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The AER Quietly Implemented a Two-Tier Mandatory Closure Spend Target

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Regulatory Change Commented On: The AER's Inventory Reduction Program

Starting in mid-2021, the Alberta Energy Regulator (AER) adopted a new liability management framework to address the problems of inactive conventional oil and gas assets. The new liability management framework includes mandatory closure spend targets, a requirement for companies to spend a certain amount on closure work each year. The mandatory closure spend targets deal with the liabilities of inactive assets and not orphan assets (it is not to be confused with the orphan fund levy, used to fund the Orphan Well Association that abandons and remediates wells with owners that went bankrupt).

In earlier blogs (here and here), I complained about the lack of transparency in how the mandatory spend targets were being set (both industry-wide and for individual companies). To my surprise and confusion, the AER updated their webpage for the mandatory closure spend targets sometime between August 12, 2022 and October 21, 2022 to include some explanation under the headings "Mandatory Targets" and "Licensee-level Target Calculation formula". Surreptitiously adding information in the middle of webpages is an odd way for a public regulator to operate, but better late than never.

In any event, the AER explains their process like this:

> A licensee's financial capability is used to set appropriate closure targets using a two-target rate approach. Licensees with a high level of financial distress, who hold approximately 10% of the industry's inactive liability, will receive a lower target rate than those not in financial distress. The intent is for all licensees to conduct closure work; the AER enables this by assessing their capability to complete closure work and providing oversight and performance managed through other Liability Management Framework (LMF) programs in addition to closure targets.
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> **Licensee-level Target Calculation formula:**
> Licensee Mandatory Closure Spend Target **=** Licensee Inactive Liability **X** Target Rate
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> *Target Rate = % of inactive liability to be spent on closure*

Year	Higher Target Rate	Lower Target Rate
2022	4.0%	3.3%

Year	Higher Target Rate	Lower Target Rate
2023	6.7%	3.6%

A few notes on the new information. First, we finally have a clear answer for how the mandatory closure spend targets are calculated. They are a percentage of each company's inactive liability as calculated by the AER, confirming that the mandatory closure spend target is based on the previous area-based closure program, which took the same approach to setting the voluntary targets for spending on inactive liability.

Second, the AER has carved out a special lower-spend requirement for those companies with "a high level of financial distress". This policy is probably a mistake. The AER's history of bending regulations to keep failing companies afloat led to companies' accumulating abandonment and reclamation liabilities far exceeding the value of their assets before they entered bankruptcy. The AER should be quickly petitioning oil and gas companies that cannot meet their regulatory obligations into bankruptcy so their remaining assets can be sold to fund the Orphan Well Association. The AER's job is to weed out failed companies to protect Alberta's finances and the overall health of the industry, not to keep failing companies afloat.

To conclude, the AER appears to have made another decision that weakens Alberta's liability management framework behind closed doors with no public comment and with almost no public notice. Who the AER consulted about the decision, if anyone, is not clear. The AER should stop doing this sort of thing. The mandatory closure spend targets could be a useful tool to deal with the inactive liability problem and restore some confidence in the AER if the program's design was not so secretive.

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