

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

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

**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.

governed by Section 5(f)(1).¹² In other words, FERC has a consultation process to follow when it specifies “open access requirements, under (f)(1), in licenses that it issues within the scope of authority provided elsewhere – most obviously § 7(c) of the [NGA].”¹³ FERC imposed such specific conditions, for example, in Order Nos. 509 and 509-A, when it imposed the open and non-discriminatory condition on pipelines holding certificates under the NGA and operating in the OCS.¹⁴

The Court also noted that the remaining portions of Section 5(f) give FERC limited authority to order expansions of capacity on an OCS pipeline or to exempt from Subsection (f)(1) any facility that first collects, separates, dehydrates or processes gas.¹⁵ The Court concluded that these powers, like the other powers spelled out in Section 5(e) and elsewhere in Section 5(f), did not give FERC general enforcement authority. As the Court stated: “Sections 5(e) and (f) of OCSLA do not grant FERC general powers to create and enforce open access rules on the OCS, but merely assign it a few well-defined tasks.”¹⁶

¹² *Id.*

¹³ *Id.*

¹⁴ See *Interpretation of, and Regulations Under, Section 5 of the Outer Continental Shelf Lands Act Governing Transportation of Natural Gas by Interstate Natural Gas Pipelines on the Outer Continental Shelf*, Order No. 509, F.E.R.C. Stats. & Regs. [Regs. Preambles, 1986-1990] (CCH) ¶ 30,842 at 31,269 (1988); *order on reh’g*, Order No. 509-A, F.E.R.C. Stats. & Regs. [Regs. Preambles, 1986-1990] (CCH) ¶ 30,848 (1989); see also 18 C.F.R. § 284.303; *Tennessee Gas Pipeline Co. v. FERC*, 972 F.2d 376, 381 (D.C. Cir. 1992).

¹⁵ *Williams*, 345 F.3d at 914 (citing 43 U.S.C. §§ 1334(f)(1)(B) and 1334(f)(2), respectively).

¹⁶ *Williams*, 345 F.3d at 916.

2. Sections 5(e) and (f) Expressly Apply to Pipelines Providing Transportation Service and Do Not Encompass Production-Related Activities.

a. The Plain Terms of Sections 5(e) and (f) of OCSLA Demonstrate that the Provisions Apply to Pipeline Transportation but Not to Production-Related Activities.

Under the express terms of OCSLA, the open and non-discriminatory access requirements apply only to “pipeline” facilities providing “transportation” services. MMS should not propose, as FERC did in Order No. 639, to encompass production-related services within the regulatory program. The open and non-discriminatory access requirements do not extend to production facilities on platforms and the production-related services provided by those facilities. Nor does the statute impose the condition on facilities and activities upstream of the platform, such as subsea manifolds and production strings and the activities undertaken in such facilities. Had Congress wanted that broader reach, it would have crafted Sections 5(e) and 5(f) of OCSLA to include platforms and production facilities.

Instead, Congress took pains to draft OCSLA so that the open-access provisions only apply to *transportation by pipelines*, as evidenced by the plain terms of Section 5(e) of OCSLA:

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 upon 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, after a full hearing . . . determine to be reasonable, taking into account, among other things, conservation and the prevention of waste.

43 U.S.C. 1334(e) (emphasis added).

Section 5(f) similarly only includes transportation by pipelines within the scope of services subject to the open and non-discriminatory access requirement:

(1) Except as provided in paragraph (2), 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.

...

(2) The Federal Energy Regulatory Commission may, by order or regulation, exempt from any or all of the requirements of paragraph (1) of this subsection *any pipeline or class of pipelines* which 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.

(3) The Secretary of Energy and the Federal Energy Regulatory Commission 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 paragraph (1) of this subsection. In preparing any such views, the Attorney General shall consult with the Federal Trade Commission.

(4) Nothing in this subsection shall be deemed to limit, abridge, or modify any authority of the United States under any other provision of law with respect to *pipelines* on or across the outer Continental Shelf.

43 U.S.C. 1334(f) (emphasis added). There is no mention of production and production-related facilities and services in any of these provisions.

The legislative history of the 1978 OCSLA amendments further shows that the “open and nondiscriminatory access” provisions apply solely to transportation in pipeline facilities:

[Section 5(f)] is intended to (1) prevent “bottleneck monopolies” and other anticompetitive situations involving OCS pipelines and (2) promote efficiency and sound planning involving pipelines sizing. . . . The agreed-to subsection (f) provides for open and nondiscriminatory access to apply to all pipelines and is a reaffirmation and strengthening of subsection 5(e), which provides for the transport or purchase of all OCS oil and gas “without discrimination.”

