



REPORT OF
THE
STATE AUDITOR

Oil and Gas Conservation Commission

Financial Review
August 2001

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This report contains the results of a financial review of the Oil and Gas Conservation Commission. The audit was conducted pursuant to Section 2-3-103, C.R.S., which authorizes the State Auditor to conduct audits of all departments, institutions, and agencies of state government. The report presents our findings, conclusions, and recommendations, and the responses of the Oil and Gas Conservation Commission.

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Oil and Gas Conservation Commission Financial Review August 2001

Authority, Purpose, and Scope

This financial review of the Oil and Gas Conservation Commission was conducted under the authority of Section 2-3-103, C.R.S., which authorizes the State Auditor to conduct audits of all departments, institutions, and agencies of state government. The audit was conducted according to generally accepted auditing standards. The audit work; which included gathering information through interviews, reviewing documents, and analyzing data; was performed between February and May 2001.

The purpose of this audit was to review the procedures and controls over financial assurance, permits, violation orders, revenue, and expenditures. We gratefully acknowledge the assistance and cooperation of staff at the Commission in completing this audit. The following summary provides highlights of the comments, recommendations, and agency responses contained in the report.

Overview

The Oil and Gas Conservation Commission is a unit within the Department of Natural Resources. The Commission is responsible for regulating oil and gas operations in the State to prevent adverse environmental impacts. Some of the Commission's responsibilities include: establishing rules and regulations governing oil and gas development, issuing permits, enforcing laws and regulations, and obtaining financial assurance from operators to ensure the proper reclamation of well sites. In Fiscal Year 2001 the Division employed about 35 FTE and had estimated expenditures of about \$4.3 million.

Deficiencies Exist in the Management of Financial Assurance

Prior to beginning oil or gas operations in the State, an operator must submit some form of financial assurance to the Commission. Financial assurance shows that an operator is financially capable of fulfilling obligations imposed by statutory requirements and Commission rules and regulations. The Commission has the authority to establish the amount of financial assurance required and to approve all forms of financial assurance submitted by operators. As of December 31, 2000, the Commission had approximately \$22.5 million in operator-provided financial assurance.

For further information on this report, contact the Office of the State Auditor at (303) 866-2051.

SUMMARY

During our audit we found that financial assurance provided by operators was not always sufficient to cover the actual costs incurred to plug a well and/or reclaim a well site. During Fiscal Years 1995 through 2000, the Commission plugged 159 wells for a total cost of \$1.2 million. Of this amount, \$314,000 was spent because the financial assurance provided by operators was insufficient to cover actual plugging costs. In cases such as these, the Commission uses monies from the Environmental Response Fund (i.e., severance tax revenue and monies derived from other taxes on production) to pay plugging costs. We are concerned with this practice because it results in all operators paying costs that individual operators should bear.

In Fiscal Year 1995 the Commission conducted a study to obtain data on the costs to plug a well. This information was used to determine the reasonableness of the Commission's existing financial assurance requirements. Even though the costs of plugging a well periodically change, the Commission has not reevaluated its financial assurance requirements since 1995. **Therefore, we recommend that the Oil and Gas Conservation Commission periodically review the reasonableness of its financial assurance requirements to ensure they are sufficient to cover the costs associated with plugging and abandoning wells and/or reclaiming well sites.**

We also found that the Commission does not routinely attempt to obtain reimbursement from operators in cases where financial assurance is insufficient to cover the actual costs for reclaiming a well site and/or plugging a well. Statutes direct the Commission to recover its excess costs; however, the Commission does not have any procedures in place to ensure compliance with these statutory requirements. As a result, the Environmental Response Fund must be used to pay these expenses even though the Commission should take steps to recover its excess costs from individual operators. **The Oil and Gas Conservation Commission should establish procedures to recover excess costs from operators in cases where financial assurance is insufficient to cover total plugging and abandonment costs.**

Once operations on a well site have ceased, the Commission must observe the site over a period of two growing seasons to ensure that proper reclamation has occurred. After this period has passed and the Commission conducts a final inspection to ensure reclamation is complete, an operator's financial assurance may be released. We tested 25 cases to determine whether financial assurance had been released in a timely manner following a final inspection. In five instances we found that documentation supporting the completion of a final inspection was not sent to the staff person responsible for releasing financial insurance. This resulted in four of the five operators' financial assurance being released between four months and two years after the final inspection had occurred. **The Oil and Gas Conservation Commission should**

develop procedures to ensure that appropriate staff are notified when a final inspection has been completed so that financial assurance can be released in a timely manner.

The Commission allows operators to submit financial assurance in the form of certificates of deposit. As of December 31, 2000, the Commission had approximately \$2 million in certificates of deposit recorded on the State's accounting system. The Commission conducts a yearly confirmation process to verify the existence and worth of these certificates. As part of our audit, we sent confirmation letters to outside financial institutions for 83 certificates totaling \$1.4 million. We could not confirm three certificates totaling \$40,000. In addition, we found that the Commission begins its confirmation process four months prior to fiscal year-end, thereby increasing the risk that the year-end account balance recorded on the State's accounting system is inaccurate. Finally, we found that the Commission did not send a second request for unreturned confirmations until June—three months after its original confirmation requests are sent. More timely follow-up procedures are needed to ensure that confirmation requests are received in a prompt manner and do not “fall through the cracks.” **Therefore, we recommend that the Oil and Gas Conservation Commission change the timing of its confirmation process from the beginning of March to on or after March 31, and follow up on confirmations that have not been returned in a timely manner.**

Documentation Related to Penalty Assessments Needs Improvement

The Commission assessed \$81,500 in penalties for the period July 1, 2000, to January 31, 2001. All penalties are calculated using base amounts that range from \$250 to \$1,000, depending upon the violation involved. Base penalty amounts are established in the Commission's rules and regulations. The Commission may adjust penalty amounts to account for aggravating or mitigating factors, which are also established in rule. We reviewed 12 penalties that had been assessed during the aforementioned time period and found that 5 did not agree to the base fine amounts set forth in the Commission's rules and regulations. Although it appeared that the Commission adjusted these penalties on the basis of aggravating or mitigating circumstances, there was no documentation that showed how these factors were figured into the penalty calculations. **We recommend that the Oil and Gas Conservation Commission improve its documentation of the aggravating and/or mitigating factors that are used to determine individual penalty assessments.**

Travel Practices Need to Comply with State Policies

The Commission has been authorized to use 11 travel cards for airfare, hotel accommodations, rental cars, cash advances, and miscellaneous expenses associated with staff travel. The total amount of Commission expenditures for travel card purchases was approximately \$16,000

from the period of July 1, 2000, through February 28, 2001. We noted two problems with Commission practices regarding travel cards. First, the Commission does not maintain receipts to support travel-related business expenses as required by State Fiscal Rules. Specifically, we found that 25 payments, or 71 percent of all travel card payments made during the abovementioned period, had little or no supporting documentation. Second, the Commission is not adhering to a Department of Natural Resources policy that requires employees to pay the credit card company for travel expenses and then request reimbursement from the Commission. Instead, the Commission is remitting payment directly to the credit card company. The Department's policy protects the State from financial liability for unauthorized travel card purchases. As such, the Commission should require its employees to adhere to it. **The Oil and Gas Conservation Commission should maintain adequate supporting documentation for all travel expenditures and follow written policies established by the Department of Natural Resources regarding the payment of travel card expenses.**

Expand Oil and Gas Information System Capabilities and Improve Information Management

In recent years the Commission has revamped its computer system to provide a more reliable and efficient means of maintaining and disseminating information to interested parties. Even with these recent improvements, however, we found areas where the information system could be further improved. For example, the Commission could further increase the number of operators who file production reports electronically, thereby reducing the need for manual data entry processes. In addition, we found that information made available to the public through the Commission's Web site and other formats is sometimes inaccurate or incomplete. **To address these concerns, the Oil and Gas Conservation Commission should expand the capabilities of the Colorado Oil and Gas Information System and periodically review all internally generated reports and the contents of its Web site to ensure the information it disseminates is both complete and accurate.**

Summary of Agency Responses to the Recommendations

The Oil and Gas Conservation Commission agrees with all of our recommendations. The Recommendation Locator (found on pages 5 and 6) provides an overview of the Commission's responses to the recommendations and its estimated implementation schedule.

