

## Report of the Committee on Development of Federal Lands

As we begin a new year and a new decade, the general tendency is to engage in retrospective reviews. Looking at 1989, the events affecting development of Federal Lands direct our thoughts into the future. A number of initiatives were begun in 1989 but few were completed. New appointments, including those of Secretary of Energy James Watkins and Secretary of the Interior Manuel Lujan, have introduced new players into the game. We can expect further changes in the rules of Federal Lands development in 1990 and beyond. Even as to those actions which may have appeared final actions of the Congress, the courts and the administrative agencies, we can expect continued evolution or a change of direction entirely.

### I. THE VALDEZ SPILL

Perhaps the event having the most impact on the development of federal lands was not staged in either the hallowed halls of Congress or the courthouse. On March 24, 1989, the Exxon oil tanker Valdez struck a shoal and leaked oil into Prince William Sound off the coast of Alaska. Since that date, the spill and its effects have remained constantly in the media. The Valdez incident has focused the interest of the nation and perhaps the world on oil spills, energy development and the environment. This interest has already had an effect on the development of federal lands and will undoubtedly continue to do so.

#### A. *Alaskan Natural Wildlife Refuge*

At the beginning of 1989, there was a general feeling that Congress would act on the proposed Alaskan Natural Wildlife Refuge (ANWR) energy development legislation. In fact hearings had been set for S.406 in March. Although there was an initial belief that the Administration would continue to pursue ANWR legislation, on May 2, Secretary Watkins advised a Congressional panel that the Administration recognized that ANWR could not move forward at this time but assured them that the Administration continued to support the orderly and prudent development of resources in ANWR.

#### B. *Strategic Petroleum Reserve*

The loss of the Valdez cargo and the interruption of deliveries of Alaskan supplies also led to a concern among some that the Strategic Petroleum Reserve should be increased to a billion barrels. To date, no action has been taken on this suggestion. There have also been suggestions for regional product reserves, partially in response to the heating oil demands of the winter of 1989-1990.

#### C. *Oil Spill Liability & Compensation*

The Senate passed S.686, a comprehensive bill on oil spill liability, compensation, cleanup and prevention on August 4, 1989, by the vote of 99 to 0.

Under this legislation the states are free to maintain their own oil spill clean up funds and enforce their own liability laws which exceed federal limits. On November 9, 1989, after a decade of insisting on a uniform federal statute which would preempt state laws, the House voted 375-5 to pass H.R. 2465, a comprehensive oil spill bill which would allow the states to enforce their own liability laws. These votes were a direct result of the Exxon Valdez spill. A conference will be held early in 1990 to hammer out the few remaining differences between the House and Senate versions and a bill is likely to be signed into law shortly thereafter.

#### *D. Oil Spill Drills*

The Minerals Management Service has increased the number of offshore oil spill drills by its inspectors. Various officials have called for new oil spill legislation or regulation at both the state and federal levels.

#### *E. Conclusion*

Perhaps the only thing that can be considered concluded about the Valdez accident is that it has had a profound and lasting effect on the development of energy resources from Federal Lands throughout the country. We can expect additional regulation of all oil handling operations, resulting in increased costs to the industry and the consumer. The new procedures and costs are likely to delay energy development in some areas.

## II. OIL SPILL DAMAGES

Oil spills have been an issue for more than just Congress and federal agencies. In *Ohio v. United States Dep't of the Interior*,<sup>1</sup> the U.S. Court of Appeals for the D.C. Circuit overturned the Department of the Interior's (DOIs) regulations on the valuation of damages for oil spills and leaks of hazardous substances. The Court found that the method used by the DOI was contrary to the Congressional intent under the Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA).<sup>2</sup> The regulation had required damages to be paid based on the lesser of the cost of restoration or the diminution of the use value of the resource.

The Court remanded the regulations to the DOI for clarification of its interpretation of the regulations concerning the application of CERCLA to private lands. The court found that CERCLA did not limit the definition of natural resources for which damages might be imposed to resources owned by the government. Although the regulatory language tracked the statute, the court felt regulatory comments appeared to exclude privately owned property no matter what level of management or control was exercised by a governmental agency.

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1. *Ohio v. United States Dep't of the Interior*, 880 F.2d 432 (D.C. Cir. 1989).

2. Pub. L. No. 96-510, §§ 107(a)(4)(c), (f)(1), 301(c)(2), 94 Stat. 2767 (1980) (codified as amended at 42 U.S.C. §§ 9607, 9651 (1982 & Supp. V 1987)).