H.R. Cong. Rep. No. 95-1474, at 87 (1978), *reprinted in* 1978 U.S.C.C.A.N. 1674, 1686.

The terms “pipeline” and “transportation” are not defined in OCSLA. 43 U.S.C. §§ 1331(k), (l), and (m). But “exploration,” “development,” and “production” are all defined terms, and Congress specifically did not include these activities within the scope of Sections 5(e) and (f). Indeed, Section 1331(m) of OCSLA, which defines “production”, plainly recognizes that Congress did not intend to subsume production activities in Sections 5(e) and (f). The definition states:

“production” means those activities which take place after the successful completion of any means for the removal of minerals, including such removal, field operations, transfer of minerals to shore, operation monitoring, maintenance, and work-over drilling.

43 U.S.C. § 1331(m). In Order No. 639, FERC had argued in Order No. 639 that this definition supported its view that the term “transportation” includes “production” because under the definition the “transfer of minerals to shore” was an activity subsumed by the term “production.”¹⁷ This argument turns the definition of “production” on its head. Even if the term “production” is meant to encompass each of the activities listed within the definition, it does not support FERC’s reading. Under this definition, “transfer of minerals to shore” (which FERC asserted refers to transportation) is distinct from “field operations,” “drilling” and other activities also identified in the definition. Thus, under the definition, transportation is a subset of activities

¹⁷ Order No. 639 at 31,516-17 n.14.

deemed to constitute “production.” Accordingly, the opposite cannot be true, *i.e.*, production is not a subset of transportation.

For these reasons, there is no basis to conclude that the references to pipelines and transportation in Section 5(e) and (f) was intended to encompass production-related facilities or services.

b. OCSLA Makes Clear that Production-Related Activities Are Governed by the Contractual Rights Granted to Lessees under the Terms of Oil and Gas Leases.

The source of producers’ rights to undertake exploration and production activities on the OCS confirms the plain intent of Congress in Sections 5(e) and 5(f) to limit the reach of those Sections to pipeline transportation and to not encompass production and production-related facilities and activities. Under OCSLA, producers undertake exploration and production activities under their contract rights granted under oil and gas leases issued by the MMS. The non-discrimination and open access condition under Sections 5(e) and (f) does not apply to such lease rights.

While Section 5(f)(1)(A) contemplates the imposition of the non-discrimination and open access condition on “every permit, license, easement, right-of-way, or other grant of authority for the transportation by pipeline” of oil or gas on or across the OCS, this language does not include leases under which MMS grants a lessee the right to explore, develop, and produce the oil and gas contained within the leased area. Leases are issued pursuant to Section 8 of OCSLA. *See* 43 U.S.C. § 1337(b)(4). Section 8 of OCSLA does not contain a non-discriminatory and open access requirement or condition. To the contrary, Section 8 contemplates the grant of *exclusive* rights to the winning bidder for lease rights to produce oil and gas from the leased area for the term of the lease. The exclusive contract rights are fundamentally inconsistent with a non-discrimination and open access condition.

In sum, the express terms of OCSLA foreclose the imposition of the non-discrimination and open access condition on production-related activities authorized under leases granted by the Secretary of the Interior.

c. MMS' Current Regulations Properly Reflect the Statutory Scheme.

MMS' regulations carefully reflect the statutory distinction between transportation and production and apply OCSLA's open access regulations only to pipelines used for transportation services. The non-discrimination and open access condition is only imposed on the grant of a pipeline for which a right-of-way must be granted. *See* 30 C.F.R. §§ 250.1001 (definition of "right-of-way pipelines"). Section 250.1010 of MMS' regulations states that the holder of a right-of-way for an "oil or gas pipeline" shall "[p]rovide open and nondiscriminatory access to a right-of-way pipeline to both owner and non-owner shippers. . . ." 30 C.F.R. §§ 250.1010(f)(1) & (2)(i).¹⁸ MMS regulations define "pipelines" as the "piping, risers, and appurtenances installed for the purpose of *transporting* oil, gas, sulfur and produced water." 30 C.F.R. § 250.1001 (emphasis added). The definition of "pipelines" expressly excludes "[p]iping confined to a production platform or structure." *Id.* This definition properly reflects the statutory distinction between production activities and facilities, and those facilities "installed for the purpose of transporting." Indeed, the regulations separately define "production facilities" as including "processing equipment for treating the production or separating it into its various liquid and gaseous components before transporting it to shore." *Id.*

In contrast, a lessee is entitled under the terms of its leases to construct and operate pipelines, platforms and other production-related facilities that are necessary for the full

¹⁸ *See Oil and Gas and Sulphur Operations in the Outer Continental Shelf - Revisions of Requirements Governing Outer Continental Shelf Rights-of-Use and Easement and Pipeline Rights-of-Way*, 68 Fed. Reg. 69,308 (Dec. 12, 2003) (redesignating sections).

