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A View from the (Deepwater) Horizon:

Regulatory and Statutory Developments Affecting Offshore Drilling and Spill Liability

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Atlanta, Austin, Chicago, Dallas, Houston, London, Los Angeles, New Orleans, New York, Sacramento, San Francisco, Washington DC

Discussion Overview

- The Deepwater Drilling Moratorium
- National Notices to Lessees and Operators
- Drilling Safety Rule and Workplace Safety Rule
- Review of NEPA categorical exclusions
- Proposed Legislation and Common Themes
- Predictions

Drilling Moratorium

- Initially issued 5/27/2010.
- Injunction lifting moratorium 6/22/2010.
- New moratorium issued 7/12/2010.
- Scheduled to Expire 11/30/2010.
- Lifted 10/12/2010.
- Interior Department held in contempt 2/2/2011.

Drilling Moratorium

- Permit issuance and approvals have been slow.
 - As of 2/11/2011, since the accident:
 - First lease sale still has not yet occurred, although the first is expected sometime this year.
 - 9 applications for deepwater wells are pending.
 - First one not expected to be issued until mid-year.
 - On 1/28/2011, the Department of Interior accepted its first application for deepwater exploration since the accident.
 - Application was first received 10/28/2010.
 - Revised seven times before it was “accepted.”

Drilling Moratorium

- On 12/13/2010, Bureau of Ocean Energy Management, Regulation & Enforcement (BOEM) issued guidance to assist in submitting information that would better facilitate approvals of activities using a drilling rig with a subsea blowout preventor (BOP), a floating drill rig using a surface BOP system, or a drilling rig on a floating platform.
 - Information also facilitates BOEM's preparation of Environmental Assessments.

Drilling Moratorium

- 2/17/2011 – Judge Feldman ordered BOEM to act on five pending applications in which Ensco Offshore Co. has a contractual stake - within 30 days.

Notice to Lessees No. 2010-N05

- Effective June 8, 2010.
- Required operators to submit CEO certification by June 28, 2010 regarding:
 - Their knowledge of rules governing oil and gas and sulphur operations in the Outer Continental Shelf (OCS) and compliance with those regulations.
 - Examination of
 - All well control system equipment to ensure functionality.
 - All rig drilling casing, cementing, well abandonment, completion and workover practices to ensure well control.
 - All emergency and dynamic positioning procedures.
 - Personnel training and competence.
- Required operators using a subsea Blowout Preventer (BOP) system or using a BOP stack on a floating platform on 5/27/10 to submit BOP and well control system information by June 17, 2010.
- Before beginning or resuming drilling, required third party verification and certification of:
 - All BOP equipment used in new floating drilling operations.
 - Suitability of the BOP stack for the specific equipment on a rig.
 - Functionality of blind-shear rams installed in a BOP stack.
 - Appropriateness of well casing designs and cementing program/procedures.

Notice of Lessees No. 2010-N06

- Effective June 18, 2010 – Expires June 1, 2015.
- Rescinded limitations in NTL No. 2008-G04 regarding the scope of information about blowout and worst case discharge scenarios that had to be submitted with an Exploration Plan.
- NTL No. 2010-N06 inapplicable if an operator is only acting under a non-deep water Application for Permit to Drill that was approved before June 18, 2010.
- Much more detailed information now required with an exploration plan.
 - Blowout scenario for potential blowouts expected to have the highest volume of oil released.
 - Assumptions and calculations underpinning the worst case discharge scenario.
 - Description of measures to enhance ability to prevent a blowout.

Notice of Lessees No. 2010-N10

- Effective November 8, 2010 – Expires November 8, 2015.
- Applicable to operators using a drilling rig with a subsea BOP system or a floating facility with a surface BOP system.
- Requires statement with each well permit application signed by an authorized company official, stating that the operator will conduct all authorized activities in compliance with law.
- Notifies of BOEM's review of Oil Spill Response Plans to confirm adequate information regarding surface and subsea containment equipment that an operator can access in a spill event.
 - Encourages voluntary revisions before being directed to revise.

Drilling Safety Rule

- Interim Final Rule announced 9/30/10 and effective 10/14/10.
- Applicable to drilling on the Outer Continental Shelf.
- Organized between Well Bore Integrity Rules and rules governing Well Control Equipment and Procedures.
- Well Bore Integrity rules require, among other things:
 - Mandatory use of API Standard RP 65 – Part 2, Isolating Potential Flow Zones During Well Construction.
 - Submittal of Professional Engineer Certification that casing and cementing program is appropriate.
 - PE certification of the presence of two independent test barriers across each flow path during well completion.
 - BOEM approval before replacing heavier drilling fluids with lighter drilling fluids.
 - Enhanced deep water well control training for rig personnel.