RECOMMENDATION LOCATOR
Agency Addressed: Oil and Gas Conservation Commission

Rec. No.	Page No.	Recommendation Summary	Agency Response	Implementation Date
1	15	Determine the reasonableness of financial assurance requirements by assessing the costs to plug and abandon a well and/or reclaim a well site to its original condition on a periodic basis.	Agree	10/01/03
2	16	Establish procedures to recover plugging and abandonment costs from operators in cases where financial assurance is not sufficient. Take immediate action to recover costs incurred in the last two fiscal years.	Agree	9/30/01
3	18	Develop procedures to ensure that appropriate parties are notified when a final inspection of a well site has been completed so that financial assurance can be released in a timely manner.	Agree	6/30/02
4	19	Develop procedures for an annual review of financial assurance submitted in the form of a performance guarantee.	Agree	6/30/02
5	22	Consider changing the timing of the confirmation process from the beginning of March to on or after March 31, and make adjustments for additions and deletions from this date to fiscal year-end. Follow up on confirmations that have not been returned within 30 days of the original confirmation date.	Agree	4/30/02
6	22	Develop procedures to ensure the Commission is notified of account information changes in a timely manner.	Agree	6/30/02
7	24	Improve the process for handling complaints.	Agree	1/01/02

RECOMMENDATION LOCATOR
Agency Addressed: Oil and Gas Conservation Commission

Rec. No.	Page No.	Recommendation Summary	Agency Response	Implementation Date
8	27	Document the aggravating and/or mitigating factors that are used to determine individual penalty assessments.	Agree	Implemented
9	27	Analyze historical collection rates in order to establish procedures to determine an allowance for doubtful accounts.	Agree	Implemented 7/26/01
10	30	Maintain adequate supporting documentation for all travel card transactions.	Agree	Implemented
11	31	Follow written policies established by the Department of Natural Resources regarding the payment of travel card expenses.	Agree	Implemented
12	32	Follow written policies and procedures to ensure that invoice approval is documented and payment vouchers are approved by the appropriate person.	Agree	Implemented
13	33	Continue the transition to an automated information system.	Agree	11/30/04
14	36	Make various record-keeping improvements.	Agree	12/31/02

Description of the Colorado Oil and Gas Conservation Commission

Overview

The Colorado Oil and Gas Conservation Commission, a unit within the Department of Natural Resources, is statutorily responsible for the protection of public health, safety, and welfare; the environment; and mineral owners' rights. The Commission also has the authority to regulate oil and gas operations to prevent significant adverse environmental impacts. The mission of the Commission is to promote the responsible development of Colorado's oil and gas natural resources. Currently Colorado has approximately 23,000 active oil and gas wells, and an additional 40,000 plugged and abandoned wells. A significant number of the State's active wells, approximately 10,000, are located in Weld County. The remaining wells are located throughout 41 of the State's other 63 counties.

Organizational Structure

The Commission comprises seven commissioners. Commissioners are appointed by the Governor and confirmed by the Senate. They are responsible for enforcing the orders, rules, and regulations for oil and gas activity in the State. The Commission holds monthly hearings to consider issues such as well spacing, rule violations, and levy amounts. (In this audit report, references to the "Commission" refer to the organization and not to the agency's Commissioners.) In addition, the Commission has 35 full-time equivalent (FTE) staff, classified into three main functional areas as described in the following table:

Oil and Gas Conservation Commission Responsibilities by Functional Area	
Functional Area	Main Responsibilities
Administration and Hearings 8 FTE	<ul style="list-style-type: none"> • Planning and forecasting budgets. • Administering appropriations from the Conservation and Environmental Response Funds, the Severance Tax Operational Account, and the Underground Injection Control Federal Grant. • Maintaining the public data room. • Responding to inquiries and investigating complaints. • Assisting the Commission in conducting hearings.
Information 12 FTE	<ul style="list-style-type: none"> • Compiling and storing well, production, and levy information. • Reviewing all drilling applications for regulatory compliance. • Ensuring operators meet financial assurance requirements. • Managing the Commission's database and Web site.
Operations 15 FTE	<ul style="list-style-type: none"> • Reviewing and approving production and abandonment applications. • Performing field inspections. • Responding to inquiries and investigating complaints. • Monitoring operations for compliance with Environmental Protection Agency rules and regulations. • Managing projects using the Environmental Response Fund.
Source: Department of Natural Resources' Fiscal Year 2001 Budget Request.	

Financial Overview

The Commission is funded by three primary sources: the Conservation Levy (cash funds), the Severance Tax Operational Account (cash funds), and federal funds from an Environmental Protection Agency grant. The Commission also receives revenue from fines and fees. The table on the following page shows the funding sources for the Commission for Fiscal Years 1998 through 2001:

Oil and Gas Conservation Commission Funding Sources Fiscal Years 1998-2001				
Source	FY 1998 (Actual)	FY 1999 (Actual)	FY 2000 (Actual)	FY 2001 (Estimate)
Cash Funds	\$ 2,803,240	\$ 3,016,892	\$ 3,749,982	\$ 4,526,538
Federal Funds	105,349	95,827	113,882	133,064
Total	\$ 2,908,589	\$ 3,112,719	\$ 3,863,864	\$ 4,659,602
Source: COFRS records.				

The Commission's expenditures for the same fiscal years are shown in the following table:

Oil and Gas Conservation Commission Expenditures and Disbursements Fiscal Years 1998-2001				
Expenditures	FY 1998 (Actual)	FY 1999 (Actual)	FY 2000 (Actual)	FY 2001 (Estimate)
Personal Services	\$ 1,581,296	\$ 1,692,290	\$ 1,795,457	\$ 1,887,885
Operating Expenses	143,000	179,351	196,429	300,447
Executive Director's Office Administration	257,506	259,398	293,446	321,842
Accelerated Drilling Projects	217,319	228,857	250,750	267,838
Well Plugging and Reclamation	210,331	218,475	219,701	193,214
Environmental Assistance Projects	163,872	179,254	179,915	141,853
Natural Resources Indirect Cost Assessment	151,981	156,644	142,051	187,101
Underground Injection Control	95,918	85,876	95,619	80,303
Other Expenditures*	134,728	339,830	339,468	905,014
Total	\$ 2,955,951	\$ 3,339,975	\$ 3,512,836	\$ 4,285,497
Source: COFRS records and Commission estimates.				
* Other expenditures include mineral audits and the cost of various projects and studies. The Fiscal Year 2001 total includes two new projects (i.e., a Raton Basin water study and an information management project).				

In years when the amount of revenue collected by the Commission does not match its expenditures, the Commission is either adding to or subtracting from its reserves (fund balance). The Commission has the authority to use these reserves, since its fund balance does not revert to the General Fund at fiscal year-end. The tables also show that the Commission's revenue increased about 60 percent, and expenditures increased about 45 percent over the period shown. These increases are due to recent price increases within the oil and gas industry. Higher prices have resulted in an increase in the revenue that the Division receives from the Conservation Levy and severance taxes. Increased revenue, in turn, has enabled the Commission to undertake additional projects (e.g., enhancements to its computer system and new environmental studies).

Oversight of Oil and Gas Operations

Chapter 1

Overview

The Oil and Gas Conservation Commission is responsible for regulating oil and gas operations in the State. In order to oversee these operations, the Commission issues permits for the drilling and operation of oil and gas wells, enforces regulations regarding well production and reclamation, and ensures that the plugging and abandonment of wells is performed according to Commission guidelines. In addition, the Commission is responsible for ensuring that operators provide financial assurance for their oil and gas operations. Finally, the Commission may assess penalties against an operator for noncompliance with statutes and Commission rules and regulations.

Operators Are Required to Provide Financial Assurance

Prior to beginning oil and/or gas operations in the State, an operator must submit some form of financial assurance to the Commission. Section 34-60-106(13), C.R.S., states that this assurance shows that an operator is financially capable of fulfilling obligations imposed by statutory requirements and Commission rules and regulations. These obligations include the proper reclamation of land and soil affected by oil and gas operations. Operators may submit any of the following forms of financial assurance:

- Performance guarantee
- Certificate of general liability insurance
- Bond or another surety instrument
- A letter of credit, certificate of deposit, or another type of financial instrument
- An escrow account or sinking fund
- A lien or another type of security interest in real or personal property

The Commission has the authority to establish the amount of financial assurance required and to approve all forms of financial assurance submitted by operators. As part of its rules and regulations, the Commission sets the amount of financial

assurance for different types of circumstances, such as surface owner protection, seismic operations, soil protection, and plugging and abandonment. Rules and regulations require that financial assurance remain in place until the operator has complied with statutory obligations or until assurance is provided by a successor operator. If an operator fails to fulfill his or her obligations, however, the Commission can foreclose on the financial assurance and use the funds to plug wells, perform site reclamation, or conduct other types of environmental activities. In these situations, the Commission will use whatever financial assurance an operator has provided; however, if the financial assurance is not sufficient to cover all costs, the Commission will utilize funds from its Environmental Response Fund. Monies in the Environmental Response Fund come from severance taxes and revenue derived from other taxes on production.