enjoyment of the rights to produce and undertake other activities authorized under the lease.¹⁹ The lease does not impose a non-discrimination and open access condition on these facilities and activities. Thus, the regulations do not impose such conditions on “lease term pipelines,” as those pipelines are defined in 30 C.F.R. § 250.1001, or on platforms or other production-related facilities. For example, Sections 250.900 through 250.914 of the MMS regulations describe the requirements for platforms and structures. 30 C.F.R. §§ 250.900 -.914. These regulations, which pertain to construction requirements, do not impose an open access requirement on the platforms and structures. Once again this is consistent with the statutory limitation of the applicability of the non-discrimination and open access condition to pipelines and not to platforms and other production facilities.

Similarly, for lease term pipelines, which are pipelines owned and operated by a lessee and are wholly contained within the lessee’s leases, 30 C.F.R. § 250.1001, the lessee is entitled under the terms of its leases to construct the pipelines and other facilities that are necessary for the full enjoyment of the lease.²⁰ For such pipelines and other facilities (such as platforms), lessees need only acquire a right-of-use and easement pursuant to 30 C.F.R. § 250.160. MMS correctly does not impose a non-discrimination and open access condition on such rights-of-use and easements.

Finally, even where a lessee needs to construct platforms and other production-related facilities on a site off the lessee’s own lease, MMS requires the producer to obtain a “right-of-use” and easement that is not subject to a non-discrimination and open access condition on such rights. *See* 30 C.F.R. § 250.160. Again, the absence of such a condition on rights-of-use

¹⁹ *See, e.g.*, OCS oil and gas lease form (March 1985) at Section 2(c).

²⁰ *See, e.g.* OCS oil and gas lease form (March 1986) at Section 2(c).

and easements for off-lease platforms and other production-related facilities reflects the applicable statutory terms.

In sum, MMS' existing regulations confirm and reflect the statutory distinction between pipelines used for transportation, which are authorized by rights-of-way, and platforms and other production-related facilities. As provided under OCSLA, MMS' regulations only impose the non-discrimination and open access condition on right-of-way pipelines and do not impose such conditions on production-related facilities and activities.

3. Congress Wisely Did Not Subject Exploration and Production Activities to the Open Access and Non-Discrimination Condition.

Failure to respect OCSLA's carefully limited scope of the non-discrimination and open access standard would jeopardize exploration and production of oil and gas in the OCS. Congress wisely excluded production-related facilities and services from the reach of the non-discrimination and open access condition in OCSLA. Such condition makes sense for pipelines providing transportation services, but would inhibit investment in and development of oil and gas leases if extended to the production realm. Producers invest huge sums – as much as \$1.5 billion in a single project – in offshore leases and infrastructure. The willingness to make this investment would be undermined if others could demand access to the facilities after producers/lessees have undertaken this risk and expense by acquiring lease rights through competitive bidding, undertaking exploration activities, and building platforms and associated production facilities.

In sum, Congress wisely recognized that a non-discrimination and open access condition is fundamentally at odds with the property rights held by producers under oil and gas leases granted by the MMS for the exploration, development and production of oil and gas resources located in the OCS. Production activities are undertaken by lessees by reason of their

exclusive rights to produce held under the oil and gas leases. Such rights would be seriously undermined if lessees were required to provide non-discriminatory and open access to the production-related facilities constructed by them for the purpose of developing their leases and producing the oil and gas found on the leases. Congress recognized that producers must invest substantial sums in exploration and development and in the construction of the associated platforms and other production-related infrastructure, and plainly provided that producers' lease rights may not be undermined by bestowing open access rights on others who did not bear the costs and risks of the investments.

Finally, there are significant practical barriers to the imposition of the non-discrimination and open access condition on a producer/lessee's production-related facilities and services. On what basis would the producer/lessee, who bore the risk and investment of the leases and production-related infrastructure, be required to provide production-related services? How would these substantial costs be allocated to individual services and among owner and non-owner customers in order to avoid a claim of discrimination or a denial of reasonable access? Congress wisely left these matters to commercial negotiation between the holders of lease rights and those seeking access to facilities constructed pursuant to such rights.

B. MMS Should Exempt Certain Pipeline Facilities.

Sections 5(e) and (f) of OCSLA impose the non-discrimination and open access requirements on gas pipelines subject to OCSLA in the OCS. However, there are several categories of pipelines that MMS should exempt from its regulatory regime. Further, in the case of feeder lines, MMS should request FERC to exercise its authority to exempt feeder lines from the non-discrimination and open access requirements.

