DOI—Minerals Management Service (MMS)

PROPOSED RULE STAGE

76. • RELIEF OR REDUCTION IN ROYALTY RATES — DEEP GAS PROVISIONS

Priority:

Economically Significant. Major under 5 USC 801.

Legal Authority:

43 USC 1331 et seq

CFR Citation:

30 CFR 203

Legal Deadline:

None

Abstract:

Declines in outer continental shelf production from existing fields need to be offset by new sources to keep up with growing demand. Very little of the deep gas potential in shallow water areas of the Gulf of Mexico has yet been explored. Extensive infrastructure already exists in shallow water, unlike in deep water, so new production could reach market quickly. Because the most prospective tracts in shallow water are already under lease, most of the deep gas potential in shallow water may already have been acquired. This rule proposes temporary incentives in the form of royalty suspension volumes for deep wells (at least 15,000 feet below significant energy action level) on existing leases that explore for or produce gas.

Statement of Need:

Very little of the deep gas potential in shallow water areas of the Gulf of Mexico has yet been explored. Extensive infrastructure already exists in shallow water, unlike in deep water, so new production could reach market quickly. Because the most productive

tracts in shallow water are already under lease, most of the deep gas potential in shallow water may already have been acquired. This rule would accelerate exploration and production of deep gas by providing temporary incentives in the form of royalty suspension volumes for deep wells on existing leases that explore for or produce gas.

Summary of Legal Basis:

The OCS Lands Act is the basis for our regulations on suspending or lowering royalties on ''producing'' OCS leases. The Deep Water Royalty Relief Act, which amended the OCS Lands Act, is the basis for regulations to reduce or eliminate royalty on ''non-producing'' leases in the Gulf of Mexico west of 87 degrees, 30 minutes West longitude. It gives the Secretary of the Interior this authority to (1) promote development or increased production on producing and non-producing leases, or (2) encourage production of marginal resources on producing and non-producing leases.

Alternatives:

There are two alternatives — providing incentives only through the lease sale process, or through an application process. Reserving the deep gas incentive only for new leases issued in future sales

will not encourage exploration and production of much of the deep gas potential that underlies existing leases. Many of the best blocks have not been through a sale in decades. Also, new leases would be less able to use the existing infrastructure than existing leases so additional gas production would be delayed. Granting royalty relief on a case-by-case basis to existing leases would better protect against unnecessary royalty relief but is unlikely to encourage much additional production. The unavoidable complexity and delays in a system like we use in the discretionary deep water royalty relief program would discourage many lessees and delay the desired activity by those that would apply.

Anticipated Cost and Benefits:

Costs of this program to the federal government are the foregone royalties associated with drilling and production of deep gas that would have occurred even if no royalty suspension incentives were offered. We estimate that recipients of deep gas royalty relief will earn an average of 350 Bcf of gas royalty relief each year from activity that would have taken place without the program.

This rule's royalty benefits derive from the extra gas production (i.e., gas produced in excess of the royalty suspension volumes) from discoveries induced by the program incentives and resulting drilling. We estimate this benefit to be, on average, 370 Bcf of gas each year, yielding a net annual royalty benefit of 20 Bcf.

The additional gas production resulting from this rule also offers an important timing benefit. We do not expect significant gas production from deep water for another 10-15 years. We estimate that this rule will result in twice as many deep wells drilled each year of the program producing 1 to 2 Tcf more gas production in shallow water. The additional gas volumes will help offset declines in other OCS gas production until deep water gas comes on stream, thereby moderating gas prices and reducing the need for gas imports and consumption of dirtier fuels.

Risks:

The risk of not offering royalty relief provided in this rulemaking

action is that some deep gas resources in shallow water will not be

developed, at least not during a period when growing demand and declines in traditional sources for natural gas will lead to volatile prices.

Timetable:

Action	Date	FR Cite
NPRM	11/00/02	
NPRM Comment Period End	01/00/03	

Regulatory Flexibility Analysis Required:

No

Government Levels Affected:

None

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