

**UNITED STATES OF AMERICA
DEPARTMENT OF THE INTERIOR
MINERALS MANAGEMENT SERVICE**

The Open and Non-Discriminatory)	
Movement of Oil and Gas as Required)	Advance Notice of
by the Outer Continental Shelf Lands Act)	Proposed Rulemaking

**COMMENTS OF
INDICATED PRODUCERS**

The Indicated Producers¹ hereby submit Comments in response to the April 12, 2004 Advance Notice of Proposed Rulemaking (“Notice”) issued by the Minerals Management Service (“MMS”) of the United States Department of Interior (“Interior”) in the above-referenced proceeding. *The Open and Non-Discriminatory Movement of Oil and Gas as Required by the Outer Continental Shelf Lands Act*, 69 Fed. Reg. 19,137 (April 12, 2004). In the Notice, the MMS solicits comments to assist the MMS in potentially amending its regulations to implement its authority to ensure that, as required by Sections 5(e) and (f) of the Outer Continental Shelf Lands Act (“OCSLA”), 43 U.S.C. §§ 1334(e) and (f), pipelines provide open and non-discriminatory access to their facilities and services.

These comments are intended to address only the open and non-discriminatory access requirement as it applies to natural gas pipelines. The comments are not intended to address oil pipelines.² To the extent members of Indicated Producers wish to comment on MMS’

¹ Indicated Producers are an *ad hoc* group of companies having interests in natural gas transported on interstate pipelines and production-related facilities in the Gulf of Mexico. The members of the group for purposes of these Comments are BP America Production Company, Chevron U.S.A. Inc., Exxon Mobil Corporation, and Shell Offshore Inc.

² While these comments do not address oil pipelines, the arguments presented herein, which demonstrate that the non-discrimination and open access condition does not and should not apply to production and production-related facilities and activities, apply with equal force to the

application of the non-discrimination and open access condition to oil pipelines, these companies or their affiliates will do so in separate comments.

I. INTRODUCTION

MMS issued the Notice in the aftermath of the Court decision vacating the Federal Energy Regulatory Commission's ("FERC") regulations requiring companies providing certain services in the Outer Continental Shelf ("OCS") to periodically file information with FERC concerning their services, shippers, rates, and terms and conditions of service.³ Under the guise of authority it claimed under Sections 5(e) and (f) of OCSLA, FERC had promulgated the regulations in Order No. 639,⁴ with the view that the resulting regulations "would enhance competitive and open access to gas transportation."⁵ FERC extended the reporting requirements not just to pipeline services on the OCS, but also to production-related services. The D.C. Circuit, however, held that FERC in Order No. 639 had overstepped its bounds under OCSLA. Specifically, the Court vacated Order No. 639 on grounds that FERC's authority under OCSLA is limited to specific tasks and does not give FERC "general powers to create and enforce open access rules on the OCS."⁶ In contrast, the D.C. Circuit pointed to the Secretary of Interior's authority to grant rights-of-way for all pipelines in the OCS. On this basis, the Court concluded

production of oil and gas.

³ *Chevron U.S.A., Inc. v. FERC*, 193 F. Supp. 2d 54 (D. D.C. 2002), *aff'd sub nom. The Williams Cos. v. FERC*, 345 F.3d 910 (D.C. Cir. 2003).

⁴ *Regulations Under the Outer Continental Shelf Lands Act Governing the Movement of Natural Gas on Facilities on the Outer Continental Shelf*, Order No. 639, F.E.R.C. Stats. & Regs. [Regs. Preambles, 1996-2000] (CCH) ¶ 31,097 (2000); *order on reh'g*, Order No. 639-A, F.E.R.C. Stats. & Regs. [Regs. Preambles, 1996-2000] (CCH) ¶ 31,103 (2000).

⁵ *Williams*, 345 F.3d at 911.

⁶ *Id.* at 916; *see also Chevron*, 193 F. Supp. 2d at 70-71.

that Congress intended to place enforcement of the open access and non-discrimination requirements in the hands of the Secretary of the Interior.⁷

In the face of the D.C. Circuit's conclusion that Interior, rather than FERC, has general enforcement authority under OCSLA, MMS issued its Notice to solicit "comment on the scope, proposed action, and possible alternatives the MMS should consider . . . in fulfilling its responsibility of assuring open and non-discriminatory access to pipelines in the OCS." Notice at 19,138.