1. **MMS Should Exempt from the Non-Discrimination and Open Access Condition Under OCSLA Pipelines Subject to FERC's NGA Jurisdiction to the Extent FERC Asserts the Authority to Enforce the OCSLA Condition Applicable to Such Pipelines.**

a. **Overview of FERC's NGA Jurisdiction.**

Under the NGA, 15 U.S.C. §§ 717-717w, FERC has jurisdiction over the transportation of gas in interstate commerce. Pipeline companies must apply to FERC for a certificate of public convenience and necessity to construct and operate an interstate pipeline. *Id.* at § 717f. FERC's jurisdiction is limited by the express exemption of production and gathering from FERC's jurisdiction. *Id.* at § 717(b). FERC and the courts have struggled for decades over the scope of the gathering exemption.

FERC has employed the primary function test to distinguish gathering from transportation. Under this multi-factored test, FERC generally looks to both the physical and non-physical characteristics of the pipeline in question. The test has evolved over the years, particularly as it is applied in the offshore. In the latest iteration of the test, as applied to offshore pipelines, the location of processing plants onshore has largely become irrelevant.²¹ By the same token, FERC and the courts have held that pipelines having a length and diameter indicative of a transmission function onshore may constitute gathering offshore, because the gathering lines must be sized to serve locations more distant from transmission lines.²² Further, FERC and the courts have given new significance to the central point of aggregation on an offshore system, that is, the point at which multiple lines converge into a trunkline that extends

²¹ See, e.g., *Williams Gas Processing - Gulf Coast Co. L.P. v. FERC*, 331 F.3d 1011, 1014 (D.C. Cir. 2003); *ExxonMobil Gas Marketing Co. v. FERC*, 297 F.3d 1071, 1077-78 (D.C. Cir. 2002).

²² *Williams*, 331 F.3d at 1014; *ExxonMobil*, 297 F.3d at 1077-78.

onshore. Upstream of this central point, FERC has concluded that pipeline facilities are likely gathering.²³

FERC and the courts have uniformly agreed that FERC's jurisdiction over interstate transportation extends to gathering when the gathering services are provided "in connection with" interstate transportation.²⁴ Specifically, as the Eighth Circuit has found, where an interstate pipeline provides gathering services in the pipeline's own facilities, NGA Sections 4 and 5 empower FERC to regulate the pipeline's rates, terms and conditions for gathering.²⁵

FERC and the courts have also addressed FERC's authority to grant abandonment of an interstate pipeline's gathering facilities by sale to an affiliate (spindown) or to a third party (spin-off). FERC and the courts have held that once abandonment is granted, the Commission no longer has NGA jurisdiction over the abandoned facilities and services. However, as part of its spindown policy, FERC stated that it may reassert jurisdiction over a gathering facility spun down to a gathering affiliate where the pipeline and affiliate act in concert and in a manner that frustrates FERC's effective jurisdiction over the pipeline. FERC in fact reasserted such jurisdiction in the North Padre complaint case, but Williams' appeal of the decision remains pending.²⁶

²³ *Williams*, 331 F.3d at 1021; *ExxonMobil*, 297 F.3d at 1084-85.

²⁴ *See Northern Natural Gas Co. v. FERC*, 929 F.2d 1261 (8th Cir. 1991).

²⁵ *Id.*

²⁶ *Shell Offshore Inc. v. Transcontinental Gas Pipe Line Corp.*, 100 F.E.R.C. (CCH) ¶ 61,254 (2002), *reh'g denied*, 103 F.E.R.C. (CCH) ¶ 61,177 (2003), *appeal pending*, *Williams Gas Processing - Gulf Coast Co., L.P. v. FERC*, No. 03-1179, *et al.* (D.C. Cir.).

b. MMS Should Exempt Gas Pipelines Subject to FERC's Natural Gas Act Jurisdiction.

Not only should MMS be careful to promulgate regulations that do not go beyond OCSLA's clear limitations, it also should be mindful not to adopt regulations that would be duplicative of the regulatory regimes of other federal agencies. Specifically, any new MMS regulations should not encompass (i) NGA certificated pipelines or gathering lines²⁷, or (ii) gathering lines owned by interstate pipelines and operated "in connection with" interstate pipelines, in the event FERC asserts jurisdiction over such pipelines under OCSLA as well as the NGA. If FERC does not assert such jurisdiction under both the NGA and OCSLA, MMS should then encompass such pipelines within its OCSLA program.