The amount of financial assurance required by an operator depends on the size and type of the oil and gas operation. Assurance amounts range from \$2,000 to \$100,000. As of December 31, 2000, the Commission had approximately \$22.5 million in operator-provided financial assurance. Of this amount, approximately \$2.4 million was in the form of cash bonds, certificates of deposit, money market accounts, letters of credit, escrow accounts, and guarantees of performance. These types of financial assurance are currently recorded on the State's accounting system. The remaining \$20.1 million in financial assurance is in the form of insurance bonds, which are not recorded on the State's accounting system.

Deficiencies Exist in the Management of Financial Assurance

During our audit we reviewed the Commission's policies and procedures for financial assurance. We identified several areas that need improvement. Specifically, we found that the Commission has not:

- Performed a recent assessment of the costs to plug and abandon a well and/or reclaim a well site to its original condition.
- Fully recovered excess plugging and reclamation costs from operators when their financial assurance was insufficient to cover these costs.
- Developed consistent internal procedures to notify the financial assurance administrator when a final inspection of a well site has been completed.
- Developed procedures so that it can perform an annual review of performance guarantees as required by statute.
- Instituted a method for identifying changes in financial assurance instruments held by financial institutions.

The following narrative provides further detail on each of these issues.

Recovery Costs Exceed Applicable Operator Funds

As stated previously, the Environmental Response Fund is used to cover the costs to plug and/or reclaim a well site if a responsible party cannot be located. If an operator's financial assurance does not cover the actual cost for reclamation and/or plugging a well, monies from the Environmental Response Fund are utilized. This fund receives money for these purposes from severance taxes and financial assurance that has been called or foreclosed upon by the Commission.

We reviewed the actual costs to plug wells during Fiscal Years 1996 through 2000. During this period the Commission plugged 159 wells for a total cost of about \$1.2 million. We noted that about \$888,000, or 74 percent, of the total cost for plugging these wells was covered by the Environmental Response Fund. Of this amount, about \$574,000 was spent because the Commission assumed responsibility for abandoned wells when a responsible party could not be located. The remaining amount, about \$314,000, was spent because the financial assurance provided by operators was insufficient to cover actual plugging costs.

In total, 101 of the 159 wells had some form of financial assurance to offset all or part of their plugging costs. Only 15 (15 percent) of these wells, however, had financial assurance sufficient to cover all costs, while the remaining 86 wells did not. Specifically, we found the following:

- **Blanket bonds did not provide sufficient assurance to cover 76 wells.** If an operator has a large number of wells (up to 100), he or she may submit a blanket bond in an amount between \$25,000 and \$50,000, depending on the type of operation. We found that 89 out of the aforementioned 101 wells were covered by blanket bonds totaling \$320,000. Of these 89 wells, the blanket bond was not sufficient to cover the costs of plugging 76 wells (85 percent). The excess costs of approximately \$230,000 were covered by the Environmental Response Fund.

In one specific case, we found that an operator had a blanket bond in the amount of \$30,000 to cover the plugging of 12 wells. The actual cost for plugging these wells was approximately \$106,000. In another instance, we found that one operator had a blanket bond in the amount of \$30,000 to cover 17 wells. The actual cost for plugging these wells was approximately \$97,000.

- **Individual bonds did not cover the costs of plugging ten wells.** Instead of submitting a blanket bond, an operator may submit financial assurance to cover an individual well. The majority of individual bonds are in the amount of \$5,000. We found that 12 out of the 101 wells in our sample were covered by individual bonds totaling \$60,000. Of these 12 wells, the individual bonds were not sufficient to cover the costs of plugging 10 (83 percent). The excess costs of approximately \$84,000 were covered by monies from the Environmental Response Fund.

In one specific instance, we found that an operator had a bond for \$5,000 to cover the plugging of one well. The actual cost to plug this well was approximately \$23,000. In another instance, we found that one operator had two bonds for \$5,000 each to cover two wells. The actual cost for plugging these wells was \$24,000.

In all of these instances, excess costs were paid by the Environmental Response Fund.

The Commission Is Not Complying With Statutes Regarding Recovery of Excess Costs

We also found that the Commission does not routinely attempt to obtain reimbursement from operators in cases where the excess costs of plugging a well must be borne by the Environmental Response Fund. Statutes authorize the Commission to require operators to meet certain obligations, including performing reclamation projects. If an operator refuses to comply with these requirements when abandoning a well, or a responsible party cannot be located, the Commission may authorize expenditures from the Environmental Response Fund. According to Section 34-60-124(7), C.R.S., “the Commission shall bring suit in the second judicial district to recover such expenditures from any responsible party who refuses to perform such mitigation...within a two-year period from the date that final expenditures were authorized.” Currently the Commission does not have any procedures in place to ensure compliance with this statutory requirement (e.g., criteria defining the situations when a court action will be pursued). As a result, the Environmental Response Fund is being used to cover costs that should be paid by individual operators. Due to the time frame established in statute, the Commission should take immediate legal action necessary to recover any costs spent in the last two fiscal years.

Average Cost to Plug a Well Exceeds Minimum Financial Assurance Requirements

In Fiscal Year 1995 the Commission conducted a study to obtain data on the costs to plug a well. This information was used to determine the reasonableness of the Commission's existing financial assurance requirements. The Commission used statewide actual cost data to calculate an average cost of about \$5,000, an amount approximately the same as the average amount of financial assurance required of an operator at that time.

Even though the costs of plugging a well periodically change, the Commission has not reevaluated costs since 1995. As previously mentioned, we reviewed the actual costs to plug wells during Fiscal Years 1996 through 2000 and found that the Commission plugged 159 wells for a total cost of about \$1.2 million during this period. The actual costs to plug these wells ranged from about \$2,000 to \$98,000. The average cost was about \$7,600 a well—almost 150 percent of the current financial assurance requirements for one well site (\$5,000).

The Commission should update its cost study to determine whether existing financial assurance requirements should be modified and this study should be updated periodically (e.g., at least biennially). If studies show that adjustments to the financial assurance requirements are needed, the Commission should ensure that all the financial assurance it currently holds reflects the adjustment. This may require obtaining additional financial assurance from some operators. By doing this, the Division will help ensure that funds from the Environmental Response Fund will not be needed to pay for plugging and reclamation costs that should be borne by individual operators.

Recommendation No. 1:

The Oil and Gas Conservation Commission should periodically determine the reasonableness of financial assurance requirements by assessing the costs to plug and abandon a well and/or reclaim a well site to its original condition (at least biennially). The Commission should use this information to determine whether financial assurance requirements are sufficient to cover average plugging and reclamation costs. If adjustments are needed, the Commission should review all current operator accounts and obtain additional financial assurance if necessary.

Oil and Gas Conservation Commission Response:

Agree. The Commission first secured adequate funding to cover the costs of plugging, abandoning, and reclaiming the backlog of orphaned well sites beginning in 1996. At that time the backlog included several extraordinarily expensive pre-1950 orphaned well sites that cost on the order of \$100,000 each to plug, abandon, and reclaim. After successfully completing those very challenging projects, Commission staff then plugged, abandoned, and reclaimed 149 other well sites, which resulted in a median cost of \$5,700 per well site and average cost of \$6,300 per well site. (The Commission's figures are included in Appendix A.) The current inventory of remaining well sites to plug, abandon, and reclaim includes 103 well sites totaling \$439,500, for an average of \$4,267 per well site. (The Commission's cost estimates are included in Appendix B.) Although the list of remaining well sites to plug, abandon, and reclaim is subject to expansion and revision as new wells are added, at this time it appears that the average cost per well site of \$4,267 will be less than the bonding level per well of \$5,000. The Commission staff will biennially perform a review of the actual cost incurred to plug, abandon, and reclaim well sites. The first such review will be completed by October 1, 2003, to cover the periods Fiscal Year 2002 and Fiscal Year 2003.