II. EXECUTIVE SUMMARY

Indicated Producers appreciate the opportunity to present their views on MMS' proposed implementation of its authority to enforce the non-discrimination and open access requirements under Sections 5(e) and (f) of OCSLA. Indicated Producers have been involved in exploration, development and production activities in the OCS for over 50 years. As lessees in numerous OCS leases in the Gulf of Mexico ("GOM"), and as producers of a significant percentage of the oil and gas produced from the GOM, Indicated Producers have a vital interest in MMS' implementation of its authority under OCSLA.

There are two fundamental principles underlying Indicated Producers' comments. First, MMS should not establish a regulatory regime that goes beyond the scope of the authority granted to MMS under OCSLA. Second, any regulatory regime adopted in this rulemaking should not impose excessive burdens on entities subject to OCSLA, but rather should carefully balance the need for the regulations with their associated burdens.

Under the express terms of OCSLA, the non-discrimination and open access requirements apply only to pipeline facilities used in providing transportation services. *The*

⁷ *Williams*, 345 F.3d at 913.

requirements do not apply to production platforms, production and production-related facilities on platforms or upstream of such platforms, or to production and production-related facilities in multi-platform production complexes in the OCS, or to the production-related activities undertaken in or on such facilities. Production is an activity separate from pipeline transportation. Production activities are undertaken under rights held by producers under oil and gas leases issued by the MMS. Under the plain terms of Sections 5(e) and (f) of OCSLA, the non-discrimination and open access requirements apply only to the rights-of-way and other grants of authority relating to pipeline transportation. These requirements do not apply to the rights granted pursuant to oil and gas leases.

In so limiting the reach of the non-discrimination and open access requirements, Congress wisely excluded production-related activities. Producers hold the exclusive right to produce oil and gas under leases granted by the Department of the Interior. The imposition of a non-discrimination and open access condition on production-related facilities and activities would directly undermine the contract and property rights held by lessees. Further, oil and gas production is a highly competitive industry in the United States. Producers invest huge sums – as much as \$1.5 billion in a single project – in offshore leases and infrastructure. The willingness of producers to make this investment would be undermined if others could demand access to platforms and other production-related facilities after the producers have undertaken the substantial risk and expense of building the platforms and associated production-related infrastructure.

To the extent MMS adopts a regulatory regime to enforce OCSLA Sections 5(e) and (f), the regime should not impose unwarranted burdens. Problems relating to access and discrimination have arisen on FERC-regulated interstate gas pipelines that FERC, after many

years of regulating the facilities and associated services, reclassified as gathering and permitted to be sold or otherwise transferred to affiliated or unaffiliated companies not subject to FERC's NGA regulation. Some gas gathering pipelines have never been regulated by FERC under the NGA. However, in the so-called spindowns and spin-offs, FERC's actions eliminating its jurisdiction under the NGA over the rates and terms and conditions of gathering service occurred at a time long after producers had connected their reserves. At that point in time, reserves are typically depleted to levels that foreclose the economical construction of alternative pipeline facilities. The result is that most of these gathering facilities provide their owners substantial market power with which to exact monopolistic rates and terms and conditions of service. But MMS can effectively address these problems without imposing onerous regulatory burdens.

Specifically, MMS should not adopt a program that includes reporting requirements such as those implemented by FERC in its Order No. 639 and vacated in *Williams*. A reporting regime would be particularly burdensome in the event that MMS, contrary to Indicated Producers' comments, adopted the ill-advised position that MMS should encompass production-related facilities and services within the proposed rules. Production-related activities are complex and entail the operation of extensive facilities. These operations are governed by multiple, complex contracts among lessees and working interest owners having interests in the offshore production. The operations, configuration of facilities, and contractual arrangements are constantly changing. The imposition of a periodic reporting regime on the charges and terms and conditions governing these complex and ever-changing production-related activities would be highly burdensome and costly to both industry and the MMS. This burden would be pointless because the exploration and production business is highly competitive, and production and

exploration activities have been undertaken in the GOM for more than 50 years without the need for regulatory intervention.

Instead, MMS should adopt a complaint-based approach. This regime should comprise two mechanisms. First, MMS should adopt a hotline mechanism modeled on FERC's Enforcement Hotline. Market participants could informally bring their complaints to MMS' attention through this hotline mechanism, and MMS personnel could then attempt to resolve any dispute without the need for formal proceedings. To address the situations where this informal process fails, MMS should have in place more formal procedures for the prosecution of a complaint. These procedures, which should also be modeled on those available at FERC, must entail the right of discovery through depositions, interrogatories and other traditional discovery tools, the right to a hearing on the record before an Administrative Law Judge with the right to present witnesses and to cross-examine opposing witnesses, and an avenue for appeal to the person delegated the authority as the ultimate decisionmaker for the Department of the Interior. Further, clear procedures providing for a timely and final decision that can be appealed to the courts should be put in place. With the more formal complaint process in place, MMS and industry participants will have the ease, convenience, and efficiency of informal resolution and the availability of a formal process for more contentious or complex cases.