Sections 5(e) and 5(f) apply to gas pipelines subject to OCSLA in the OCS, including gas pipelines subject to FERC's NGA jurisdiction. Accordingly, MMS could arguably enforce the open access and non-discrimination provisions of OCSLA even against interstate gas pipelines subject to FERC's NGA regulation. Nevertheless, in order to avoid duplicative and/or conflicting regimes, MMS should exempt from its regulatory program gas pipelines regulated by

²⁷ The term "gathering" is here used to refer to gathering as it is currently understood in the context of NGA regulation. In contrast, MMS defines "gathering" in 30 C.F.R. § 206.51 as:

the movement of lease production to a central accumulation or treatment point on the lease, unit, or communitized area, or to a central accumulation or treatment point off the lease, unit or communitized area as approved by BLM operations personnel for onshore leases.

This MMS definition is found in its royalty regulations and is used to delineate what is deductible transportation for royalty computation purposes; this definition was never intended to relate to the meaning of transportation or gathering in the NGA. In the Notice, MMS recognizes that "gathering" has different meanings with respect to OCS pipelines, depending on whether it is used in the context of MMS royalty valuation regulations, or if it is used with respect to the NGA." Notice at 19,138 n.l.

FERC under the NGA to the extent FERC asserts its jurisdiction under OCSLA as well as the NGA.

Specifically, FERC possesses the authority to enforce the open and non-discriminatory access condition under OCSLA where FERC has imposed the condition in certificates for interstate gas pipelines in the OCS. In *Williams*, the Court held that the Department of the Interior was the agency that held general enforcement authority by reason of its authority to impose the open access and non-discrimination condition under rights-of-way granted under OCSLA.²⁸ But FERC also has the duty to impose this condition under certificates granted to interstate pipelines in the OCS, because Section 5(f)(1) provides that a license or any other grant of authority for a pipeline for transportation through the OCS must require operation of the pipeline in accordance with OCSLA's competitive principles. 43 U.S.C. § 1334(f)(1). The *Williams* Court specifically recognized FERC's obligation to impose this condition in certificates granted under the NGA.²⁹ Thus, *Williams* does not foreclose the position that FERC has the authority to enforce Sections 5(e) and (f) on certificated interstate pipelines.

While MMS also holds such authority by reason of its grant of rights-of-way to such pipelines, MMS should instead defer to FERC to enforce the OCSLA condition imposed on certificated gas pipelines, provided that FERC asserts its authority over such pipelines under OCSLA as well as under the NGA. The policy proposed herein is consistent with sound principles of efficiency. It would be duplicative, and potentially a source of confusion and inconsistent regulation, for MMS and FERC to exercise OCSLA jurisdiction over the same facilities and services. Further, while there are differences in the statutory schemes under

²⁸ *Williams* 345 F.3d at 913-14.

²⁹ *Id.* at 914.

OCSLA and the NGA, both prohibit unlawful discrimination. It is appropriate for FERC to address issues arising under both statutes in order to avoid duplicative litigation burdens on pipelines and shippers and to ensure the consistent application of law and policy.

For these reasons, to the extent FERC affirmatively asserts the right to enforce the OCSLA non-discrimination and open access condition on (i) NGA-certificated pipelines and gathering lines, and (ii) gathering lines owned by interstate pipelines and operated “in connection with” the interstate pipelines, MMS should exempt these pipelines from its own OCSLA regulatory regime.

2. MMS Should Affirmatively Request FERC to Exercise Its Authority to Exempt Feeder Lines.

Under Section 5(f)(2), FERC is authorized to exempt feeder lines from the non-discrimination and open access requirements of OCSLA. 43 U.S.C. § 1334(f)(2). This Section defines feeder lines as “any pipeline or class of pipelines which 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.” *Id.*

Indicated Producers urge MMS to affirmatively request that FERC exercise its authority to exempt feeder lines. In FERC’s Order No. 639, which was vacated on other grounds in *Williams*, FERC exempted feeder lines from its reporting regime under Section 5(e) and (f) of OCSLA. FERC based this decision on the fact that such lines are typically owned and operated by the same entity holding the right to produce from the field served by the feeder line. In such circumstances, FERC concluded that issues of access or discrimination were not likely to arise.

As FERC explained:

Such “feeder line” facilities are typically owned and operated by the same entity that holds the right to produce gas from a particular field; we do not expect issues of access or discrimination to arise

where the same entity owns or leases both the mineral rights and the facilities necessary to draw gas from its own reservoirs.

Order No. 639 at 31,525. Further, FERC expressly stated that the exemption was intended to be as broad as permitted under the statute. As FERC stated, “[w]e view our regulatory exemption as an expansive application of what OCSLA section 1334(f)(2) allows.” Order No. 639-A at 31,684.

Moreover, the feeder line exemption is warranted because feeder lines are typically part of the complex production facilities and operations in the OCS and, accordingly, are subject to the complex contractual relationships among producers holding lease and working interests in production. Because of the relationship of feeder lines with production activities, the imposition of non-discrimination and open access requirements on feeder lines would be disruptive to the contractual relationships and expectations of entities holding the rights to produce oil and gas under applicable leases.

