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REMARKS ON REPORT OF PUBLIC LAND LAW REVIEW COMMISSION MINERAL RESOURCES (OIL AND GAS)

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THE study by the Commission and the publication of its *Report*[1] is probably the most significant event affecting the public lands which has occurred in this century. It has long been needed. For the first time a coordinated in-depth study has been made of the law of the public lands and their resources.

In reading the *Report*, it should be remembered that it represents a consensus of 19 Commission members of diverse backgrounds and philosophies, that it was intended to point up strengths and weaknesses in our public land law and its administration, and to indicate the general nature of corrective measures which should be taken. For these reasons, the formal recommendations are, for the most part, somewhat general, and detailed recommendations are relatively few. There are some ambiguities in the *Report,* some problems are given only superficial treatment, and others are not dealt with at all. This may be partially due to the fact that the *Report* is, after all, a consensus and a compromise. But in the final analysis, the Commission has done an excellent job and is to be commended for accomplishing its task. The *Report,* and the 33 studies upon which it is based, now provide a substantial basis for considering revision of public land laws and policies.

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1. PUBLIC LAND LAW REVIEW COMM., ONE THIRD OF THE NATION'S LAND: A REPORT TO THE PRESIDENT AND TO THE CONGRESS (1970). [Hereinafter cited as REPORT].

In general, the Commission approved the basic framework of laws governing oil and gas exploration and production as contained in the Mineral Leasing Act of 1920,[2] the Outer Continental Shelf Lands Act of 1964,[3] and other acts, but concluded that the system can be improved and that modifications should be made.[4]

Chapter Seven deals with onshore mineral resources and consists of 17 pages, of which only 5 pages deal directly with oil and gas.[5] For such an important subject, the treatment is brief and the recommendations are few, but this is consistent with the Commission's general approval of the leasing system.

Chapter Eleven is principally concerned with offshore oil and gas leasing and operations, and consists of 18 pages,[6] which is longer than the oil and gas section of Chapter Seven. This is to be expected because of the relative newness of offshore oil and gas development, and because of attendant environmental problems, increasing interest in marine resources, and concern by some who feel that the Federal Government should, for the first time, exercise its authority with respects to prorationing of production, which has heretofore been successfully regulated by the states. Because no major changes are advocated and because the recommendations are relatively few, a fair conclusion is that the Federal leasing system has worked well for all concerned, and that present laws and administration of oil and gas exploration and development should not be materially changed.

BASIC MINERAL POLICY

To the oil and gas industry, probably the most encouraging parts of the *Report* are the basic mineral policy statements in the recommendations, together with the implementing comments and discussion. One of the most important statements of the *Report* relates to the necessity to develop a sound domestic oil and gas industry because of the close relation between

2. 30 U.S.C. § 181 (1964).
3. 43 U.S.C. §§ 1331-1343 (1964).
4. REPORT, 134.
5. *Id.*, 121.
6. *Id.*, 187.

minerals and national security. This necessity is implicit in the statement that

> [e]xperience in Peru, the Middle East, and elsewhere demonstrates that total reliance on foreign sources would be a hazardous economic and political policy. We strongly favor, therefore, an overriding national policy that encourages and supports the discovery and development of domestic sources of supply.[7]

Evidence of the hazard of relying on foreign sources at the expense of a sound domestic industry is found in recent increases in tanker shipping rates and royalties demanded by foreign governments, as a result of which foreign crude delivered to refineries in the United States now costs approximately 75¢ per barrel more than domestic crude delivered to the same points.