Recommendation No. 2:

The Oil and Gas Conservation Commission should establish procedures to recover plugging and abandonment costs from operators in cases where financial assurance is not sufficient to cover these costs. Due to the time frame established in statute, the Commission should take immediate action to recover costs incurred in the last two fiscal years.

Oil and Gas Conservation Commission Response:

Agree. Under the statute, recovery of expended Environmental Response Fund (ERF) monies can only be sought when those ERF monies are used to mitigate a significant adverse environmental impact on any air, water, soil, or biological resource. Upon review of the past two years of ERF expenditures, there is only one case in which ERF monies were expended in a case where financial assurance was not sufficient to cover all of the costs to mitigate a significant adverse environmental impact. In this case, all of the bond funds have been expended but ERF monies are continuing to be expended to finish the project. As soon as the project is completed, recovery of those expended funds will begin immediately by referring the matter to Central Collections to first verify

that the responsible party has assets and to then bring suit to recover expended ERF monies.

In the future, the COGCC will immediately refer ERF expenditures to Central Collections in all cases where financial assurance is not sufficient to cover all of the mitigation costs once the projects are completed. Because ERF expenditures used to prevent possible significant adverse environmental impacts are not subject to recovery under the statute, the Commission will immediately begin to order any operator for whom ERF monies have been used to prevent the threat of a significant adverse environmental impact to reimburse the Fund as a condition of being able to conduct any future operations in the State. (Because most of these cases have historically involved insolvent entities, it would be unrealistic to expect a high frequency of success in recovering funds from them.)

Operators' Financial Assurance Is Not Released on a Timely Basis

Once operations on a well site have ceased, the Commission must observe the site for a period of two growing seasons to ensure that proper reclamation has occurred. After the Commission determines the well site has been properly restored (as indicated by a final inspection), an operator's financial assurance may be released. During our review we found that although final inspections usually occur as required, the Commission's financial assurance manager is not routinely notified of this fact so that an operator's financial assurance can be released.

We tested 25 bonds that had been released to determine whether a final inspection had been completed. Out of the 25 released bonds selected, only 8 were required to have a final inspection. In the remaining 17 situations, a final inspection was not required, because these bonds were released due to a change in operator, financial assurance, or bonding company. Out of the eight bonds that required a final inspection, we noted five instances where supporting documentation of the inspection was not sent to the manager responsible for releasing financial assurance. This resulted in three of the five bonds being released more than four months after the final inspection had been completed. Another bond was released more than two years after the final inspection. The remaining bond was released in a timely manner even though the appropriate notice was not sent to the financial assurance manager.

Delays in releasing financial assurance occur because there is no standard procedure for engineers to notify the appropriate staff person that a well site has passed final

inspection. A request for an inspection form is sent to the engineer conducting the final inspection of a particular well site; however, this form is not always returned to the financial assurance manager. Instead, the financial assurance manager must make telephone calls and other inquiries to determine final inspection status. If one of these methods is used, the financial assurance manager will document the communication in the operator's bond file without requiring a final inspection form from the engineer.

Significant delays between the time that the final inspection is completed and the financial assurance is released can have a financial impact on an operator. Since financial assurance is being held by the Commission, an operator may lose interest on those funds, since these monies held cannot be reinvested in other, perhaps higher-interest, investment vehicles. In addition, an operator may be paying premiums to a bonding company for financial assurance that is no longer required. These premiums typically range from \$200 to \$500 a year depending upon the bond amount. Therefore, the Commission should ensure that engineers are consistently informing the financial assurance manager when a final inspection has been completed so that financial assurance can be released in a timely manner.

Recommendation No. 3:

The Oil and Gas Conservation Commission should develop procedures to ensure that appropriate parties are notified in a timely manner when a final inspection of a well site has been completed so that, if necessary, financial assurance can be released.

Oil and Gas Conservation Commission Response:

Agree. There should be an automated procedure to notify the financial assurance administrator that a facility operated by a party requesting bond release has passed a final surface reclamation inspection. This process will be developed and implemented by June 30, 2002.

Develop Procedures for Annual Review of Performance Guarantees

Pursuant to Section 34-60-106(13)(a), C.R.S., an operator may submit financial assurance in the form of a performance guarantee. A guarantee demonstrates that the operator has sufficient net worth to ensure it is financially capable of properly plugging a well and reclaiming the land and soil affected by oil and gas operations.

Should an operator provide a performance guarantee, statutes require the Commission to perform an annual review of the guarantee and any related net worth statement.

During our audit we noted the Commission currently holds two performance guarantees. One of these guarantees was provided by a municipality, while the other was provided by an individual operator. Annual review of performance guarantees provided by municipalities can be streamlined by review of audited financial statements, which are made available to the public each year. On the other hand, the performance guarantee provided by the individual operator is over a year old and has not been reviewed as required by statute. An annual review of an individual operator's net worth will help ensure that the operator's financial resources continue to be sufficient to meet his or her statutory responsibilities regarding plugging and site reclamation. A review of net worth may include requiring an annual submission of the operator's current year financial statements and/or confirmation of ownership of properties pledged as net worth. Annual completion of this review for current and future guarantees may protect the Commission from incurring unnecessary reclamation and plugging costs at a later date.

Recommendation No. 4:

The Oil and Gas Conservation Commission should develop procedures for annually reviewing all financial assurance submitted in the form of a performance guarantee.

Oil and Gas Conservation Commission Response:

Agree. The COGCC does not routinely accept performance guarantees as a form of financial assurance. Of its total of 1,053 active financial assurance instruments, the COGCC has two performance guarantees, one with the City and County of Denver and another with a private party. The COGCC will develop criteria to review the adequacy of the individual party guarantee by consulting other states that use such financial assurances, if any, by the end of June 2002.

The City and County of Denver's performance guarantee was accepted because of the obvious perpetual existence of the entity. The other performance guarantee is with an individual for whom the Commission ordered a lien to be placed on their property where a well was located. The Assistant Attorney General advised the Commission that placing a lien on the property was not cost-effective, and that the preferred alternative was a guarantee of performance agreement. The guarantee of performance agreement was then drafted by the Assistant Attorney General and approved by the Commission.

The Commission does not plan to accept any additional performance guarantees in the future.

Certificates of Deposit Should Be Confirmed Annually

In addition to performance guarantees, the Commission allows financial assurance in the form of certificates of deposit. As of December 31, 2000, the Commission had approximately \$2 million in certificates of deposit. This amount was recorded on the State's accounting system.

The Commission's financial assurance procedures require a yearly confirmation of certificates of deposit. Confirmation is necessary to verify the existence and worth of the certificates that are recorded on the State's accounting system. The financial assurance manager performs the annual confirmation by contacting various financial institutions and following up on any discrepancies identified. This can be a time-consuming process, since the Commission holds approximately 200 certificates of deposit. Further, because account information changes frequently, follow-up activities can take staff several months. Therefore, staff begin the confirmation process at the beginning of March, which is about four months prior to the end of the State's fiscal year.

In April 2001 we sent confirmation letters to outside financial institutions to verify the accuracy and existence of 83 certificates of deposits recorded on the State's accounting system. These 83 certificates comprised about \$1.4 million of the \$2 million balance noted previously. We noted the following problems with the confirmation process:

- **We could not confirm three certificates in the amount of \$40,000.** After a three-month period, our office had not received a response for six confirmation requests (7 percent). We typically expect that 100 percent of the confirmations we send out will be returned; therefore, this response rate was lower than expected. In addition, nine confirmation requests (14 percent) were returned to our office by the financial institution indicating that the account number of the certificate of deposit could not be located. For these 15 certificates that were not verified, we reviewed the confirmations that were sent out by the Commission and were able to substantiate the accuracy and existence of 12. However, three certificates totaling \$40,000 (or about 3 percent of the total amount confirmed) were never verified through either process.