For these reasons, Indicated Producers urge MMS to affirmatively request that FERC again grant an exemption for feeder lines.

3. MMS Should Also Exempt Shipper-Owned and Single-Shipper Pipelines.

In Order No. 639, FERC also exempted from its reporting regime any pipeline in the OCS that carries gas only for the pipeline owner, or where the pipeline only transports for a single shipper. As discussed below, Indicated Producers strongly oppose a reporting regime as unnecessary and overly burdensome. In the event MMS establishes a reporting regime, notwithstanding Indicated Producers’ objections, Indicated Producers urge MMS to adopt these same exemptions.

FERC’s rationale for the shipper-owner and single-shipper exemptions was the same as that underlying the feeder-line exemption: where a pipeline only transports its own gas

or only transports gas for a single shipper, there is no potential for the denial of access or discrimination. Order No. 639 at 31,525. As FERC stated: “where a service provider carries gas only for itself or for a single customer, there is no call to compare conditions of service among multiple shippers.” *Id.* at 31,525.

C. The Meaning of the Open Access and Non-discriminatory Requirements.

Indicated Producers urge MMS not to attempt to devise bright-line tests under the non-discrimination and open access standard. These concepts are inherently difficult to comprehensively articulate in the abstract. Rather, they are best developed in the application of the standards on a case-by-case basis to the facts and circumstances presented in actual cases and controversies. This case-by-case approach has been effectively utilized by FERC (and its predecessor agency, the Federal Power Commission) in applying the undue discrimination standard under the NGA.

1. Discrimination.

While a specific bright-line definition of unlawful discrimination under OCSLA should be left to a case-by-case determination, one fundamental question is appropriately addressed at this time. During the recent public conferences held pursuant to the Notice, the MMS panel members asked commenters whether the discrimination standard under OCSLA should be read differently from the discrimination standard under the NGA. The panel members observed that under OCSLA, unlike the NGA, the discrimination standard was not qualified by the term “undue.” Because of this difference, the panelists were interested to understand if this meant that the standard was stricter under OCSLA than under the NGA.

Section 4(b) of the NGA contains a prohibition against undue discrimination and preference. 15 U.S.C. § 717c(b); *see also* 18 C.F.R. § 284.7(b)(1) (requiring interstate pipelines

to offer services without undue discrimination). Although there is no “per se” rule for when a transaction is unduly discriminatory, FERC has explained that

the general rule is that discrimination is “undue” when there is a difference in rates or service among similarly situated customers that is not justified, whether by differences in the cost of providing the service or by some other legitimate factors.³⁰

Thus, under this standard, a party claiming undue discrimination must demonstrate that the customers are similarly situated.³¹ While the question of whether different parties are similarly situated must be resolved on the facts presented on a case-by-case basis,³² there is no reason why the similarly-situated standard is not equally applicable to the discrimination standard under OCSLA and the undue discrimination standard under the NGA.

There is little basis in precedent or reason to suggest that the discrimination standard under OCSLA should be read as stricter than the undue discrimination standard under the NGA. In 1988, in issuing Order No. 491, FERC initially took the position that the OCSLA standard is stricter than the NGA standard, and concluded that OCSLA required pro rata allocation of capacity, while the NGA does not.³³ But subsequently in Order No. 509, FERC

³⁰ *Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 436, F.E.R.C. Stats. & Regs. [Regs. Preambles, 1982-1985] (CCH) ¶ 30,665 at 31,541 (1985).

³¹ *See, e.g., Tennessee Gas Pipeline Corp. v. FERC*, 860 F.2d 446, 452 n.9 (D.C. Cir. 1988); *City of Vernon, Cal. v. FERC*, 845 F.2d 1042, 1046-47 (D.C. Cir. 1988); *Consolidated Edison Co. of New York, Inc. v. FERC*, 676 F.2d 763, 773 & 773 n.31 (D.C. Cir. 1982).

³² *See, e.g., Koch Gateway Pipeline Co.*, 84 F.E.R.C. (CCH) ¶ 61,143 (1998), *reh'g denied*, 85 F.E.R.C. (CCH) ¶ 61,426 (1998); *Wisconsin Gas Co. v. Viking Gas Transmission Co.*, 105 F.E.R.C. (CCH) ¶ 61,303 (2003).