To the extent parties provide information to MMS and other parties during the informal and formal complaint process, the information provider should have the right to seek protection from public disclosure, under the Freedom of Information Act ("FOIA") or otherwise, of commercially sensitive and other confidential or proprietary information. Determination of confidentiality should be done on a case-by-case basis. Again, FERC has in place procedures that provide a good model for such procedures.

Finally, the rulemaking to implement MMS' authority under Sections 5(e) and (f) should not be used as a pretext to change MMS' royalty valuation regulations. MMS permits lessees to deduct from royalty value certain costs of transportation. MMS disallows the costs it defines as "gathering." There is nothing in Sections 5(e) and (f) that requires or permits MMS to alter its definitions and policies relating to deductible transportation and non-deductible gathering, or otherwise to amend its regulations affecting the royalties due under the terms of the applicable oil and gas leases.

III. DISCUSSION

A. MMS' Proposed Regulations Should Only Encompass The Facilities And Services Subject To OCSLA's Non-Discrimination And Open Access Standard.

1. An Overview of the Authority Held By the Department of the Interior and FERC, Respectively, under the Non-Discrimination and Open Access Provisions of OCSLA.

a. The Statutory Provisions.

i. The Purposes of the Statute.

In 1953, in passing OCSLA, Congress addressed the issue of federal authority over the submerged lands extending seaward from the navigable waters of the United States, otherwise known as the OCS. In 1978, Congress substantively amended OCSLA to provide for increased domestic development of resources on the OCS, increased environmental protections, public compensation from OCS development, and a competitive market structure. *See* H.R. Rep. No. 95-590, at 122 (1978), *reprinted in* 1978 U.S.C.C.A.N. 1450.

Under OCSLA, the exploration, development, and production of minerals on the OCS were brought under federal control, and a framework was established for federal coordination and support of similar state and local activities in State Coastal Zones. Congress allocated the primary responsibility for administering the statute to the Secretary of the

Department of the Interior, including the regulation and administration of mineral leasing and the exploration and development of leased areas in the OCS. *See, e.g.*, 43 U.S.C. § 1334(a) (the Secretary of the Interior shall have the power to “administer the provisions of this subchapter relating to the leasing of the [OCS], and shall prescribe such rules and regulations as may be necessary to carry out such provisions”). The Secretary of the Interior has the authority under OCSLA over the issuance of oil and gas leases, whose terms govern, among other things, the exploration, development and production of oil and gas (43 U.S.C. §§ 1337(a) and (b)). More limited authority over specific matters was given to other governmental agencies. *See, e.g.*, 43 U.S.C. §§ 1334(a), 1334(f), 1334(g), 1337(a) (granting regulatory authority over specific matters to the Departments of the Interior, Energy, Transportation and Justice, and to FERC and the Federal Trade Commission).

ii. OCSLA Section 5(e).

Section 5(e) of the OCSLA provides the Secretary of the Interior with the authority to grant certain rights-of-way conditioned on the obligation of the pipelines to transport or purchase without discrimination:

Rights-of-way through the submerged lands of the outer Continental Shelf, whether or not such lands are included in a lease maintained or issued pursuant to this subchapter, may be granted by the Secretary for *pipeline* purposes for the *transportation* of oil, natural gas, sulfur, or other minerals, or under such regulations and such conditions as may be prescribed by the Secretary . . . and upon the express condition that oil or gas *pipelines shall transport or purchase without discrimination, oil or natural gas* produced from submerged lands or outer Continental Shelf lands in the vicinity of the *pipelines* in such proportionate amounts as the Federal Energy Regulatory Commission, in consultation with the Secretary of Energy, may . . . determine to be reasonable, taking into account, among other things, conservation and the prevention of waste.

43 U.S.C. § 1334(e) (emphasis added). Under this Section, FERC's authority is limited to the determination, in consultation with the Secretary of Energy, of "proportionate amounts" of oil and gas production to be transported or purchased by pipelines.

iii. OCSLA Section 5(f).

