

How do we dismantle offshore oil structures without making the public pay?

September 7 2023, by Martin Lockman and Martin Dietrich Brauch



Credit: U.S. Bureau of Ocean Energy Management

As pressures build for the energy industry to move away from fossil

fuels, two new reports examine the risk that fossil-fuel companies will default on future obligations to decommission offshore oil and gas infrastructure and pass the costs on to the public. The reports lay out recommendations to avoid such a scenario. They were just published by the Sabin Center for Climate Change Law and the Columbia Center on Sustainable Investment (CCSI), as part of their broader [Climate Law and Finance Initiative](#).

More than 12,000 [offshore oil](#) and gas installations straddle the globe, and industry analysts anticipate annual offshore oil and gas investments to reach [\\$173 billion by 2024](#). A number of oil companies are expected to [significantly expand](#) their offshore drilling activities in the coming years.

At the same time, many jurisdictions face a growing need to dismantle offshore infrastructure, whether because it is aging, the resources are depleted, or mandated net-zero strategies require some installations to be decommissioned earlier than expected—a process that is can be [laborious and expensive](#). A 2021 forecast by the financial analysis firm IHS Markit estimated that globally, offshore decommissioning could cost nearly \$100 billion between 2021 and 2030, a period that S&P Global Commodity Insights has described as a potential "[decade of offshore decommissioning](#)." Some experts have predicted that decommissioning costs may increase significantly. in coming years.

The Intergovernmental Panel on Climate Change projects that [greenhouse gas emissions](#) from existing and planned fossil-fuel infrastructure will push global warming past [the Paris Agreement's 1.5°C threshold](#). A separate study of [detailed regional projections](#) estimates that nearly 60% of known oil and gas reserves must remain in the ground to keep within that budget.

Increased public focus on reducing greenhouse emissions, coupled with

the global push for electrification and declining prices for [renewable energy](#), may cause a [rapid decline](#) in oil and gas demand that [forces the mass closure of offshore installations](#). Even without policy changes or concerted climate action, the increasing adoption of renewable energy systems and energy-efficient technologies is [likely to depress demand for fossil fuels](#).

These combined dynamics may create serious risks for the public in a rapid phase-out scenario. Most countries with significant offshore oil and gas resources have [laws, regulations, and contracts](#) that require companies to bear the cost of decommissioning. A formal assignment of legal liability, however, does not guarantee that decommissioning will occur, or that funds will be available when obligations arise.

Governments often sit as the "[decommissioner of last resort](#)," and if oil companies default in their obligations, the public will be left footing the bill.

The legal and economic tools that states have used to ensure that oil companies pay up were often adopted without much, if any, consideration to climate change or the transition to clean energy. As a result, a rapid phase-out of offshore oil and gas could cause a series of defaults and create a serious risk of immense financial burdens for governments of oil- and gas-producing jurisdictions. In turn, delayed, inadequate or nonexistent decommissioning could cause [enormous environmental harm](#) to the world's oceans and marine life.

A [joint framing report](#) by the two centers identifies risks in decommissioning regimes around the world and provides recommendations to strengthen them. To protect the public and ensure that oil companies meet their obligations, the report recommends that governments, policymakers and industry participants take four key steps.

First, jurisdictions should create and regularly update comprehensive

decommissioning plans. Some jurisdictions prepare such plans only when an installation or field is approaching the end of its usable life. This may create bottlenecks in a rapid phase-out scenario, where facilities may need to be quickly taken down long before the ends of their previously anticipated lifespans.

Second, jurisdictions should reexamine the mechanisms aimed at assuring that companies will pay. Legal mechanisms like collateral packages, guarantees and funding structures are often predicated on assumptions that oil and gas assets will remain valuable, and that oil companies will remain solvent. With the transition away from fossil fuels, these assumptions may be incorrect.

Third, policymakers and industry participants who are planning for decommissioning expenditures should ensure that they are aware of, and prepared for, the tax implications of a rapid phase-out affecting the entire oil and gas industry.

Finally, governments should be aware that stabilization clauses in investor-state contracts may shift or create additional burdens related to offshore decommissioning. Governments should consider modifying such clauses in line with international best practices to allow them to mandate early decommissioning if offshore assets become legally impaired or otherwise "stranded" by the transition away from [fossil fuels](#)

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[The second report](#), by the Columbia Center on Sustainable Investment, assesses decommissioning provisions in investor–state oil and gas contracts in 24 international jurisdictions. To avoid a scenario where the government must cover decommissioning costs, the report recommends creating a dedicated fund sufficient to cover all costs, prefunded by the oil and gas company as part of its capital and operating expenses; contributions would be assured by the ultimate parent company

beginning before project construction.

It also recommends including provisions governing decommissioning as an integral stage occurring at the end of the project, not as a post-project activity. These provisions would factor in health, environmental, safety, and financial risks throughout the project's life cycle.

Separately, the Sabin Center submitted an August [comment letter](#) in response to a rule proposed by the U.S. Bureau of Ocean Energy Management, which governs offshore activities. The bureau is [considering a rule](#) that would revise the financial mechanisms that the United States uses to secure offshore decommissioning obligations. While the comments are broadly supportive of the Biden administration's efforts to strengthen the bureau's mechanisms, it provides several technical recommendations to protect the public against oil company defaults related to climate action.

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