- **The Commission begins its confirmation process four months prior to fiscal year-end and does not follow up on unanswered requests in a timely manner.** As previously stated, the Commission sends out its confirmation letters in the beginning of March. One of the confirmations that we could not verify had been confirmed with the Commission in March. However, this account was closed after the Commission's confirmation and prior to our office's verification in April 2001. By completing its annual confirmation in March, the Commission is increasing the risk that the account balance recorded on the State's accounting system is inaccurate at fiscal year-end. The Commission should consider changing the timing of its confirmation process to on or after March 31 and should account for additions and deletions to the balance from this date to the end of the fiscal year. This time frame is consistent with the State Controller's Office guidelines for physical inventories. In addition, we found that the Commission did not send a second request for unreturned confirmations until June—three months after the original confirmation had been sent. The Commission should follow up on unreturned confirmations in a timely manner (e.g., within 30 days) to help ensure that confirmations do not "fall through the cracks."
- **The Commission is not notified of account information changes in a timely manner.** We found that 13 certificates of deposit, which were eventually confirmed, had account information changes during the year. These changes resulted from rollovers that were assigned new account numbers, changes in dollar amount of certificates, and changes in bank and/or operator names. As the primary account holder, operators are notified of any changes to account information by the financial institution. As a secondary account holder, however, the Commission is generally not made aware of any changes until discrepancies are noted during its annual confirmation process.

There are no procedures in place to notify the Commission when account information changes. Therefore, until the annual confirmation is performed, the Commission cannot be assured that it has accurate information on the certificates of deposit it holds as financial assurance. The Commission should develop procedures to ensure it is notified of account information changes in a timely manner so that it can keep its records updated. These procedures may include requiring operators to notify the Commission of any changes financial institutions make to their accounts, or requiring financial institutions to notify the Commission, as the joint account holder, of any changes they make to account information.

Recommendation No. 5:

The Oil and Gas Conservation Commission should consider changing the timing of its confirmation process from the beginning of March to on or after March 31, and make adjustments for additions and deletions from this date to fiscal year-end. In addition, the Commission should follow up on confirmations that have not been returned within 30 days of the original confirmation date.

Oil and Gas Conservation Commission Response:

Agree. The COGCC will move its certificate of deposit confirmation process to April of each year, beginning in 2002. If the confirmation process is moved to later in the fiscal year, there is a significant risk that the letter exchange with the financial institutions to confirm the certificates will not be completed before the end of the fiscal year (June 30th).

Recommendation No. 6:

The Oil and Gas Conservation Commission should develop procedures to ensure it is notified of account information changes in a timely manner.

Oil and Gas Conservation Commission Response:

Agree. It is already a difficult process to have the financial institutions confirm existing certificates of deposit annually to either the operators or the COGCC. The COGCC does not have the authority to enforce a requirement that financial institutions provide notification of account number changes. A statutory change would be necessary to provide such authority to the Commission.

The Division of Banking currently requires quarterly reporting of all Public Deposit Protection Act (PDPA) account balances and annual reporting of all PDPA account numbers and balances. The Commission will pursue development of a process to cross-check PDPA account numbers with the Division of Banking by the end of June 2002.

The Commission's Complaint-Handling Procedures Need to Be Improved

The Commission routinely receives complaints regarding oil and gas operations throughout the State. For instance, individuals may contact the Commission to report concerns regarding damage to personal property, noise levels, or water quality issues. Any party who may have been adversely affected as a result of an alleged violation may make a complaint to the Commission either by phone or in writing. Responding to citizen complaints and concerns is an important responsibility for any governmental agency. Prompt, appropriate handling of complaints shows that an agency is responsive, accountable, and concerned with the quality of its services.

In Calendar Year 2000 the Commission received approximately 210 complaints. The majority of the complaints received (about 140) were regarding environmental damage allegations, noise concerns, requests for water testing, and site reclamation problems. We reviewed 25 complaints that had been received by the Commission during the period of April 2000 through April 2001. During our review we noted that the Department's complaint-handling processes need improvement. Specifically, we found that the Commission does not:

- **Track complaint resolution to ensure timeliness of response.** One of the Commission's performance objectives is to initially respond to complaints within two days of their receipt. During our audit we noted that there is no process in place to track how quickly the initial response to a complaint occurs. Therefore, we could not determine whether the Commission staff were following up on complaints in a timely manner to meet this objective.
- **Consistently enter complaint information into its database.** One staff member told us that he does not enter complaint information into the Commission's database until after the complaint has been sufficiently resolved, while other staff enter the information when they first receive a complaint and then update it as new information becomes available. Since staff are not consistently entering information into the Commission's database, the Commission cannot ensure that complaints are not "falling through the cracks." In addition, we could not determine whether the number of complaints that the Commission reported for the above-mentioned time period is accurate. This is because staff enter complaint information into the Commission's database at different times. Finally, members of the public may be limited in their ability to access complete and accurate data regarding the status of their complaint, since complaint information from the Commission's database is available through its Web site.

- **Accurately categorize all complaints received to identify problem areas.** When a complaint is received, a staff member classifies the complaint into one of five categories: environmental damage, noise, payment, site maintenance, and “other.” Of the total complaints reported for Calendar Year 2000, we found that approximately 75 complaints (36 percent) were classified as “other.” Unless complaint information can be categorized more accurately, the Commission is limiting its ability to analyze the information to identify problem areas. The Commission can also use complaint information to focus enforcement strategies and provide education to staff members and/or operators, but it cannot do this without better categorization and more thorough analysis.

In addition, we noted that the Commission does not have formal, written policies and procedures relating to complaints. By developing these procedures, the Commission could better mitigate the problems identified above and ensure that complaints are handled consistently.

Recommendation No. 7:

The Oil and Gas Conservation Commission should improve the process for handling complaints by:

- Tracking complaint resolution to ensure responses occur in a timely manner.
- Entering complaint information into the database in a consistent manner.
- Accurately categorizing complaints received in order to identify potential problem areas.
- Developing formal policies and procedures relating to complaints.

Oil and Gas Conservation Commission Response:

Agree. The COGCC has attempted to utilize the new computer system to track complaints but has been unsuccessful due to current system limitations. The remotely located employees receive a significant number of the complaints, but are not able to input the complaints they receive into the database. This has resulted in inconsistent complaint information in the database.

By January 1, 2002, the COGCC will develop temporary, interim procedures to utilize the existing computer system as much as possible until system limitations have been resolved. The COGCC will work with the Department of Natural Resources to identify options to develop computer system applications that will permanently correct this problem.

Penalty Assessment and Collection Needs Improvement

As previously mentioned, the Commission receives complaints for any number of reasons including spills, noise, and property damage. Any complaint made to the Director requires an investigation by an inspector or engineer close to the operation. Often complaint investigations will cause the Commission to cite a violation against an operator. There are three types of violations the Commission may issue, as follows:

- **Notice of Alleged Violation (NOAV).** The Commission may issue an NOAV on the basis of information obtained through a complaint or an inspection. NOAVs are issued when an operator has violated a Commission rule, regulation, or law. After the NOAV has been issued, the operator has the opportunity to resolve issues in order to comply with provisions of the notice. According to the Commission's April 2001 Monthly Staff Report, 244 NOAVs were issued in Calendar Year 2000.
- **Administrative Order by Consent (AOC).** NOAVs that are not resolved by a written agreement or that have a penalty imposed may be resolved by negotiations between the operator and Commission. If an agreement for correction and abatement is made, an AOC is issued. This agreement is reviewed by the Commissioners, and if approved, a penalty is imposed. According to the Commission's April 2001 Monthly Staff Report, 13 AOCs were issued in Calendar Year 2000.
- **Order Finding Violation (OFV).** If an operator contests the existence of a violation, the proposed corrective action, or the penalty assessed, staff may recommend the issuance of an OFV. These matters are heard at a meeting of the Commissioners, and a penalty may be imposed. According to the Commission's April 2001 Monthly Staff Report, seven OFVs were issued in Calendar Year 2000.

For the period July 1, 2000, to January 31, 2001, the Commission assessed \$81,500 in penalties and collected \$11,000 of this amount. Further, the Commission has an additional \$245,800 in penalties that it assessed against 21 operators since 1993, but these penalties are still pending collection.

All penalties are calculated using base amounts that range from \$250 to \$1,000, depending upon the violation. All penalties are subject to adjustment by the application of aggravating or mitigating factors, which are also established by rule. Once a penalty order has been approved, the Commission notifies the operator that a penalty has been assessed and payment is then due within 30 days. If payment is not received within this time frame, the Commission sends a second letter to the operator, requesting payment. After another 30 days have elapsed, all outstanding penalties are turned over to Central Collection Services at the Department of Personnel/General Support Services as required by Section 24-30-202.4, C.R.S.

