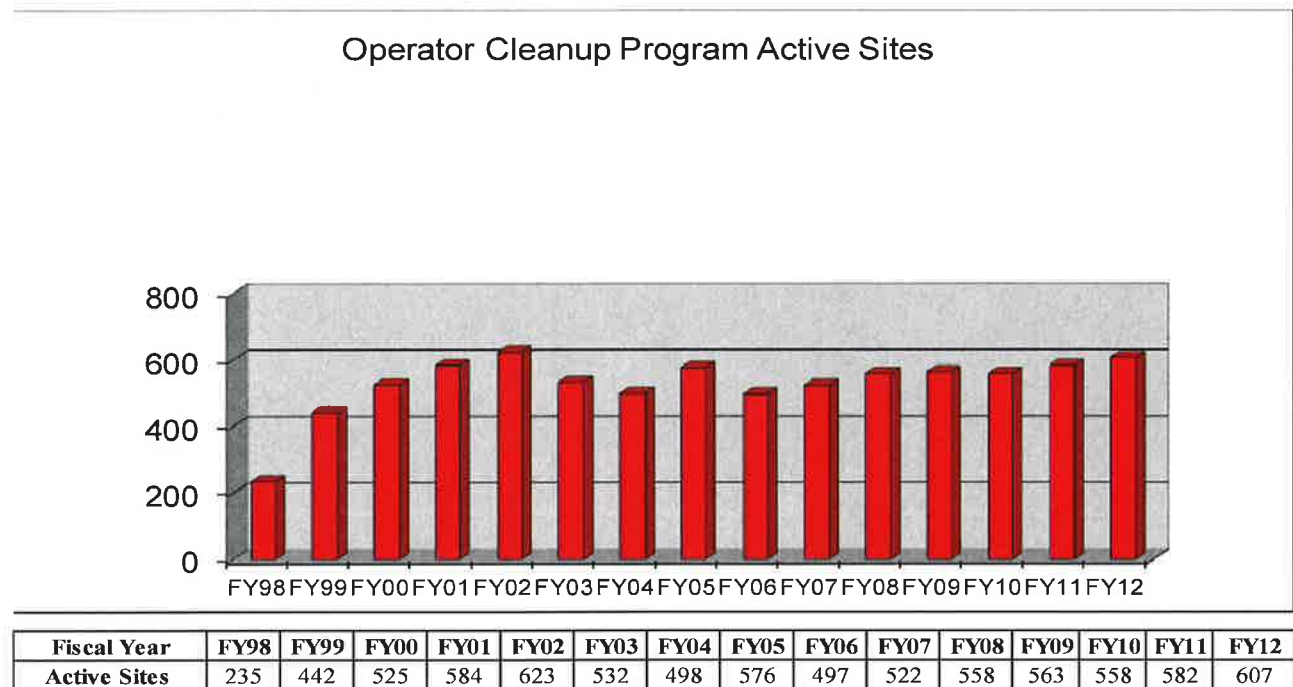


Figure 19