

Attachment E.

Oil and Gas from the Outer Continental Shelf:
Analysis of the "Energy Supply Act"
and Summary of the Senate Debate on S. 3221



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OIL AND GAS FROM THE OUTER CONTINENTAL SHELF:
ANALYSIS OF THE "ENERGY SUPPLY ACT"

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OIL AND GAS FROM THE OUTER CONTINENTAL SHELF:
ANALYSIS OF THE "ENERGY SUPPLY ACT"
AND SUMMARY OF THE SENATE DEBATE ON S. 3221

The 93d Congress was and the 94th Congress will be concerned with: the demand for offshore oil and gas; the leasing policies regulating development of the Outer Continental Shelf (OCS); the need to avoid polluting the sea; and the desire to preserve the environmental integrity of the coastal zones. Major questions concerning development of the OCS which were not answered by the 93d Congress, but which will confront the 94th Congress include:

1. What national policies for development and exploitation of the OCS are needed?
2. What terms and conditions should govern the leasing of the OCS?
3. Should the Federal Government involve itself in a vigorous OCS oil and gas exploration program?
4. Who should be liable for oil spills resulting from exploitation of the OCS?
5. What form of compensation should be given to coastal states impacted by OCS development?
6. What course of appeal has a *Governor* of a coastal state when aggrieved by proposed leasing action of the Secretary of the Interior?

This paper reviews the passage of S. 3221 by the Senate, a major action taken by the 93d Congress on the development of oil and gas from the OCS. A sectional analysis of S. 3221, the "Energy Supply Act of 1974" is presented. Selected reasons for and against S. 3221 which were brought out during Senate debate are summarized. Also, comments and questions useful for further considerations of the "Energy Supply Act" are detailed.

I. SECTIONAL ANALYSIS OF THE "ENERGY SUPPLY ACT OF 1974"
AS PASSED BY THE SENATE ON SEPTEMBER 18, 1974

Purpose of S. 3221

S. 3221 is a multi-purposed bili. Its major provisions se

1. To increase oil and natural gas production in the Outer Continental Shelf (OCS) in order to assure material prosperity and **national Security**, reduce dependence on unreliable foreign sources of *energy*, and assist in maintaining a favorable balance of payments.

2. To encourage development of new and improved technology for *energy* resource production that will increase human safety and eliminate or reduce risk of damage to the environment;

3. To provide States which are directly impacted by OCS development with comprehensive assistance in order to assure protection of the onshore social, economic, and environmental conditions of the coastal zone; and

4. To make oil and natural gas resources in the Outer Continental Shelf available as rapidly as possible consistent with the need for orderly resource development, and protection of the environment, in a manner consistent with the Mining and Mineral Policy Act of 1970 and designed to insure the public a fair market return on disposition of public resources.

National Policy for the Outer Continental Shelf

S. 3221 establishes a national policy to guide the development and exploitation of the OCS, which should be made available for orderly development, subject to environmental safeguards, consistent with and when necessary to meet national needs. S. 3221 recognizes that development of the OCS will have significant impact on the coastal zone areas of *certain* States, and that these States may require assistance in protecting their coastal zones, insofar as is possible from adverse effects of such impact.

Development of OCS Leasing Program

S. 3221 declares that certain OCS lands should be made available for leasing as soon as practicable. The Secretary of the Interior is directed to prepare and maintain a leasing program which shall indicate the size, timing, and location of leasing activity that will best meet national energy needs for a ten year period.

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Selected Features of the OCS Leasing Program Under S. 3221

1. Management of the OCS in a manner which considers all its resource values and the potential impact of oil and gas development on other resource values of the OCS and the marine environment;

2. Timing and location of leasing to distribute exploration, and development, and production of oil and gas among various areas of the OCS, considering:

- existing information concerning their geographical, geological, and ecological characteristics;
- their location with respect to, and relative needs of, regional energy markets;
- their location with respect to other uses of the sea and seabed including but not limited to fishing areas, access to ports by vessels, and existing or proposed sea lanes;
- interest by potential oil and gas producers in exploration and development as indicated by tract nominations and other representations;
- an equitable sharing of developmental benefits and environmental risks among various regions of the United States;
- timing and location of leasing so that to the maximum extent practicable areas with less environmental hazard are leased first; and
- receipt of fair market return for public resources.