During our audit we noted that the Commission needs to improve its methods for assessing and collecting penalties. Specifically, we found the following:

- **Penalty assessments do not always agree to the base fine amount set forth in Commission rules and regulations.** We reviewed 12 penalties that had been assessed from July 1, 2000, through January 31, 2001. We found that five of these penalties did not agree to the base fine amounts set forth in Commission rules and regulations, and the Commission did not document whether aggravating and/or mitigating factors were figured into their penalty calculation. Out of the three penalties that were assessed higher than the base amount, two were doubled from the base penalty amount (an increase of \$3,000) and one was increased by a factor of 2.5 times the base penalty amount (an increase of \$1,500). Out of the two penalties that were assessed lower than the base amount, one was decreased by half of the base penalty amount (a decrease of \$2,000) and the other was lowered by two-thirds (a decrease of \$4,000). Although rules allow the Commission to modify penalties in this manner, the Commission should document the aggravating and/or mitigating factors it uses to adjust base fine amounts. This will ensure that the Commission does not appear to be unfair or biased in its enforcement activities.
- **Penalty revenue may be overstated.** During the period July 1993 through January 2001, the Commission assessed nearly \$1.1 million in penalties. During this same time period, the Commission collected or waived about \$680,000, or approximately 65 percent of the total penalties assessed. The remaining \$378,000 is either pending collection or has been deemed

uncollectible. In Fiscal Year 2001 the Commission began to record outstanding penalties that had been turned over to Central Collections as accounts receivable. The recorded amount of the Commission's receivables affects the amount of revenue reported on the State's accounting system. If this amount is overstated, state revenue will be inaccurately increased for TABOR purposes. Since excess TABOR revenue is required to be refunded to taxpayers, the accuracy of the revenue recorded on the State's accounting system is critical. Using the Commission's historical penalty collection rate of 65 percent, we estimated that the penalty receivable, and thus revenue recorded, may be overstated by about \$86,000. To ensure the revenue is accurately recorded, the Commission should develop procedures to routinely analyze historical collection rates. This analysis would allow the Commission to estimate the amount of uncollectible penalties, which, in turn, will help it establish an allowance for doubtful accounts. This allowance will improve the accuracy of revenue reported on the State's accounting system.

Recommendation No. 8:

The Oil and Gas Conservation Commission should document the aggravating and/or mitigating factors that are used to determine individual penalty assessments.

Oil and Gas Conservation Commission Response:

Agree. Administrative Orders by Consent and Orders Finding Violation will immediately begin to consistently describe which mitigating or aggravating factors were considered when computing a fine amount.

Recommendation No. 9:

The Oil and Gas Conservation Commission should analyze historical collection rates in order to establish procedures to determine an allowance for doubtful accounts.

Oil and Gas Conservation Commission Response:

Agree. An allowance for doubtful accounts has been determined and entered into COFRS for Fiscal Year 2001 receivables for penalties. Completed July 26, 2001.

Accounting and Information System Issues

Chapter 2

Overview

As part of our audit we reviewed the Oil and Gas Conservation Commission's accounting and information systems. We identified five areas that need improvement. Specifically, we found that the Commission is not maintaining adequate supporting documentation for travel card expenditures, following procedures for the payment of travel card expenditures, or following procedures to ensure that invoice approval is documented and payment vouchers are approved by the appropriate person. We also noted that the Commission needs to continue its transition to an automated information system and make improvements in its record keeping. The following narrative provides further detail on each of these issues.

Travel Practices Need to Comply With State Policies

The State's Travel Management Policy authorizes travel cards to be issued to state employees for official government travel expenses. The Commission has been authorized the use of 11 travel cards. Cards can be used for airfare, hotel accommodations, rental cars, cash advances, and miscellaneous expenses. The total amount of Commission expenditures for credit card purchases was approximately \$16,000 from the period of July 1, 2000, through February 28, 2001. The amount of credit card expenditures for travel in Fiscal Years 1999 and 2000 was about \$25,000 and \$27,000, respectively.

We noted two problems with Commission practices regarding travel cards. First, State Fiscal Rules require employees to submit receipts to support their travel-related business expenses. The documentation should clearly show the business purpose of the travel, the date travel occurred, and the location and amount of the transaction. Currently the Commission does not maintain all required documentation. Commission staff stated that employees are required to present receipts supporting all travel card transactions. According to staff, these receipts are compared with travel card statements and known

employee travel dates prior to authorizing payment. After the payment is made to the credit card company, however, Commission staff discard all receipts.

As part of our audit we reviewed all of the travel card payments made during the above-mentioned period (35 transactions). We found that 25 payments, or 71 percent, had little or no supporting documentation. The remaining ten payments had supporting documentation attached; however, most of the receipts did not have the business purpose of the travel clearly documented. Since the Commission does not maintain supporting documentation, we asked staff to provide us with a log of all employee travel incurred for the period of July 1, 2000, through February 28, 2001. The Commission provided us with information regarding dates traveled, travel itineraries, the name of the employee who traveled, and the business purpose of the travel. We were able to agree the log to travel card transactions incurred, and nothing came to our attention that would indicate unusual items or discrepancies. However, because of the condition of the documentation, we could not determine whether all travel card transactions were appropriate.

Second, according to the Statewide Travel Management Policy, employees are solely liable for the expenditures charged on travel cards. This policy protects the State from financial liability for travel card purchases. Because of this statewide policy, the Department of Natural Resources developed written procedures requiring employees to pay the credit card company for travel expenses and request reimbursement from the divisions for these expenses. We contacted four other departments and found that they paid travel card transactions in this same manner. The Commission is not adhering to this policy. Instead, the Commission is remitting payment directly to the credit card company. The Commission should adhere to the Department's policy to ensure that the State is not unnecessarily exposed to a financial liability situation.

Recommendation No. 10:

The Oil and Gas Conservation Commission should maintain adequate supporting documentation for all travel card transactions. The supporting documentation should include all receipts of transactions incurred and the business purpose of the expenditures.

Oil and Gas Conservation Commission Response:

Agree. State Fiscal Rules relating to required supporting documentation for travel-related business expenses have been reviewed and are being followed by accounts payable staff. This recommendation has been implemented with the concurrence of the Department's Accounting Office.

Recommendation No. 11:

The Oil and Gas Conservation Commission should follow written policies established by the Department of Natural Resources regarding the payment of travel card expenses.

Oil and Gas Conservation Commission Response:

Agree. Accounts payable staff are now following the Department's Accounting Office procedures requiring employees to pay the credit card company for travel expenses and request reimbursement from the Division. This recommendation has been implemented.

Follow Written Procedures for Approval of Invoices and Payment Vouchers

The Commission has written policies and procedures for approving both invoices and payment vouchers. According to these policies, invoice approval should be clearly documented with a signature by the appropriate staff person. In addition, policies require that payment vouchers for amounts over \$1,000, with certain exceptions, are approved by Department accounting staff. Amounts below \$1,000 can be approved by certain Commission staff.

We found that the Commission is not always following these written procedures. We reviewed a sample of 60 payment vouchers to evaluate the Commission's basic controls over expenditures and found that Commission staff did not indicate proper invoice approval in 14 instances (approximately 23 percent). We also found that eight payment vouchers in excess of \$1,000 (approximately 13 percent) had been inappropriately approved by Commission staff, rather than by Department accounting staff. Although these expenditures appeared to be proper, the Commission should ensure written policies

and procedures relating to the payment of expenditures are being followed. This will decrease the risk that payments are made for unauthorized transactions.

Recommendation No. 12:

The Oil and Gas Conservation Commission should follow written policies and procedures to ensure that invoice approval is documented and payment vouchers are approved by the appropriate person, given established guidelines.

Oil and Gas Conservation Commission Response:

Agree. Commission staff responsible for processing and approving invoices and payment vouchers have reviewed and are following Commission procedures. This recommendation has been implemented with the concurrence of the Department's Accounting Office.

Expand Oil and Gas Information System Capabilities

Over the last several years, the Commission has revamped its computer system, the Colorado Oil and Gas Information System (COGIS), to provide a more reliable and efficient means of disseminating information to interested parties. We commend the Commission for its efforts; however, we found areas relating to the information system that could be improved, as follows:

- **Increase the number of electronic filings.** The Commission has enabled operators to report oil and gas production and Conservation Levy data electronically. Currently about 81 percent of all oil and gas production reports and 15 percent of the Conservation Levy reports are submitted electronically. Although these percentages indicate a high number of production electronic filers, the Commission should encourage all operators to submit information in an electronic format to reduce the need for manual data entry and, therefore, the potential for errors and misreporting of data. This will also enable the Commission to handle increased workloads in the future without additional resources.