³³ *Interpretation of Section 5 of the Outer Continental Shelf Lands Act (“OCSLA”)*, Order No. 491, 43 F.E.R.C. (CCH) ¶ 61,006 at 61,031 (1988).

backed away from this view and concluded that the standard in each statute should be read as essentially the same and that pro rata allocation would not be required under OCSLA.³⁴

In *Bonito Pipe Line Co.*, 61 F.E.R.C. (CCH) ¶ 61,050 (1992), *aff'd in part and rev'd in part sub nom. Shell Oil Company v. FERC*, 47 F.3d 1186 (D.C. Cir. 1995), FERC in fact defined the OCSLA standard in the same way as the NGA standard. Specifically, FERC held that Bonito had discriminated against Shell by refusing access to Shell's sour crude oil while permitting existing shippers to ship similar crude oil. FERC concluded that Bonito had discriminated against Shell Oil because it had allowed access to similarly-situated shippers. This is essentially the same standard that FERC applies under the NGA.³⁵ The D.C. Circuit upheld FERC's conclusion.

Similarly, in *Shell Offshore*, FERC concluded that Williams had discriminated against Shell by imposing on Shell a new 8-cent charge for transportation in spun-down gathering facilities, but imposing no additional charge for service in the spun-down facilities on shippers also using Williams' upstream gathering facilities. *Shell Offshore*, 100 F.E.R.C. ¶ 61,254 at PP 55-56, *order on reh'g*, 103 F.E.R.C. ¶ 61,177 at PP 37-38. Concluding that all shippers seeking service in the spun-down facilities are similarly situated, FERC held that Williams' actions amounted to unlawful discrimination under both the NGA and OCSLA. *Id.*

FERC's position in *Bonito* and *Shell Offshore* is reasonable. Under the NGA, FERC has held that discrimination is reasonable and lawful when it is founded on different treatment of shippers that are not similarly situated. Eliminating this concept of reasonableness

³⁴ Order No. 509 at 31,272-73.

³⁵ See, e.g., *Tennessee Gas Pipeline Co. v. FERC*, 860 F.2d 446, 452 n.9 (D.C. Cir. 1988).

would lead to patently absurd and unfair results where pipelines would be required to treat all shippers alike even when they are *not* similarly situated.

2. Open Access.

As in the case of discrimination, the meaning of “open access” is best left to development on a case-by-case basis. Nevertheless, MMS should make clear that the standard is not narrowly designed to prohibit only an overt denial of physical access. As in the case of discrimination, a notion of reasonableness should be implied. On this basis, pipelines should be prohibited from conditioning access on the potential shipper’s agreement to unreasonable rates, terms, and conditions of service. It remains for MMS to determine on a case-by-case basis what rates, terms, and conditions, when demanded by a pipeline, constitute an unreasonable denial of access.

FERC’s decisions reflect this concept of reasonableness. FERC has concluded that gas pipelines in the OCS can give priority to shippers entering into firm contracts.³⁶ FERC reached the same conclusion for oil pipelines in the OCS.³⁷ FERC found that respect for firm contracts was important to support reliance interests necessary for the orderly development of the OCS, concluding that upholding pre-existing contract rights was a reasonable basis to deny access to a shipper. Accordingly, like FERC’s interpretation of discrimination, FERC’s interpretation of open access under OCSLA implies a standard of reasonableness. MMS should adopt this same standard and establish that, while pipelines are lawfully permitted to deny access on reasonable grounds, pipelines may not deny access unreasonably or demand unreasonable rates, terms, and conditions as a condition to access.

³⁶ Order No. 509 at 31,272-74.

³⁷ *Caesar Oil Pipeline Co., LLC*, 102 F.E.R.C. (CCH) ¶ 61,339 at PP 34-38 (2003); *Proteus Oil Pipeline Co.*, 102 F.E.R.C. (CCH) ¶ 61,333 at PP 32-36 (2003).

3. Remedies.

The matter of remedies is inextricably intertwined with the meaning of the non-discrimination and open access standard, since the meaning of the standard itself largely defines the remedies MMS could impose. Nonetheless, it is appropriate for MMS to note in the rulemaking the provisions of OCSLA that specifically address remedies that are available to MMS to enforce Sections 5(e) and (f) of OCSLA.

Section 5(e) of OCSLA provides that failure to comply with the Section and the non-discrimination conditions stated therein shall be grounds for forfeiture of the grant (such as a right-of-way or certificate) under which the condition was imposed. But this remedy can be granted only via a judicial enforcement proceeding in federal court. *See* 43 U.S.C. §§ 1334(e), 1349, & 1350.

Judicial actions to enforce OCSLA requirements can be brought by private citizens under 43 U.S.C. § 1349 and by the Attorney General under 43 U.S.C. § 1350. Both sections are broadly worded in authorizing suits to compel compliance. Under Section 1349(a)(5), temporary restraining orders, injunctions, and reimbursements for the costs of litigation (including attorneys' fees and expert witness fees) are expressly contemplated. Further, Section 1349(b)(2) provides that any party injured by a violation of any agency regulation, order or permit under OCSLA can seek damages, including attorneys' fees and expert witness fees.