### III. OUTER CONTINENTAL SHELF LEASING AND DEVELOPMENT TASK FORCE

In his February 9, 1989, budget address to Congress, President Bush announced a new cabinet level task force to review environmental concerns in three outer Continental Shelf (OCS) oil and gas lease sales scheduled for the 1990 fiscal year. These sales were Sale 91, Northern California, Sale 95, Southern California and Sale 116, Part II, Eastern Gulf of Mexico. On August 11, 1989, the Task Force issued a notice summarizing the environmental concerns presented to it as of that date and soliciting comments on any additional concerns.<sup>3</sup> The comments were to be considered by the Task Force in developing its report for submission to the President by January 1, 1990. We can expect to hear more on this report in 1990.

### IV. MINERALS MANAGEMENT SERVICE COAL VALUATION REGULATIONS

In his last days at the Department of the Interior, Secretary Donald Hodel approved new coal valuation royalty regulations.<sup>4</sup> The stated purpose of the final regulations was to clarify the methods by which value is determined and provide uniform guidance to the industry. Among other things, the regulations allowed operators to deduct state severance taxes, black lung taxes and abandoned mine reclamation fees from the reported value of the coal they mined, thus reducing royalties by about \$33 million per year. However, even before the March, 1989 effective date, incoming Secretary Manuel Lujan indicated that he was going to propose that these deductions be eliminated because they did not appear to stimulate an increase in consumption. The Secretary also indicated that he would consider lowering the royalty rate if the industry could make a case for it.

Following Secretary Lujan's comments, MMS reopened the comment period but did not stay the effectiveness of the final rule.<sup>5</sup> MMS did not make any specific proposal but requested additional comments on the fiscal impact of the deductions on the Federal Treasury, states, Indian tribes and on coal production.<sup>6</sup> Based on prior experience, it will probably be a year or more before changes, if any, are made to the regulations. The President's proposed 1991 budget, released January 29, 1990, shows no change in expected revenues for coal.

### V. GEOTHERMAL ROYALTY REGULATIONS

In addition to coal valuation regulations, the MMS is proposing regulations affecting royalties on geothermal resource valuation.<sup>7</sup> Current valuation standards are grouped according to how geothermal resources are utilized: electrical generation, direct utilization, and/or recovery of by-products.

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3. Notice 54 Fed. Reg. 33,150 (1989).

4. Final Rule 54 Fed. Reg. 1492 (1989); 30 C.F.R. pts. 202, 203, 206, 210, 212 (1989).

5. Notice of Meeting and Request for Comments, 54 Fed. Reg. 16,105 (1989).

6. *Id.*

7. 54 Fed. Reg. 354 (1989) (to be codified at 30 C.F.R. pts. 202, 206, 210, 212) (proposed Jan. 5, 1989).

Within each group, valuation standards are described according to the type of transaction: arm's-length or non-arm's-length and dispositions of the resource not subject to a sales transaction. The valuation procedures are different for each group. For geothermal resources sold under an arm's-length contract, proposed section 206.352(b) would provide that the lessee's gross proceeds accruing from the arm's-length transaction would establish the value of the resource for royalty purposes. MMS reserves the right to establish a different value if it determines that the contract does not reflect the total consideration or discovers that the value is unreasonable due to impropriety between the contracting parties.

For geothermal resources used to generate electricity and not sold through an arm's-length contract, proposed section 206.352(c) provides a sequence of benchmarks to value the resource. The value would be established in accordance with the first applicable of the following procedures:

- (1) the weighted average of the gross proceeds paid or received by the lessee under its own arm's-length contracts for the purchase or sale of similar quantities of like quality resources in the same field; or
- (2) the value determined by the netback method taking into account the lessee's costs of generating and transmitting electricity; or
- (3) any other reasonable valuation method approved by MMS.

In 1990, we may see final regulations on this subject. Because these proposed regulations are similar in approach to those for oil and gas, not much change is expected.

## VI. FOREST SERVICE RULES FOR OIL AND GAS LEASING

On January 23, 1989, the Forest Service issued a notice of proposed rulemaking to develop its oil and gas leasing procedures.<sup>8</sup> In the past, the Forest Service relied on the Bureau of Land Management (BLM) procedures and regulations; however, federal courts have ruled that the Service must promulgate its own procedures and regulations. Additionally, the Federal Onshore Oil and Gas Leasing Reform Act of 1987<sup>9</sup> expanded the authority of the Secretary of Agriculture in the management of oil and gas resources on national forest system lands and directed the Secretary to issue rules on bonding and reclamation standards.<sup>10</sup> The proposed rule is designed to fulfill these judicial and statutory requirements as well as to coordinate Forest Service oil and gas resource management with BLM efforts.