- **Provide access to forms on the Web site.** The Commission uses written forms to facilitate various processes such as registration, permitting, and complaint filing. These forms cannot be accessed on the Commission's Web site and, therefore, cannot be submitted in an electronic format. Allowing electronic access to certain processes will establish a more efficient and timely means for operators to communicate with the Commission.
- **Reduce the paper filing system.** The Commission has undertaken a project to scan all of its historical files into an electronic format for posting on its Web site. In addition, the Commission is scanning new documents as they are submitted. Because of its transition to an electronic filing system, the Commission sometimes maintains information in three different forms. For example, we noted that when a complaint is received, a form is completed and maintained by Commission staff. The information is then entered into the Commission's database and the completed form is scanned. Both the entered information and the document image are made available on the Commission's Web site. Since the scanned information is also available to staff through the Internet, the Commission should consider eliminating the paper filing system.

During our audit we did not identify, and the Commission did not provide, any cost benefit data relating to the above areas for improvement. However, elimination of duplicative and/or paper-based processes should result in long-term savings to the Commission.

Recommendation No. 13:

The Oil and Gas Conservation Commission should expand its Colorado Oil and Gas Information System capabilities by:

- a. Increasing the number of electronic filings for oil and gas production and Conservation Levy reports.
- b. Providing access to all forms on the Commission's Web site.
- c. Eliminating the paper files that it maintains.

Oil and Gas Conservation Commission Response:

Agree. The COGCC has been pursuing electronic reporting for a number of years. The following are processes being pursued in answer to this issue:

- 1) Electronic data transfers—This method is most beneficial to larger operators and the COGCC, as it requires the least data manipulation.
 - a) XML format using National Standards—The COGCC is active in organizations representing state and federal oil and gas agencies to create a standard transfer protocol.
 - b) ASCII flat files—This is a tried and true method that is used currently for the largest data sets that the COGCC currently receives. Other data sets will be formatted for transfer.
- 2) Internet forms:
 - a) Printable formatted forms—This is simply a copy of a form that can be printed and completed and mailed or faxed.
 - b) HTML-interactive forms—These forms are standard Internet pages that do not print consistently unless a report is attached to control the output.
 - c) Printable online-fillable forms—This is a formatted form that allows input and printing from the same form.
- 3) Paper forms converted to digital data without manual data entry—This can be achieved by using imaging technology to read the printed characters and convert them to digital characters.

The COGCC plans to have all of these different formats in place by June 30, 2003 for all 42 different forms. The COGCC goal is to no longer retain paper records by November 2004.

Information Management Needs Improvement

The Commission maintains a database containing information that is made available to the public either through the Commission's Web site or in a Monthly Staff Report. Throughout our audit we were provided with various reports generated from the database, including reports regarding financial assurance, permit applications, and complaints. Upon review of these reports, information published on the Web site, and Commission files, we noted

several instances of incorrect entries, duplicate listings, incorrect dates, and missing information. Specifically, we noted the following:

- **Financial assurance is overstated by approximately \$1.4 million.** The Commission provided us with a report detailing the amount of financial assurance it holds and showing that amount to be a total of approximately \$22.5 million. This report contained numerous errors, including duplicate entries, bonds listed as active, even though they have been released; bonds differing from actual amounts; and one bond that had been assigned two different numbers. These errors resulted in the overstatement mentioned previously. Although this overstatement does not affect the financial assurance amount recorded on the State's accounting system, the Commission maintains the information to ensure that operators have provided financial assurance as required by statute. In addition, financial assurance information is made available to the public on the Commission's Web site. These inaccuracies may impair reliance placed on the financial assurance information.
- **Information made available to the public is inaccurate.** During our audit we noted that penalty information provided in the Commission's Monthly Staff Reports is incorrect. For example, recent Monthly Staff Reports showed three penalties in the amount of \$88,000 as uncollectible, even though Central Collections considers these active accounts. In addition, information on the Commission's Web site detailing reclamation projects has not been updated since 1997. It is important for information provided by the Commission to be accurate and kept current to ensure its reliability and usefulness.
- **Staff are not utilizing the existing file checkout system.** During our review of well permit files, one file could not be located and four files required an extensive search before they were located. The Commission has a checkout system in place to ensure it can account for all files. However, during our audit we noted that a checkout card is not always completed by staff when a file is removed. Until the Commission completes its transition to an electronic filing system, it should enforce the use of the existing file checkout system to help ensure files do not become lost or misplaced.

The Commission should take actions to correct the deficiencies noted in its record keeping to ensure internal information—as well as information provided to the public—is accurate, reliable, and useful.

Recommendation No. 14:

The Oil and Gas Conservation Commission should make improvements in its record keeping by:

- Periodically reviewing all information available on the Commission's database to ensure its accuracy.
- Reviewing all internally generated reports and information made available through the Commission's Web site, and updating the information in a timely manner.
- Consistently enforcing the use of the existing file checkout system until the transition to an electronic filing system is complete.

Oil and Gas Conservation Commission Response:

Agree. Data quality is of the utmost concern to the COGCC. The COGCC requested and was appropriated the funding to implement a Fiscal Year 2002 and Fiscal Year 2003 project for a one-time review of the well files to correct the database records to match the paper records. However, it is not feasible to review all of the information in the database on a routine basis. Records are quality-controlled when the forms are submitted, and corrections are made to the data prior to approval in the automated form processor. Erroneous information will still get through the system when it is overlooked in the manual edit process. The COGCC continues to develop automated edit routines in the form processor and create reports that scan all data in an attempt to identify data that are grossly in error. Neither of these processes will ever be a 100 percent quality control solution. As the data are complex and highly variable, the only solution for some data errors continues to be manual identification. The creation of data edits and scanning reports is an ongoing process that cannot be predicted when, if ever, it will be completed because of the time-consuming and complex nature of this type of programming. Improvements are ongoing as staff and funding are available.

The COGCC is committed to maintaining its Web site and providing the most current information to its customers through its Web site. It is in the best interest of the COGCC to be very diligent in review and update of its Web pages to reduce customer inquiries and maintain customer satisfaction. The COGCC will create a task force to review options for creating an indexed catalog of its Web