3. The Secretary of the Interior shall establish procedures for receipt and consideration of nominations for areas to be offered for lease, and

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shall, within two years submit a proposed leasing program, which shall include the reservation of an appropriate area as a National Strategic Energy Reserve, to the *Congress*. "

Establishment of Federal OCS Oil and Gas Survey Program

S. 3221 directs the Secretary of the Interior to conduct a survey program on oil and gas resources of the **OCS, and to obtain information about the** probable location, extent, and characteristics of such resources. This information is to provide a basis on which to develop a leasing program, and to promote more informed decisions regarding the value of public resources to be leased.

Safety Regulations for Oil and Gas Operations

S. 3221 seeks to insure that through improved techniques, maximum precautions, and maximum use of the best available technology by well-trained personnel, the safest possible operations in the OCS will occur. The Secretary of the Interior, with the concurrence and advice of *others* is directed to develop, revise, and promulgate safety regulations for operations in the OCS. S. 3221 contains a provision which states that the National Academy of Engineering shall conduct a study of the adequacy of existing safety regulations and technology, equipment, and techniques for operations in the OCS, and to make recommendations for improved safety regulations.

Research and Development to Improve Technology for OCS Development

The Secretary of the Interior is, under S. 3221, directed to carry out a research and development program designed to improve technology related to development of oil and gas resources of the OCS. Areas of

investigations shall include: downhole safety devices, methods for re-establishing control of blowing out or burning wells, methods for containing and cleaning up oil spills. " new or improved methods of development in water depths over 600 meters, and subsea production systems .

Enforcement of Safety Regulations

The Secretary of the Interior and the Secretary of the department in which the Coast Guard is operating shall jointly enforce the safety and environmental protection regulations promulgated under the Act. These regulations shall provide for:

1. physical observation at least once each year of the installation or testing of all safety equipment designed to prevent or ameliorate blowouts, fires, spillages, or other major accidents; and
2. periodic onsite inspection without advance notice to the lessee to assure compliance with public health, safety, or environmental protection regulations.

S. 3221 directs the Secretary of the department in which the Coast Guard is operating to make an investigation and public report on all major fires and major oil spillage occurring as a result of operations pursuant to this Act.

Liability for Oil Spills

S. 3221 establishes an Offshore Oil Pollution Settlements Fund as a nonprofit corporate entity which shall be administered by the holders of leases issued under regulations prescribed by the Secretary of the Interior. The holder of a lease or right-of-way issued or maintained under this Act and the Offshore Oil Pollution Settlements Fund shall be liable

without regard to fault and without regard to ownership of any adversely affected lands, structures, fish, wildlife, or biotic or natural resources relied upon by any damaged party for subsistence or economic purposes for all damages sustained by any person as a result of discharges of oil or gas from any operation **authorized under** this Act under certain conditions; The provision **places a limit** of \$100 million, for all claims arising out of any one incident. The holder shall be liable for the first \$7 million of such claims that are allowed. The fund which S. "3221 establishes is liable for the balance of the **claims that** are allowed up to \$100 million. **If the total claims allowed exceed \$100 million, they shall be reduced proportionately, and the unpaid portion may be asserted and adjudicated under applicable Federal or State law.**

A fee of 2 1/2 cents per barrel of oil, produced pursuant to any lease issued or maintained under this Act, is to be paid into the fund. costs of administration of the fund are paid from the fund. Subject to certain limitations, if the fund is unable to satisfy a valid claim, it may borrow the money needed from any commercial credit source at the lowest available rate of interest upon the approval of the Secretary of the Interior.

Coastal State Fund

S. 3221 establishes the Coastal State Fund to assist coastal States impacted by anticipated or actual oil and gas production related to the OCS. Monies from the Fund are to ameliorate adverse environmental effects and control secondary social and economic impacts from development of certain Federal energy resources in or on the OCS adjacent to the submerged lands of such states. The grants may be used for planning, construction of public facilities and provision of public services, and

such other activities as may be prescribed by regulations promulgated by the Secretary of Commerce. Under S. 3221 the Secretary of Commerce shall establish requirements for grant eligibility and shall coordinate all grants with management programs established pursuant to the Coastal Zone Management Act of 1972. Initially, \$100, 000,000 are to be authorized to be appropriated for the fund. Subsequently, 10 per centum of the Federal revenues from the Outer Continental Shelf Lands Acts, as amended by this Act, or the equivalent of forty cents per barrel from Federal revenues from the OCS Act, whichever is greater, shall be paid into the fund. Grants shall be made to impacted coastal States in proportion to the effects and impacts of offshore oil and gas exploration, development and production on such States.

