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A Proposed Agenda for the Presidential Commission

The ***National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling*** has been tasked with investigating the Deepwater Horizon accident and making recommendations on how to prevent and mitigate future spills. Given the large stakes to the marine environment, coastal and national economies, U.S. energy security, and revenues to the federal government, the Commission's recommendations are likely to have consequences that go well beyond an investigation of the accident and implementation of a new regulatory program.

EPRINC recommends the Commission give careful review to the following agenda items:

1. The Deepwater and Offshore Arctic Drilling Moratorium

The costs of the moratorium on deepwater drilling are high, and the likelihood that it is not delivering substantial benefits in lower risk should place this agenda item as the first order of business for the Commission. Priority regulatory reviews to address well control concerns, either reviewing plans on a case-by-case basis, or issuing some interim new regulatory orders, can be done quickly. The Commission's first order of business should be to provide the President with a regulatory strategy and risk assessment that would permit the deepwater rigs to return to work in the next few weeks.

The stakes are also high as to the timing of when new deepwater drilling may return. Many of the more advanced and expensive drilling rigs are under long-term contract; however, the moratorium may lead project operators to declare force majeure on their Gulf rig contracts, freeing themselves of such contracts. The most advanced and safest rigs have the highest day rates and the cost of keeping them idle is high. These rigs will leave the Gulf in the near future if the moratorium is not resolved quickly. Even if the moratorium is eventually resolved, uncertainty on the regulatory path forward could substantially lower future oil and gas production from the Gulf.

The moratorium on offshore Alaska drilling will further delay access to the potential of the Chukchi Sea. This delay in access to the Chukchi Sea could contribute to an accelerated loss in domestic production due to the cost structure of the Trans Alaskan Pipeline System (TAPs). TAPs is experiencing continued declines in throughput and rising costs per barrel shipped. Current throughput is approximately 670,000 bbl/d (barrels per day) and declining at about 6 percent per year. Once production falls to below 300,000 bbl/d costs may accelerate as this volume of crude moving through TAPs will most likely require major

modifications in the transport system. In the absence of new crude supplies, the rising cost structure of TAPs may force early abandonment of North Slope production. This issue should command high priority and be carefully reviewed by the Commission.

2. Regulatory Program

There will be a tendency for the Commission to recommend detailed and new regulatory reviews, including very prescriptive provisions on how offshore operations should be conducted. Longer delays and higher costs for offshore operations are likely. While such an approach is politically appealing, it may not lead to a higher level of safety in offshore operations. Offshore exploration technology is advancing at a rapid pace. Alternative regulatory regimes, such as "safety cases" should be given careful review.[1]

In the end, the cause of the Deepwater Horizon accident likely will be the result of an error in well design or any number of human failures in well control procedures, but the Commission should take care not to fight the last war. Regulatory regimes which reward and re-enforce a strong "Culture of Safety" system are likely to yield better long-term results than a regulatory process that quickly becomes out of date due to technological advances. Given the catastrophic consequences of whatever errors BP made in drilling the Macondo well, these mistakes are not likely to be repeated in the future by offshore operators worldwide.

3. Building Public Trust

The data demonstrates that blowout induced spills are extremely rare. While the Commission should certainly evaluate strategies to drive the risks of oil spills as low as possible, public support for continued offshore operations will require greater confidence that a spill can be mitigated quickly and effectively. Congress is likely to raise the tax on oil production and petroleum imports as provided for in the Oil Pollution Act of 1990. The act provides for a Liability Trust Fund which currently has approximately $1.5 billion on hand and is likely to see large increases as Congress imposes higher taxes on crude production and imports of crude and petroleum products. Some portion of these funds should be allocated to support a sustained research effort on after spill control technologies, including unique strategies to address emergency deep sea operations, as well as more effective organizational protocols for addressing a spill.

[1] A "safety case" system is a structured approach to the operation of facility, such as an offshore drilling rig, which provides a body of evidence that provides a compelling, comprehensible and valid case that a system is safe for a given application in a given operating environment. It is a regulatory program used in some offshore petroleum provinces and can offer a more effective regulatory strategy for keeping current with technological advances than regulatory approaches often used in the U.S. Regulatory strategies for offshore operations are the subject of a forthcoming EPRINC report.

Real time assessments and official comments on the extent of the accident that include repetitive statements that it is the worst environmental disaster in U.S. history or the end of a way of life for Gulf residents are not likely to give the public much useful guidance on the seriousness of the event. There is no doubt that the spill is a major environmental problem and is causing sustained damage to beaches, marshlands, fisheries, and wetlands. But large segments of the Gulf remain clear of damage and marine environments have demonstrated the capacity to recover from such events in the past. The Commission can do the economy and residents of the Gulf an enormous favor by providing the public with some precision on the extent and location of damage and likely recovery periods.

4. Raising the Liability Cap

There is considerable Congressional interest in raising the liability cap to either unlimited levels or somewhere in the range of $10 billion. Raising the cap is viewed as an appropriate incentive to limit "reckless" offshore operations. However, the reputational and direct costs of a major spill, at least from the experience of the Deepwater Horizon, are substantial with or without a higher liability cap. The Commission should evaluate the costs and benefits of liability distribution. Very high liability caps are likely to result in lower competition, reduced demand for offshore leases, lower revenues to the federal government, and lower oil and gas production. The OPA Liability Trust Fund provides a mechanism for providing a form of re-insurance for very high levels of liability.

A Final Comment

The direct revenue consequence to the federal government, contribution to economic growth, employment, and energy security are all benefits from offshore drilling. This benefit stream places the federal government as the petroleum industry's most important partner; getting the correct balance in the distribution of liability and a workable regulatory program is worth careful evaluation.

Finally, the revenue considerations for the government are substantial. From 2005-2009 BP paid a total of $14.8 billion to the federal government in corporate income taxes and an additional $6 billion in production taxes (bonus bids and royalties). Similar payments were made by many other companies producing oil and gas in the U.S. offshore. Finding a path forward to sustain these revenues to the government and at the same time continue safe operations in the Gulf should be a critical piece of the Commission's work. To date, none of the alternative fuels and fuel technologies generate this level of revenue to the federal government – and many require large subsidies that will likely continue for years.