Section 5(f)(1)(A) of OCSLA further establishes that oil and gas pipelines on the OCS must provide open and non-discriminatory access:

Except as provided in paragraph (2) [under which FERC is entitled to exempt *pipelines* that feed into facilities where oil and gas are first collected or first separated, dehydrated or otherwise processed], every permit, license, easement, right-of-way, or other grant of authority for the *transportation by pipeline* on or across the outer Continental Shelf of oil or gas shall require that the *pipeline* be operated in accordance with the following competitive principles:

(A) *The pipeline must provide open and nondiscriminatory access to both owner and non-owner shippers.*

43 U.S.C. § 1334(f)(1)(A) (emphasis added). It is important to note that the phrase "permit, license, easement, right-of-way, or other grant[s] of authority" referenced in the statute are not limited to those grants issued pursuant to OCSLA, but rather appear also to refer to grants such as the issuance by FERC of a certificate of public convenience and necessity under the NGA.

OCSLA Section 5(f) refers to FERC in its various subparts. OCSLA Section 5(f)(1)(B) gives FERC the power to

order a subsequent expansion of throughput capacity of any *pipeline* for which the permit, license, easement, right-of-way, or other grant of authority is approved or issued after September 18, 1978.

43 U.S.C. § 1334(f)(1)(B) (emphasis added). This authority is significantly limited by the last sentence of Section 5(f)(1)(B), which provides that the paragraph does not apply to pipelines in the Gulf of Mexico or the Santa Barbara Channel.

Section 5(f)(2) allows FERC to exempt a “pipeline or class of pipelines” from any of the requirements of Section 5(f)(1) if the pipeline

feeds into a facility where oil and gas are first collected or a facility where oil and gas are first separated, dehydrated, or otherwise processed.

43 U.S.C. § 1334(f)(2). FERC’s authority to exempt feeder lines is important inasmuch as it must be FERC that exempts such lines, even from rules such as proposed in this rulemaking by MMS to enforce the open access and non-discrimination provisions of OCSLA.

Finally, Section 5(f)(3) establishes that FERC

shall consult with and give due consideration to the views of the Attorney General on specific conditions to be included in any permit, license, easement, right-of-way, or grant of authority in order to ensure that *pipelines* are operated in accordance with the competitive principles set forth in [Section 1334(f)(1)].

43 U.S.C. § 1334(f)(3) (emphasis added).

b. The Demise of FERC’s Prior Regulatory Program to Implement OCSLA Sections 5(e) and (f).

As MMS observed in its Notice, this rulemaking emanates from the action of the D.C. Circuit vacating FERC’s regulations promulgated to implement what FERC believed to be its authority to enforce Sections 5(e) and (f) of OCSLA. The D.C. Circuit vacated FERC’s regulations based on the conclusion that the Department of the Interior, not FERC, holds this enforcement authority.

As interpreted by the D.C. Circuit in the Order No. 639 appeal, neither Section 5(e) nor Section 5(f) provides FERC with the authority to promulgate regulations setting forth reporting requirements on pipelines and other service providers to enforce OCSLA’s open access and non-discrimination provisions.⁸ Specifically, the D.C. Circuit vacated FERC’s reporting

⁸ *Williams*, 345 F.3d at 913-14.

regime purportedly established as part of FERC's effort to enforce the open access and non-discrimination provisions in OCSLA. As the Court noted, OCSLA Section 5(e) "grants FERC a single power: to determine, along with the Secretary of Energy, the proportions of oil, gas, or other minerals that each member of any relevant group of pipelines may be required to transport or purchase pursuant to those conditions," *i.e.*, to determine ratable take orders.⁹ For this reason, the Court concluded that Congress intended to place enforcement in the hands of the Department of the Interior or other obligee of the rights-of-way granted under Section 5(e) by the Secretary of the Interior, subject to the open access and non-discrimination condition.¹⁰

The Court also analyzed Section 5(f) and again concluded that FERC is not given general enforcement authority, but rather is given specific, limited authority. The Court noted that portions of Section 5(f) are directed at FERC's role as licensor, such as the issuer of certificates of public convenience and necessity pursuant to Section 7(c) of the Natural Gas Act, 15 U.S.C. § 717f(c). For example, Section 5(f)(1) "states that permits, licenses, easements, etc., granted to pipelines for transportation through the OCS, 'shall require' the firms in question to operate their pipelines in accordance with the . . . 'competitive principles'" pronounced in subsections (A) and (B) of Sections 5(f)(1). Thus, under OCSLA Section 5(f)(1), FERC must impose the open access and non-discrimination conditions on all certificates that it issues under NGA Section 7.¹¹

Further, Section 5(f)(3) directs FERC to consult with the Attorney General on the "specific conditions" to be imposed when crafting any license or other grant of authority

⁹ *Id.* at 913.

¹⁰ *Id.* at 913-14.

¹¹ *Id.* at 914.