Citizen Suits

S. 3221 contains a provision to allow for citizen suits under certain circumstances by any person having an interest which is or may be adversely affected by the Act.

Promotion of Competition

The Secretary of the Interior is directed to publish a report with recommendations for promoting competition and maximizing production and revenues from the leasing of OCS lands. Such report shall include considerations of bidding systems, measures to ease entry of new competitors; and measures to increase energy supply to independent refiners and distributors.

Environmental Baseline and Monitoring Studies

Prior to permitting oil and gas drilling on any area of the Outer Con-

tinental Shelf not previously leased under this Act, the Secretary of the Interior, in consultation with the Administrator of the National Oceanic and Atmospheric Administration, shall make a study of the area involved to establish a baseline of those critical parameters of the OCS environment which may be affected by oil and gas development. The study shall include background levels of trace metals and hydrocarbons in water, sediments, and organisms; characterization of benthic and planktonic communities; description of sediments and relationships between organisms and abiotic parameters; and standard oceanographic measurements such as salinity, temperature, micronutrients, and dissolved oxygen.

Revision of Lease Terms

Under existing law the Secretary of the Interior is authorized to offer (OCS) oil and gas leases on the basis of either (1) a cash bonus bid with a royalty fixed at no less than $12 \frac{1}{270}$ of the gross revenue from the lease, or (2) on the basis of a royalty rate bid with a fixed cash bonus. Almost all OCS leases have been offered for cash bonus bids with a royalty rate fixed at $16 \frac{2}{3}\%$ of the gross value of production, since the OCS Lands Act was approved in 1953. Under the "Energy Supply Act of 1974" the bidding **shall be: (1) on the basis of cash bonus bid with** a royalty fixed by the Secretary at ~~not~~ less than $12 \frac{1}{2}$ per centum in amount or value of the production saved, removed, or sold, (2) on the basis of a cash bonus bid with a fixed share of the net profits derived from operation of the tract of no less than 30 per centum reserved to the United States, or (3) on the basis of a fixed cash bonus with the net profit share reserved to the United States as the bid varies.

A rationale for this proposal was elucidated in the Report on S. 3221

by the Senate Committee on Interior and Insular Affairs:

The Committee's decision to eliminate the royalty bidding alternative is based on the widespread agreement of most economists and oil industry representatives concerning the undesirable effects of royalty bidding. Specifically, the Committee believes that royalty bidding would encourage speculation, increase the likelihood of premature shutdown of production under conditions of high royalty rates, and result in reduction in petroleum output and lease revenues.

However, the Committee wants to provide a lease allocation system that would encourage the widest possible participation in competitive lease sales consistent with receipt by the public of fair market value for its resources. Testimony before this Committee and elsewhere has revealed general acceptance of the proposition that high bonus bids have created a barrier to the entry of small and medium size oil firms to the OCS arena. The Committee believes that net profits share arrangements can be effective in shifting government revenue away from initial bonuses and into deferred payments made out of a leaseholders profits. 1 /

Other, changes in the leasing and exploration aspects of the OCS program proposed in S. 3221 were summarized in the Report of S. 3221 of the Senate Interior and Insular Affairs Committee:

Under existing law, all OCS oil and gas leases are for a primary term of five years. As amended by section 203, Subsection 8(b) of the OCS Lands Act would permit the Secretary to issue leases with a primary term of up to ten years.

The purpose of the increase in permissible maximum primary lease term is to encourage exploration and development in areas of unusually deep water or adverse weather conditions, where the five year period may be insufficient for both exploration and the mobilization of new technology called for in the event of a discovery.

Section 204 further amends Section 8 of the OCS Lands Act by requiring that royalty and net profits share oil produced from all leases granted after the effective date of the amendment be offered by the Government at a competitive auction. . . 2 /

According to the Committee Report:

The purpose of the amendment is to create a free market in crude petroleum. However, the Committee was anxious to insure, that independent refiners not be denied access to OCS crude. To this end, Section 203 directs the Secretary to limit participation in sales where

1/ U. S. Congress. Senate. Committee on Interior and Insular Affairs. Report No. 93-1140. Energy Supply Act of 1974. September 9, 1974. p. 21.

