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D.C. CIRCUIT COURT REJECTS CHALLENGE TO OFFSHORE LEASING PROGRAM BUT LEAVES DOOR OPEN FOR MAJOR REFORM

Ruling could pave the way for natural resource valuation changes

In a lawsuit challenging the Bureau of Ocean Energy Management's (BOEM's) 2012-2017 leasing plan for the Gulf of Mexico and the Alaskan coast, the Center for Sustainable Economy (CSE) argued that incomplete and flawed economic analysis leads the government to sell resource leases too quickly and too cheaply, potentially costing the American public billions of dollars and leading to high-risk drilling. Today, the U.S. Court of Appeals for the D.C. Circuit ruled against CSE. However, part of the ruling could lead to major changes in how the government values the natural resources it leases.

"While we're very disappointed with the ruling, there is a silver lining," said CSE president John Talberth. "The ruling charted a path forward for our economic claims. The court also rightly found that CSE had associational standing to challenge these practices."

Michael Livermore, associate professor at the University of Virginia School of Law and a senior advisor for the Institute for Policy Integrity at New York University School of Law, argued this case in the D.C. Circuit on behalf of CSE. Livermore argued that government agencies engaged in leasing decisions should account for option value—a concept widely used in financial markets that analyzes the value of delaying irreversible decisions until more information is available. The value associated with the option to delay can be large, especially when there is significant uncertainty about price, extraction costs, and/or the environmental and social costs imposed by drilling. Option value is widely recognized in both economic theory and the practices of industry actors. Applied properly, an option value analysis would guide leasing away from areas with the greatest uncertainty, and help BOEM optimally time leases.

The court's decision, authored by Judge Pillard, acknowledges that there is "a tangible present economic benefit to delaying the decision to drill for fossil fuels to preserve the opportunity to see what new technologies develop and what new information comes to light."

The court found that BOEM's failure to quantify option value was reasonable at this time because the methodology is not yet "readily quantifiable." It stated: "Our holding is a narrow one…the agency is not permitted to substitute qualitative assessments for well-established quantitative methods whenever it deems such substitutions convenient." The court further noted: "Had the path been well worn, it might have been irrational for Interior not to follow it."

"The ruling strongly suggests that advancements in option value research could compel the government to alter its leasing practices and better quantify risks," said Livermore. "This change could pay enormous dividends to the American public."

The Institute for Policy Integrity is currently exploring new research on the quantification of option value, with the aim of improving natural resource valuation and leasing decisions at BOEM and other federal agencies.

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The Center for Sustainable Economy is a 25-year-old environmental economics think tank that works to speed the transition to a sustainable society.

The Institute for Policy Integrity at New York University School of Law is a non-partisan think tank dedicated to improving the quality of government decisionmaking through research and advocacy in economics, law, and regulatory policy.

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Environmental law experts including Michael Livermore, who argued the case, are available for interviews.