Drilling Safety Rule

- Well Control Equipment and Procedures rules (applicable to the BOP and BOP control systems) require, among other things:
 - Submittal of documentation and schematics for all control systems.
 - Certain engineer certifications regarding the capabilities of the blind-shear rams under maximum anticipated pressure.
 - A Subsea BOP stack to be equipped with Remotely Operated Vehicle (ROV) capability.
 - Maintenance of a ROV and ROV trained crews on floating rigs at all times.
 - Auto shear and deadman systems for dynamically positioned rigs.
 - Prescribed training for personnel operating BOP equipment.
 - Documentation of subsea BOP inspections and maintenance according to API RP 53.
 - Testing of well control systems.

Work Place Safety Rule

- Interim Final Rule announced 9/30/10 and effective 10/15/10.
- Applicable to all offshore oil and gas operations in Federal waters.
- Requires offshore oil and gas operators to develop and maintain a Safety and Environmental Management System (SEMS).
- Makes mandatory practices in API RP 75.
 - 13 elements.
 - Key elements are:
 - Hazards analysis.
 - Training.
 - Emergency response planning.
 - Periodic audits of SEMS, with initial 2-year evaluation and subsequent 3-year audit intervals.
 - Records and documentation.

NEPA Categorical Exclusions

- National Environmental Policy Act requires assessment of the environmental impact of major federal actions.
- OCS leasing, exploration and drilling activities can be the subject of Environmental Assessments (EAs) and even detailed Environmental Impact Statements (EISs).
- EISs can take approximately 2 years to conduct. EAs can take months to conduct.

NEPA Categorical Exclusions

- BOEM has categorical exclusions for activities for which EAs or EISs are not required because under normal circumstances they do not have and are not expected to have significant individual or cumulative environmental impacts, including:
 - Except in limited circumstances, approval of an offshore lease or unit exploration, development/production plan (offshore plan) in the central or western Gulf of Mexico.
 - Approval of or minor variances from activities described in an approved offshore plan.
 - Approval of drilling permit applications when the well and appropriate mitigation measures are described in an approved offshore plan.

NEPA Categorical Exclusions

- 8/16/10 – BOEM directed:
 - The first two listed categorical exclusions not be used where the proposed activity involves the use of a subsea BOP or a surface BOP on a floating facility.
 - Categorical exclusion review for all other offshore plans will be undertaken on a case by case basis.
 - Key consideration: Is the off shore plan's worst case discharge or peak production volume greater than that in the corresponding Oil Spill Response Plan?

NEPA Categorical Exclusions

- How BOEM has managed NEPA issues so far:
 - BOEM issued guidance on what operators must submit in an offshore plan to have their application “accepted.” Much of the information will facilitate the performance of an EA.
 - It may take months before the application is deemed “accepted.”
 - Only one application has yet been accepted.
 - Context: Supplemental Exploration Plan in a producing field.
 - Acceptance triggers a 30 day review period, including a 10-day period for public review and comment.
 - The EA will be prepared during the review period.
 - BOEM announced in November that it will conduct a supplemental EIS for remaining lease sales in the Gulf for the period ending 2012.

Proposed Legislation

- HR 3534
 - Passed House on July 30, 2010; no Senate action.
 - Mandates division of leasing, safety and environmental enforcement, and revenue collection functions.
 - **Requires regulations that:**
 - **Mandate third party certification of well control safety systems, and well casing and cementing programs and procedures.**
 - **Establish performance requirements for blow-out preventers.**
 - **Mandate safety and environmental management systems by OCS operators.**
 - **Imposes similar requirements for wells on state waters if a blowout could lead to extensive and widespread harm to safety or the environment.**
 - Requires lease bidders and well permit applicants to certify:
 - They meet due diligence, safety, and environmental requirements on other leases.
 - They have met all Oil Pollution Act obligations for all other discharges for which they were a responsible party.
 - In the previous 7 years [they were not BP].

Proposed Legislation

- HR 3534
 - Inspections
 - On-site inspection at least once/year for facilities on the OCS.
 - Scheduled on-site inspection at least once/month during drilling.
 - Periodic unannounced inspections.
 - Periodic audits of Safety and Environmental Management Plans.
 - **References cooperation in investigations as a condition of a lease or permit and maintenance of incident reports in a publicly available database.**
 - **Requires annual operator certification of compliance with laws and regulations.**
 - **Mandates CEO attestation of compliance, spill response capability and planning, and well design safety before issuing drilling permits.**
 - Eliminates streamlined exploration plan preparation practices for activities in the Gulf of Mexico and requires an analysis of blowout scenarios involving the **highest** potential volume of oil that may be discharged, and a description of response planning in response to same.