2/ Ibid., p. 21-22.

such limitation is necessary to assure adequate supplies of oil at equitable prices to independent refiners. The Secretary can define the term "independent refiner" by regulation. The Committee intends that the term apply only to those refiners not part of an organization which produces crude petroleum. The Secretary could impose a size limitation in terms of refining capacity if he deemed that desirable. 3/

S. 3221 contains other revisions of OCS leasing terms, which are designed to insure maximum production from outstanding leases. It provides that all leases issued after S. 3221 is enacted must require that development be carried out in accordance with a development "plan which has been approved by the Secretary. Failure to comply with the development plan will terminate the lease.

The development plan will set forth, in the degree of detail established in regulations issued by the Secretary, specific work to be performed, environmental protection and health and safety standards to be met, and a time schedule for performance. The development plan may apply to all leases included within a production unit.

A proposed development plan must be submitted to the Secretary within six months after the date of enactment of S. 3221 for all outstanding permits and leases. Failure to submit a development plan or to comply with an approved development plan shall terminate the lease.

According to the Senate Report on S. 3221 the Senate Interior Committee recognized that:

.... there must be some flexibility in the degree of detail required in development plans. It expects that the Secretary will require exploration activity to start within a specified time. If production is established the development plan would need to be revised. This subsection authorizes revisions of development plans if the Secretary determines that revision will lead to greater recovery of the oil and gas, improve the efficiency of the recovery operation, or is the only

3/ Ibid. , p. 22.

means available to avoid substantial economic hardship on the lessee or permittee. 4/

Holder of oil and gas leases issued **pursuant to this Act shall not be** permitted to flare natural gas from any well **after the date of enactment of S. 3221**, unless the Secretary finds that there is no practicable way to obtain productioner to conduct testing or workover operations without flaring. The Senate Interior and Insular Affairs Committee maintained **that unnecessary** waste of this valuable natural resource must not be permitted.

S. 3221 amends Section 11 of the OCS Lands Act which authorizes the Secretary to permit geological and geophysical exploration in the Outer Continental Shelf. It would require that all permits for such explorations contain terms and conditions designed to (1) prevent interference with actual operations under any OCS lease, (2) prevent or minimize environmental damage, and (3) would required the permittee to furnish the Secretary with copies of all data (including geological, geophysical, and geochemical data, well logs, and drill core analyses) obtained during such exploration. The Secretary must maintain the confidentiality of all data so obtained until after the areas involved have been leased or until such time as he determines that making the data available to the public would not damage the competitive position of the permittee, whichever comes later.

Postponement of Lease Sales

S. 3221 provides that prior to the sale of each (OCS) lease the Governor of the adjacent States may request the Secretary to postpone such sale for

~/ Ibid., p. 23.

a period not to exceed three years following the date proposed in such notice if he determines that the sale will result in adverse environmental or economic impact or other damage to the State or residents thereof. Once, presented with such a request for postponement the Secretary is given three options:

1. grant the request for postponement;
2. allow for a shorter postponement than requested provided that such time is adequate for study and provision to ameliorate adverse economic or environmental effects, and for controlling secondary social or economic impact associated with development of Federal **(OCS) energy resources; or**
3. deny the request for postponement.

National Coastal Resources Appeals Board

S. 3221 creates within the Executive Office of the President the National Coastal Resources Appeals Board which shall hear appeals from the Governor of a State aggrieved by the action of the Secretary on requests for postponement of OCS lease sales. The Board can overrule the action of the Secretary if it finds that the State is not adequately protected from adverse environmental and economic impacts and other specified damages or if the request for postponement by the Governor is consistent with the national policy expressed in S. 3221.

Miscellaneous Provisions

Miscellaneous provisions of S. 3221 include:

1. A report on the adequacy of existing transport facilities and regulations to facilitate distribution of oil and gas resources of the Outer Continental Shelf;
2. A report listing all shut-in oil and gas wells and wells flaring

natural gas on leases covered by the OCS Lands Act;

3. A study on methods and procedures to implement a uniform law providing liability for damage from oil spills from OCS **operations**, tankers, deepwater ports, and other **sources**; **and**

4. A study to determine the feasibility of establishing **fuel stamp** program to utilize coupons to assist those on low and **fixed** incomes in **purchasing home heating fuels in the winter months**. .