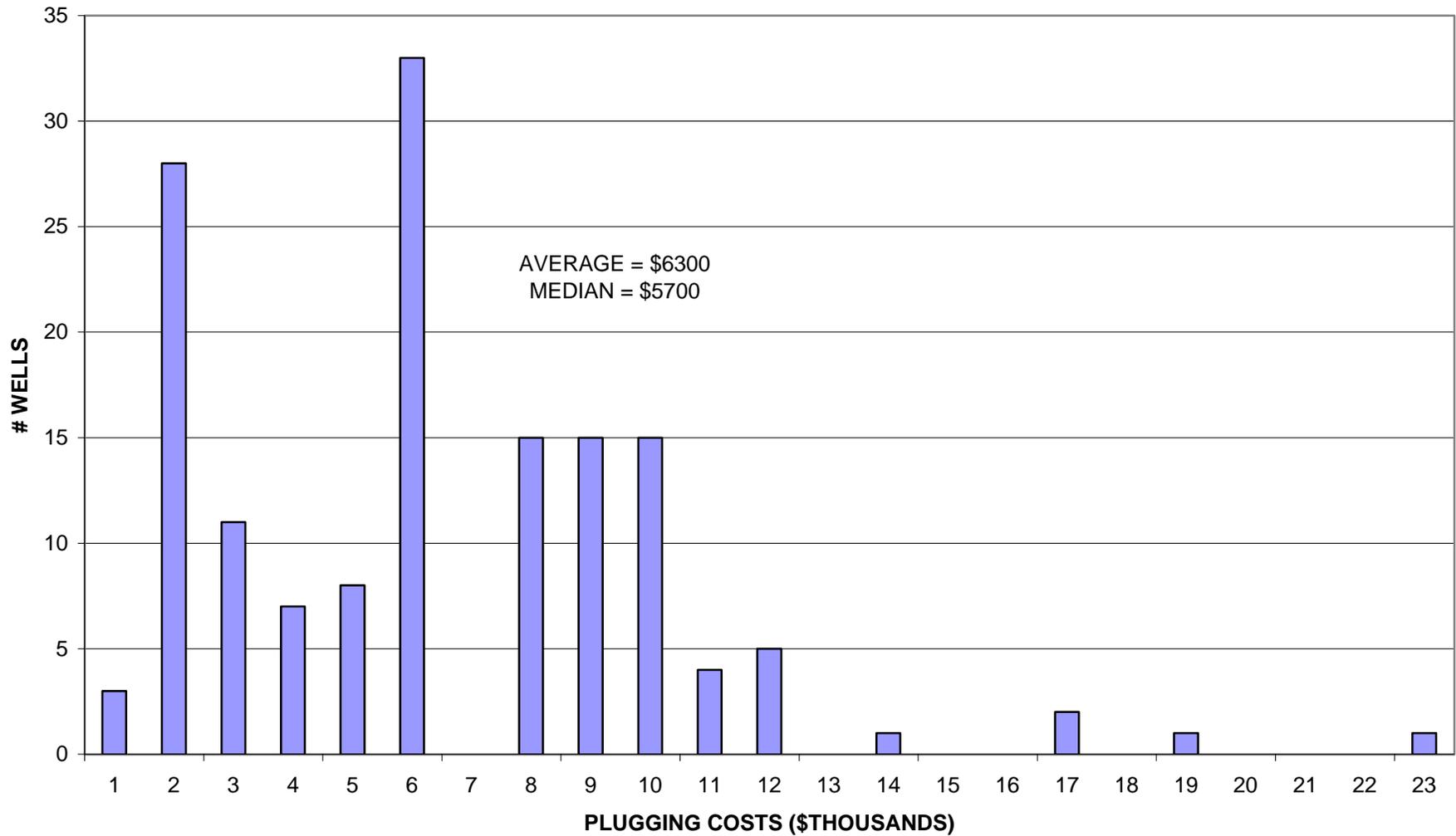
pages with information such as page dependencies, name, location, frequency of change, and data refresh methodology (static vs. dynamic). Once the task force has determined the necessary data to catalog, a staff member will be assigned to be responsible for cataloging and upkeep of the page. This will be an extensive project that is planned to be completed by December 2002.

The COGCC created a policy of using checkout cards when pulling data files. However, since the files are subsequently routed throughout the office once they are pulled, a correctly completed checkout card does not always ensure success in finding a specific file. This workflow process causes the checkout policy to be ineffective, even when 100 percent implemented. The COGCC is committed to optimizing its investment in document imaging technology, and has recently converted an FTE to a document image administrator. The backlog of documents to be scanned is large but is beginning to decrease steadily. The COGCC believes that the imaging system will be free of backlog by August 2002, and that the document images and the database will be the best sources of information for staff and COGCC customers.

Appendices

Appendix A

Supplemental Information Provided by the Oil and Gas Conservation Commission PLUGGING AND RECLAMATION COSTS FOR COGCC FINANCIAL ASSURANCE FOR 149 WELLS



Appendix B

Supplemental Information Provided by the Oil and Gas Conservation Commission

COGCC PLUGGING, ABANDONMENT, AND RECLAMATION COST ESTIMATE LIST

8/1/200

COUNTY	PROJECT	TOTAL		COST	DESCRIPTION
		COST ESTIMATE	# OF WELLS PER WELLSITE		
ROUTT	TOW CREEK P&A	\$50,000	6	\$8,333	PA AND RECLAIM SIX (6) WELLS
ROUTT	TOW CREEK RECLAMATION	\$10,000	7	\$1,428	RECLAIM 6 WELLSITES & PITS AND 1 BATTERY SITE
MOFFAT	BUCK PEAK P&A	\$40,000	5	\$8,000	PA AND RECLAIM FIVE (5) WELLS
MOFFAT	BUCK PEAK RECLAMATION	\$5,000	1	\$5,000	RECLAIM ROAD, BATTERY SITE AND SALT KILL AREA
WELD	KEOTA RECLAMATION AREA 1	\$5,000	1	\$5,000	SALT KILL SITE
WELD	KEOTA RECLAMATION AREA 2	\$5,000	1	\$5,000	SALT KILL SITE
WELD	KEOTA RECLAMATION AREA 3	\$2,000	1	\$5,000	SALT KILL SITE
WELD	KEOTA RECLAMATION AREA 4	\$3,000	1	\$5,000	SALT KILL SITE
DENVER	DERBY DOME 2 WELLS	\$16,000	2	\$8,000	PA AND RECLAIM TWO (2) WELLS
DENVER	DERBY DOME FACILITY & PIT RECLAMATION	\$6,000	1	\$6,000	RECLAIM HISTORIC STEAM GENERATION FACILITY & PIT
RIO GRANDE	JYNNIFER 1-9	\$6,000	1	\$6,000	PA WELL AND RECLAIM
CHEYENNE	HOFFMAN 6-2	\$6,000	1	\$6,000	PA WELL AND RECLAIM
RIO BLANCO	RANGELY MANCOS (39 WELLS)	\$78,000	39	\$2,000	PA 39 WELLS AND RECLAIM
LA PLATA	(JAY MAGNESS BD CLM) POWELL 1-6	\$10,000	1	\$10,000	PA & RECLAIM 3 WELLS
ARCHULETA	SULLENBERGER 1	\$12,000	1	\$12,000	PA WELL AND RECLAIM
LA PLATA	CARSON 1	\$10,000	1	\$10,000	PA WELL AND RECLAIM
LAPLATA	TAYLOR 2	\$11,000	1	\$11,000	PA WELL AND RECLAIM
MORGAN	MCCOURT 1	\$5,000	1	\$5,000	PA WELL AND RECLAIM
WASHINGTON	MARWITZ 1	\$10,000	1	\$10,000	PA WELL AND RECLAIM
BOULDER	BOULDER FIELD (8 WELLS)	\$30,000	8	\$3,750	PA 8 WELLS AND RECLAIM
EL PASO	IRONHORSE STATE 1	\$1,500	1	\$1,500	CLEAN UP LOCATION AND RECLAIM
EL PASO	MARTIN 1	\$1,000	1	\$1,000	NO PAPERWORK, RECLAMATION
ELBERT	J EDWARD CLARK 1	\$1,500	1	\$1,500	CLEAN UP LOCATION AND RECLAIM
LA PLATA	VIRBETH LAND CO 1	\$1,500	1	\$1,500	CLEAN UP LOCATION AND RECLAIM
LAPLATA	K-F 1	\$1,500	1	\$1,500	CLEAN UP LOCATION AND RECLAIM

Appendix B

Supplemental Information Provided by the Oil and Gas Conservation Commission

COGCC PLUGGING, ABANDONMENT, AND RECLAMATION COST ESTIMATE LIST

8/1/2001

COUNTY	PROJECT	TOTAL COST		COST PER WELLSITE	DESCRIPTION
		ESTIMATE	# OF WELLS		
WASHINGTON	SMITH 1	\$4,000	1	\$4,000	FINISH PA
WELD	FRANKS 1-4	\$1,500	1	\$1,500	CLEAN UP LOCATION AND RECLAIM
WELD	CEI-LRB 1	\$4,000	1	\$4,000	FINISH PA AND RECLAIM
FREMONT	FLORENCE WELLS (6)	\$27,000	6	\$4,500	PA AND RECLAIM 21 WELLS
MORGAN	LEONA BUTTERS 1	\$11,000	1	\$11,000	PA WELL AND RECLAIM
BOULDER	MAXWELL 5	\$10,000	1	\$10,000	PA WELL AND RECLAIM
LA PLATA	WHEELER 2	\$10,000	1	\$10,000	PA WELL AND RECLAIM
MORGAN	REINHOLDT SCHMIDT 1	\$5,000	1	\$5,000	PA WELL AND RECLAIM
ARAPAHOE	SPICKERD B-1	\$10,000	1	\$10,000	PA WELL AND RECLAIM
BACA	DEEDS 1	\$10,000	1	\$10,000	PA WELL AND RECLAIM
WASHINGTON	JOLLY 1	\$10,000	1	\$10,000	PA WELL AND RECLAIM
WASHINGTON	JOLLY C-1	\$10,000	1	\$10,000	PA WELL AND RECLAIM
TOTALS/AVERAGE		\$439,500	103	\$4,267	

Average estimated cost of the 103 outstanding plugging, abandonment, and reclamation projects currently identified in Colorado as of 8/01/2001 is

\$4,267 per wellsite.

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