The industry has further grounds for reassurance in the Commission's restatement of the policy that development of mineral resources on the public lands should be developed by private enterprise:

> *The Federal Government generally should rely on the private sector for mineral exploration, development, and production by maintaining a continuing invitation to explore for and develop minerals on the public lands.* We are satisfied that private enterprise his (sic) succeeded well in meeting our national mineral needs, and we see no reason to change this traditional policy. . . . The efforts of private enterprise will be effective only if Federal policy, law, and administrative practices provide a continuing invitation to explore and develop minerals on public lands.[8]

The oil and gas industry is fully aware of, and concerned with, the need for the protection of the environment. It is taking all reasonable measures to adjust its operations to the environment in which it operates, and to minimize their impact upon that environment. It will no doubt endorse many of the basic environmental goals and policies set forth in Chapter Four. Nevertheless, the industry is concerned with

7. *Id.*, 121.
8. *Id.*, 122.

the excessive demands of some groups that large segments of the public lands be set aside exclusively as primitive areas, recreational areas, and other uses. The Commission, while recognizing the utmost importance of preserving these values, at the same time believes that regulations must not be arbitrarily applied to the extent that mineral exploration will be discouraged or effectively prohibited with the resulting impairment of the nation's economic and strategic well-being. The discussion in the *Report* on this point is of particular interest:

> Consequently, we have concluded that it is in the public interest to acknowledge and recognize the importance of mineral exploration and development in public land legislation. Also, a decision to exclude mineral activity from any public land area should never be made casually or without adequate information concerning the mineral potential.
>
> *Mineral exploration and development should have a preference over some or all other uses on much of our public lands.* As a land use, mineral production has several distinctive characteristics. Mineral deposits of economic value are relatively rare and, therefore, there is little opportunity to choose between available sites for mineral production, as there often is in allocating land for other types of use. Also, development of a productive mineral deposit is ordinarily the highest economic use of land.
>
> While mineral exploration activities are conducted over substantial areas of land, experience has demonstrated that mineral production requires less surface area than most other land uses. . . . Therefore, a use preference is warranted by nature's sparse and random distribution of valuable mineral deposits and the vital relationship between our national welfare and assured supplies of minerals. Furthermore, a worthwhile mineral deposit is usually concealed and becomes available to meet our national needs only as the result of an expensive, long-term and high risk search effort.[9]

9. *Id.* (emphasis added).

> Even though we are concerned about various impacts on the environment, and make recommendations in this report for the strengthening of the Federal Government's authority to regulate such impacts, we recognize that mineral exploration, development, and production will, in most cases, have an impact on the environment, or be incompatible with some other uses. By its very nature, mineral activity alters the natural environment to some degree, and if no such impact were to be tolerated, it would be necessary to prohibit the activity. Mineral exploration, development, and production are essential to our national economic and strategic well-being, however, and such activities cannot be barred completely.
>
> Accordingly, our emphasis must be on minimizing impacts. These impacts range from tracks left by exploration vehicles to large production pits. Because of the national requirement for the development of domestic mineral sources, development will frequently have to proceed, subject to reasonable controls designed to lessen the adverse impacts, even though those impacts exist. Stated another way, we believe that the environment must be given consideration, but regulations must not be arbitrarily applied if the national importance of the minerals is properly weighed.[10]

NON-COMPETITIVE LEASING

There has been wide-spread criticism of the present system of non-competitive leasing of Federal lands which became available for leasing through cancellation, termination, or relinquishment of existing leases. This is now done by the simultaneous filing system, which involves public drawing among multiple applicants.[11] The industry was divided on this subject, and its disagreement became polarized between those favoring retention of the present system with modifications to correct existing evils, which admittedly would be hard to do, and those proposing competitive bidding for all Feder-

10. *Id.*, 122-123.

11. 43 C.F.R. Subpart 3123 (1970).

al leases. The Commission took a middle ground in its Recommendation 49[12] that

> [c]ompetitive sale of exploration permits or leases should be held whenever competitive interest can reasonably be expected.

and that

> . . . competitive leasing would be appropriate (1) in the general area of producing wells, (2) for land covered by relinquished or forfeited leases or permits, or (3) where past activity and general knowledge suggest reasonably good prospects for success.

This seems to be a good solution to the problem because it eliminates simultaneous filing, while making it possible to lease the great bulk of Federal lands in which there is no competitive interest, without the administrative burden of going through a competitive sale.