Proposed Legislation

- HR 3534
 - Penalties
 - Civil penalties raised to \$75K/day per violation.
 - If non-compliance is or was a threat of harm or damage to life, property, mineral deposits or the environment a civil penalty not more than \$150K must be assessed for each day.
 - Knowing and willful violations raised from \$100K to \$10 million.
 - Other Civil and administrative penalties are also increased.
 - Class I: Raised from \$10K to \$100K with a \$250K maximum (up from \$25K).
 - Class II: Raised from \$10K to \$100K with a \$1 million maximum (up from \$125K).
 - § 1321(b)(7): \$25K violations raised to \$100K; and per barrel limits raised to \$2500 from \$1000. (gross negligence violations are even higher)
 - Indexing for inflation.
 - ***Removes limit of liability for offshore facilities, presently set at removal costs plus \$75 million, absent gross negligence, willful misconduct, or non-compliance.***
 - Financial responsibility for offshore facilities raised from \$35 million (OCS) and \$10 million (state waters) to \$300 million.
 - **Adds damages to human health (including mental health) as compensable damages under OPA.**

Proposed Legislation

- S. 3516 – Outer Continental Shelf Reform Act of 2010
 - Passed on a bipartisan basis by the Senate Energy and Natural Resources Committee on June 30, 2010.
 - Did not receive full Senate consideration – lack of support from key Democrats, including Landrieu and Begich.
 - More modest in scope than corresponding House bill.
 - Key provisions:
 - Endorses Salazar's plan to separate leasing and revenue functions from environmental and safety regulation functions.
 - Requirements for exploration plans:
 - Requires information on major-safety related equipment and a demonstration that it meets best available technology requirements.
 - Mandates preparation of blowout scenarios and response plans for highest “expected” volume of oil.
 - Gives regulators 90 day approval periods (rather than current 30 day period) with extensions of up to 180 days.

Proposed Legislation

- S. 3516
 - Key provisions:
 - Drilling permits
 - Review by at least 2 agency engineers.
 - Written determination of:
 - » Critical safety systems will use best available technology.
 - » Blowout prevention systems will include redundancy and remote triggering capability.
 - Requires approval of Safety and Environmental Management Plan.
 - » At least 2 environmental and safety managers who are employees and will be present at all times.
 - » By 5/1/2012 requires all rig employees meet training and experience requirements.
 - **By 5/1/2011, applications to be accompanied by a *SAFETY CASE* – complete set of safety documentation to determine if a system is adequately safe for a given application in a given environment.**
 - Incident reports and data are to be available in a publicly available database.

Proposed Legislation

- S. 3516
 - Key Provisions
 - Penalties under Outer Continental Shelf Act:
 - Civil - \$75K/day (raised from \$20K).
 - Criminal – raised cap from \$100,000 to \$10,000,000 for knowing and willful violations.
 - Increases with Consumer Price Index.
 - Requires regulations within two years after enactment requiring offshore exploration, development and production systems to be constructed, maintained and operated so as to meet standards that protect health safety, and the environment as verified by independent third parties.
 - Applicable at least to mobile offshore drilling units, fixed and floating drilling or production facilities, and equipment dedicated to safety systems.

What Does the Future Hold?

- Outer Continental Shelf Safety Oversight 9/1/10 Board Report.
 - Results from charge to provide recommendations to improve and strengthen DOI's management, regulation and oversight.
 - Key Enforcement Recommendations:
 - Evaluate deterrence of present enforcement methods; consider sanctions for repeat offenders whose violations don't trigger civil penalties under current standards. because they are corrected within a short period of time.
 - Reviewing means of shortening the time period for the assessment of civil penalties.
 - Consider a voluntary self-disclosure policy.
 - Evaluate potential increases in per day civil penalty of \$32,500.
 - Consider development of whistleblower protections.

What Does the Future Hold?

- Key recommendations of the National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling.
 - Update regulations
 - To be at least as rigorous as regulatory peers.
 - Include implementation of the “safety case” approach to regulation.
 - The burden rests on the applicant to determine the different ways something could go wrong, then demonstrate the manner, by work practice or through technology, the applicant will avoid or deal with the problems.
 - Updated at least every 5 years.
 - Separate MMS into three divisions.
 - Industry should create and maintain deployable resources for large events.
 - Develop means for industry to fund environmental science, oil spill research and development, and regulatory oversight.
 - Develop plans for dealing with “spills of national significance.”
 - Dedicate 80% of CWA penalties to the restoration of the Gulf.
 - Significantly increase liability cap and financial responsibility levels.

What Does the Future Hold?

- Any legislation would look more like the prior Congress's Senate bill than the House bill.
- Likely to be part of a larger energy bill.
- Given that DOI has regulatorily addressed much of what the statutes would require regarding safety and well construction, and third party verifications, any such legislation likely would focus more on liability limits, penalties, and enforcement matters and ratify BOEM efforts to date.
 - Compromise under discussion regarding unlimited liability: Raise liability cap to \$250MM, after which an industry-fed insurance fund would apply.

What Does the Future Hold?

- Spill response partnering and resource sharing among operators.
 - Kevin Costner sold/leased BP 32 centrifuges that can separate oil and water while at sea.
 - He proposed the creation of a 200 vessel spill response fleet using his technology: for \$895 million with annual costs of \$100-150 million.
 - Idea presented to BP, Chevron and ExxonMobil.

What Does the Future Hold?



Conclusion/Q&A

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