The proposed rules identify steps by which the Forest Service will identify potential leaseholds and coordinate leasing with the BLM. They also require operators to obtain Forest Service approval of a surface use plan of operations before conducting any operations, establish bonding requirements and oversee reclamation operations. Additionally, the Forest Service seeks to establish procedures to deal with material, non-material and emergency

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8. 54 Fed. Reg. 3326 (1989) (to be codified at 36 C.F.R. pts. 211, 228, 261) (proposed Jan. 23, 1989).

9. 16 U.S.C. § 3148 (Supp. V 1987); 30 U.S.C. §§ 187a, 187b, 188, 191, 195, 226, 226-3 (Supp. V 1987).

10. 30 U.S.C. § 226 (1988).

instances of noncompliance. Criminal penalties for non-compliance are available to the Forest Service.

Both the additional requirements sought by the Forest Service and necessary coordination with the BLM will create added complexity for lessees. In some ways, however, having formal regulations should avoid some of the confusion that has resulted from the informal arrangements of the past.

## VII. NATURAL GAS WELLHEAD DECONTROL ACT OF 1989

In 1989, the thirty-five year struggle over deregulation of the prices charged by producers of natural gas finally came to an end when the President signed the Natural Gas Wellhead Decontrol Act of 1989 (the Act).<sup>11</sup> The Act, which went into effect July 26, 1989, will phase out federal control of wellhead prices charged by producers by the end of 1992. Some interstate sales of gas at wholesale have been subject to regulation since the Supreme Court's decision in *Phillips Petroleum Company v. Wisconsin*,<sup>12</sup> and other dispositions were brought under federal control with the enactment of the Natural Gas Policy Act of 1978 (the NGPA).<sup>13</sup> While the NGPA deregulated certain gas, it provided for perpetual regulation of other gas.

The Act deregulated all otherwise regulated gas to which no first sale contract applied on the date of enactment. If regulated gas was subject to a contract, even if gas was not flowing on the date of enactment (*e.g.*, it was shut in), it continues to be subject to regulation until deregulated pursuant to one of the other provisions of the Act. Price regulations cease to apply: (1) when the contract expires or is terminated; or (2) when the parties to the contract, by written agreement, provide that the gas will be deregulated; provided, however, that such written agreement must have been entered into after March 23, 1989, must provide a specified date for deregulation, and must not have been effective prior to July 26, 1989.

Further, in the case of a well spudded after the date of enactment, gas from that well is deregulated effective May 15, 1991, if not earlier freed from price controls. In addition, all wellhead sales of gas not otherwise deregulated are to be freed from regulation on January 1, 1993; however, the Act preserves the authority of each state to regulate wellhead sales prices of gas produced and consumed in that state. Finally, the Act also frees price-decontrolled gas from the certificate and abandonment provisions of the Natural Gas Act.<sup>14</sup>

On December 13, 1989, the Federal Energy Regulatory Commission issued a Notice of Proposed Rulemaking setting forth a proposed set of regulations for public comment to be included in the Act.<sup>15</sup>

In analyzing the impact of the Act for federal lessees, one quickly concludes that gas marketing will be more competitive because of the movement from regulated pricing to market-based pricing. Regulation has artificially

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11. Pub. L. No. 101-60, 103 Stat. 157 (1989).

12. *Phillips Petroleum Co. v. Wisconsin*, 247 U.S. 672 (1954).

13. 15 U.S.C. §§ 3301-3432 (1988).

14. 15 U.S.C. §§ 717-717w (1988).

15. 54 Fed. Reg. 51,902 (1989) (to be codified at 18 C.F.R. pt. 272) (proposed Dec. 19, 1989).

increased prices for some gas to above market-clearing levels while artificially restraining prices for other gas. Perhaps more important, freeing gas from the certificate and abandonment requirements of the Natural Gas Act will enable lessees to get gas to the markets that want it most (provided, of course, that transportation is available). The result will be a national market with market-set prices. This should encourage gas producers to seek additional federal leases and encourage production of gas from old leases that might otherwise have been prematurely abandoned due to low wellhead prices. In short, increased economic efficiency is likely to be a chief result of wellhead price deregulation. This efficiency should inure to the benefit of both private and public land development.

#### VIII. 1990 AND BEYOND

Recent Presidential appointments, the public statements of the President, and deliberations in Congress all indicate that there will be more emphasis on appointing administrators which are sensitive to environmental issues and on increasing federal revenues from public lands. This applies to all federal agencies that affect energy development. Although the President is proposing some tax breaks for industry, these proposals face tough battles in Congress. In addition, the IRS and the DOI will be under increased pressure to make sure that the Government has collected all the royalties and windfall profits taxes to which it is entitled.

If Congress and the federal agencies continue to pursue the unresolved issues generated in 1989 on the topic of federal lands, we can expect a busy year in 1990.

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