COMPETITIVE BIDDING

The *Report* recommends that greater flexibility should be authorized and practiced in the sale of onshore[13] and offshore[14] leases. Combination bonus, royalty and rental bidding would replace the cash bonus system[15] now in use. While use of a combination of these factors would not in and of itself be undesirable, such a system would be impractical in most instances because of the difficulty in assigning comparative values to the various combination bids submitted so as to identify the winning bid.

Several objections to royalty bidding are apparent. One is that irresponsible bidders tend to be attracted who will bid high royalties to win leases. This can result in early abandonment of wells because of the heavy royalty charge as an operating cost. As a result, such leases would tend to be bought and sold as speculation rather than for bona fide exploration and development.

12. REPORT, 132.
13. *Id.*, 134.
14. *Id.*, 192.
15. 43 C.F.R. Subpart 3124 (1970) (onshore).
43 C.F.R. Subpart 3382 (1970) (offshore).

Another consequence of royalty bidding might be loss of bonus and royalty revenue to the Government. For example, the winning bid might be a high royalty and a comparatively low cash bonus. In the event of a dry hole, the Government would not have received the large cash bonus which might otherwise have been bid and the high royalty would be of no value. If a producing well were drilled, the high royalty, as a part of the cost of operation, would cause premature abandonment of the well, leaving unrecovered oil in the ground. The royalty which would otherwise have been payable to the Government would be lost, and the Government would have realized a relatively small cash bonus.

Continuation of the present system of cash bonus bidding therefore seems to be the best answer for the competitive sale of oil and gas leases.

LEASE PERFORMANCE REQUIREMENTS

The *Report* is critical of the fact that there are no "performance requirements" in Federal oil and gas leases, and that Federal leases may be extended for two years by drilling operations at the end of the primary term.[16] With respect to the latter, the report states that "[s]uch a provision does not adequately protect against mere speculation and certainly does not assure diligent exploration efforts."[17] These objections and the basis for them are not clear. The *Report* does not specify what is meant by "performance requirements," nor does it detail its objections to the 2-year extension. It would appear that the economic burden of lease rentals and other factors are sufficient to prevent undue speculation and encourage reasonable exploration efforts.

ENVIRONMENTAL CONTROLS—

OPERATIONS ON NON-PUBLIC LANDS

One of the most objectionable recommendations of the *Report* is Recommendation 23 which provides:

16. 30 U.S.C. § 226(E) (1964).
17. REPORT, 133.

> Congress should authorize and require the public land agencies to condition the granting of rights or privileges to the public lands or their resources on compliance with applicable environmental control measures governing operations off public lands which are closely related to the right or privilege granted.[18]

This recommendation is based on the premise that the granting of public land rights and privileges should be used as a leverage to force compliance with environmental laws in subsequent operations and facilities located on non-public lands. Federal leases and permits could thus be cancelled in instances where the natural resources produced from the lease are processed in a plant found to be in violation of local, state, or Federal environment law. Also, firms found to be in violation would not be eligible to obtain leases if production therefrom was to be processed in a plant where such violations occur. This would mean that oil and gas leases would be subject to cancellation if the refinery processing the crude were found to be in violation of environmental laws. The objections to this recommendation are obvious. Among them are (1) that it will result in a high degree of insecurity of lease tenure and (2) that other laws and regulations are available to secure compliance with environmental regulations.

PRORATION AND CONSERVATION

Market demand prorationing is discussed briefly in the *Report*.[19] It recognizes existing state prorationing authority and previous court approval of market demand prorationing as serving a legitimate conservation purpose. It also cites recognition by Congress of state prorationing as a conservation system by its consent to the Interstate Oil Compact Commission and passage of the Connally Act,[20] which prohibts interstate transportation of oil produced in excess of allowables fixed by state regulation.[21] On the other hand, the *Report* is somewhat critical of the Department of the Interior for not having previously instituted a system of prorationing of pro-

18. *Id.*, 81.
19. *Id.*, 134, 188.
20. 15 U.S.C. § 715-7151 (1964), *as amended*, (Supp. V, 1970).
21. REPORT, 189.

duction from Outer Continental Shelf oil and gas leases, although the *Report* emphasizes the need for close cooperation between the Federal Government and the adjacent states. However, Assistant Secretary Hollis M. Dole of the Department of the Interior recently stated that present arrangements with the states have worked well in the past and should not be disturbed except for good reason.[22] The principle of market demand prorationing has already received approval of the United States Supreme Court,[23] and there should be no reason why excessive production from Federal leases should be allowed to contribute to or precipitate an over-supply of crude oil with the attendant evils that market demand prorationing is designed to eliminate.

