United States Department of the Interior

BUREAU OF OCEAN ENERGY MANAGEMENT
WASHINGTON, DC 20240-0001

OCT 19 2011

Michael A. Livermore
Executive Director
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New York University School of Law
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Dear Mr. Livermore:

Thank you for your letter dated April 25, 2011, to Secretary Ken Salazar petitioning the Department of the Interior to revise its current Outer Continental Shelf Oil and Gas Leasing Program for 2007–2012 or initiate rulemaking to replace the current program with one that incorporates option value analysis. You also request that the Secretary take into account option value analysis in all future leasing decisions and leasing programs, particularly, the one planned for 2012–2017. As the Director of the Bureau of Ocean Energy Management (BOEM), I have been asked to respond on the Secretary's behalf.

For the reasons stated below, the Department will not revise its current 5-year leasing program or amend its regulations to replace the current 5-year leasing program, which expires June 30, 2012.

BOEM is studying option value and how this type of analysis might be considered in the upcoming 5-year program analysis and in future lease sale timing decisions. Any such incorporation would depend on its consistency with the governing laws. BOEM will not make any significant revisions to its current 5-year leasing program because that program is ending soon, and because program resources are focused on designing the next 5-year leasing program. BOEM did propose a relatively large increase in the minimum asking price for leases to be offered for sale in the remainder of the current 5-year program. BOEM will not entertain repeal of its current 5-year leasing program through regulations because the regulatory process is not the proper legal vehicle for modifying the existing leasing program.

Be advised that Section 18 of the Outer Continental Shelf Lands Act (OCSLA) provides that BOEM may consider many different factors in making program and leasing decisions; 43 U.S.C. § 1344. The U.S. Court of Appeals for the District of Columbia discussed this in great detail in the case *Natural Resources Defense Council, Inc. v. Hodel,* 865 F.2d 288, 292 (D.C. Cir. 1988). In that opinion, the court stated that Section 18 of OCSLA, "requires the Secretary to prepare, maintain, and periodically revise a leasing program consisting of a schedule of proposed lease sales." *Id.* The court stated that "the Secretary is to indicate 'as precisely as possible, the size, timing and location of leasing activity." *Id.* Moreover, the court summarized the four guiding principles for the leasing program in section 18(a) as follows:

(1) Impact on other resources and on "economic, social, and environmental values" must be considered.

(2) "Timing and location of exploration, development, and production of oil and gas among the oil- and gas-bearing physiographic regions" of the OCS shall be based on eight factors:

(A) "existing information concerning the geographical, geological, and ecological characteristics of such regions";

(B) "an equitable sharing of developmental benefits and environmental risks among the various regions";

(C) "the location of such regions" with respect to energy markets;

(D) "the location of such regions" with respect to other uses of the sea;

(E) the interest of producers in development;

(F) such laws and policies of affected states as the governors of those states specifically identify as relevant;

(G) "the relative environmental sensitivity and marine productivity" of different areas; and

(H) "relevant environmental and predictive information for different areas" of the OCS.

(3) Timing and location of leasing shall obtain, "to the maximum extent practicable . . . a proper balance" between the risk of environmental damage and the potential for oil and gas discovery.

(4) Leasing "shall be conducted to assure receipt of fair market value for the lands leased." *Id.*

As noted in the court's opinion, OCSLA requires that the lease sale timing involve consideration of a lengthy list of factors, including the agency's knowledge of the geographical, geological, and ecological characteristics, the location of energy markets, other uses of the sea, the interests of producers, the interests of affected states, the agency's ability to distribute development among geographical units in an equitable manner, the relative environmental sensitivity of the regions. Moreover, OCSLA contains the requirement that the 5-year leasing program balance environmental risks against the likelihood of oil and gas discovery. The opinion does not state or imply that lease sale timing should be based solely on maximizing the government's economic return.

Although the Act does mandate the receipt of fair market value, obtaining fair market value does not require that the government withhold lands from sale in order to take advantage of future increases in the potential value of the lands. Indeed, the Act states that expedited development is a specific factor to be balanced in planning lease sales. As the court noted, the "purposes of OCSLA include the 'expedited exploration and development of the Outer Continental Shelf in order to achieve national economic and energy policy goals, assure national security, reduce dependence on foreign sources, and maintain a favorable balance of payments in world trade." *Id.* at 291.

The agency's goal is to balance the need for expedited development against the potential environmental consequences of such development, not to balance expedited development against the potential for increasing future revenues by deferring development. Given these statutorily defined objectives, BOEM generally does not attempt to manage leasing based on its own perception of market conditions.

Following the OCSLA mandate for expeditious and orderly development of resources, BOEM gives the lease operator a 5 to10 year lease term (depending on water depth) in which to conduct exploration and development activities. Operators purchase tracts if they conclude that the tracts are valuable or will become valuable during the lease term. In this way, the operator is able to make timing decisions, within the lease term, for exploration and development. To allow the operator to make evaluations on the value of leases, there is a great benefit in scheduling of lease sales far in advance.

Early notice of sales gives lease operators adequate time to contract service companies, acquire seismic data, and secure drilling rigs. By establishing a schedule for potential lease sales, BOEM seeks to avoid interruptions in operations, which can lead to job losses and declines in domestic energy production. With the long lead-time required for operations and leasing program development, decisions need to be made in advance, rather than being based on oil prices that fluctuate daily.

Thank you again for the option value report. We will continue to review the report and study option value concepts to see if it is possible to incorporate them in one form or another in the next 5-year program, in the design of future lease sales, or in the decision on whether or not to lease specific tracts. For the reasons discussed above, we will not revise the current 5-year program or initiate rulemaking to replace the current program with one that incorporates the option value concepts you outline. Nor are we prepared at this time to use these concepts in the lease sales remaining under the current program.

Finally, your petition for rulemaking does not comply with the requirements of 43 C.F.R. § 14.2 in that it did not include either the identification of a current regulation that you seek to have repealed, nor the text of a proposed rule or amendment. The 5-year leasing program itself is not a rule promulgated under the Administrative Procedure Act, but a plan prepared under the procedures set forth in section 18 of OCSLA. 43 U.S.C. § 1337. Please note further that a significant revision to a 5-year program would require compliance with the same procedures under OCSLA as required to adopt the program in the first instance, which would require more time than remains before the current program expires on June 30, 2012.

Sincerely,

Tommy P. Beaudreau
Director