Similar reasoning applies to onshore Federal leases, which are frequently interspersed among fee leases. Although the *Report* recognizes that in the past Federal authorities have allowed state conservation regulations to be applied to operations on public lands, it opposes making Federal lands subject to state conservation authority.[24] So far there has been a relatively harmonious relationship between the states and the Federal Government because the administrators involved have generally agreed on what is or is not good conservation practice. Nevertheless, an oil or gas reservoir cannot be operated without waste, nor can correlative rights be protected, if two different sets of conservation rules are applied. This is always a threat and a possibility so long as Federal lands are not subject to state conservation authority in the same manner as other lands.

OFFSHORE OIL SPILLS

The Commission is justifiably concerned with avoidance of further oil spills. Without question, the oil and gas industry is committed to the same goal. The *Report* refers to "the passage by Congress of an act imposing absolute liability upon the lessee for clean-up of oil spills occasioned by drilling or pro-

22. *Hearing before the Subcommiittee on Antitrust and Monopoly of the Senate Committee on the Judiciary*, Oil & Gas Journal, 42 Aug. 17, 1970.
23. *See* Chaplain Refining Co. v. Corp. Comm'n of Okla., 286 U.S. 210 (1932).
24. REPORT, 134.

duction operations."[25] However, the writer has been unable to find any such act which applies to Outer Continental Shelf operations. Absolute liability does exist under the regulations[26] for cleaning up oil spills, although there may be Constitutional limitations and some question as to the statutory authority of the Secretary to impose such liability.[27] Administrative procedures directed toward preventing further oil spills have already been improved and tightened as recommended in the report.

The Commission favors statutory definition of a lessee's liability, however it is difficult to determine from the discussion in the report whether this recommendation relates to liability for clean-up or liability for damages. If the reference is to clean-up, such liability already exists in the regulations. If the reference is to damages, then the industry would undoubtedly favor liability based on common law negligence. A more stringent basis of liability would in all probability inhibit offshore development.[28]

OIL SHALE

> Recommendation 52[29] deals with oil shale as follows: Some oil shale public lands should be made available now for experimental commercial development by private industry with the cooperation of the Federal Government in some aspects of the development.

Specifically, the *Report* recommends that such a program should:

> (1) offer for lease tracts sufficiently large to permit amortization of investments required for commercial development; (2) give weight to industry nominations relating to location and size of tracts, lease duration, and size of plant; (3) not bar the holder of a test lease from eligibility for leases subsequently issued

25. *Id.*, 191.
26. 30 C.F.R. § 250 43 (b) (1970).
27. Aitken, *The New Outer Continental Shelf Operations and Leasing Regulations and Oil and Gas Lease Form*, 3 NATURAL RESOURCES LAWYER 298 (1970).
28. Connally, *Regulation on Submerged Land*, 21 OIL & GAS INST. (Sw. Legal Fdn.) 34, 45 (Mathew Bender 1970).
29. REPORT, 135.

> under a general leasing program; (4) include experimental use of bonuses, royalties, and rentals; (5) provide fixed terms, conditions, and royalty payments for the term of the lease; and (6) not interfere with process patent rights of lessees acquired prior to issuance of the leases.

The *Report* also recommends that in a test program

> [T]he Federal Government should accept partial responsibility for the costs of minimizing environmental impacts and for carrying out rehabilitation of mined areas.[30]

The above specific requirements have merit and satisfy the principal objections to the 1968 Test Leasing Program which contributed to its failure. It does appear, however, that the Mineral Leasing Act will have to be amended and present patent policy clarified to permit points (3), (4), and (6) above to be carried out.

30. *Id.*, 135-136.