Section 1350(a), in turn, also broadly authorizes the Attorney General to seek an injunction, temporary restraining order, "or other appropriate relief" to enforce the terms of OCSLA, or any order, permit or regulation issued thereunder. Section 1350(b) also authorizes the Secretary of the Interior to impose civil penalties of up to \$10,000 per day for failure to correct (after prior notice) any violation of the OCSLA or of orders, regulations or permits issued

thereunder. And Section 1350(c) provides for criminal penalties of up to \$100,000, or up to ten years in prison, for knowing and willful violations of OCSLA or any permit, order or regulation issued thereunder. Section 1350(d) extends that criminal liability to corporate officers and agents.

D. MMS Should Adopt A Combination Hotline And Complaint System In Lieu Of A Reporting Regime.

An overarching question in MMS' Notice is how MMS should exercise its authority to enforce non-discrimination and open access requirements. Foremost, MMS should not follow FERC's example in Order No. 639 by imposing a reporting regime. In its Notice, MMS suggests a hotline mechanism, but also recognizes that a more rigorous dispute resolution process might also be necessary. Notice at 19,139. As further detailed and explained below, the Indicated Producers agree that both a hotline and a formal complaint procedure should be established to enable MMS to carry out its enforcement duties under OCSLA.

The dual mechanism should provide for procedures that would allow the discovery of the information and data necessary to develop a record on which MMS can resolve the dispute on a reasoned basis. Specifically, the formal complaint process should provide for full discovery rights (including the rights to take depositions and other traditional discovery tools), a hearing on the record before an Administrative law Judge with the right to present witnesses and the right 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.

Finally, under the contemplated procedures, it is likely that confidential and commercially sensitive information may need to be given to MMS and opposing parties. MMS'

procedures should provide parties an opportunity to seek confidential treatment of this information.

1. In Developing its Enforcement Mechanisms under OCSLA, MMS Should Not Establish a Periodic Reporting Regime.

In developing regulations to enable it to carry out its enforcement obligations under OCSLA, MMS should avoid adopting any sort of reporting regime, such as the one FERC attempted to establish in Order No. 639. As a threshold matter, OCSLA does not authorize MMS to adopt a reporting regime to enforce the open and non-discriminatory access provision. Even if MMS could promulgate such reporting regulations, it should not do so. The burden of a periodic reporting regime far outweighs the benefits of such a program. A complaint-based approach better balances the needs of shippers seeking access to OCS pipelines and the costs and burdens of the enforcement program on MMS and industry participants.

a. MMS Lacks the Statutory Authority to Establish a Reporting Regime.

In *Chevron* (the district court opinion rejecting Order No. 639), the Court carefully analyzed Sections 5(e) and 5(f) of OCSLA and found that these provisions did not authorize FERC to promulgate regulations establishing a periodic reporting regime. *Chevron*, 193 F. Supp. 2d at 70-71, *aff'd on other grounds*, *Williams*, 345 F.3d 910. Similarly, OCSLA does not grant such reporting power to MMS to enforce the open and non-discriminatory access standards. Nowhere do Sections 5(e) or 5(f) authorize MMS to implement a reporting regime related to the open and non-discriminatory access conditions. Section 5(e) contemplates the imposition of a non-discrimination condition on pipelines providing transportation that are subject to OCSLA, and Section 5(f) requires that transportation by pipelines on the OCS subject to OCSLA be provided in accordance with competitive principles (*i.e.*, the open and non-

discriminatory access standard). Neither Section empowers MMS to promulgate regulations imposing reporting requirements.³⁸

b. Even If MMS Possesses the Requisite Statutory Authority, the Agency Should Not Establish a Reporting Regime.

Even if MMS had the statutory authority to implement a reporting regime, it should not do so. A reporting regime would be highly burdensome on both industry and MMS. This heavy burden is not warranted.

The burden of a reporting regime would be particularly burdensome in the event MMS encompassed production-related facilities and activities within the program. As noted previously, there is no basis in statute or policy to support the imposition of the non-discrimination and open access condition on production-related facilities and activities. If MMS nevertheless attempts to impose the condition on production-related facilities and activities, it should not impose a reporting regime on such facilities and activities.

Reporting would be burdensome if imposed on production-related facilities and activities because of the complex and ever-changing configuration of production facilities and arrangements, and the multitude of functions they perform. Specifically, offshore production facilities perform a range of complex functions and activities, including extraction, collection, separation, dehydration, and treatment. Production can be accomplished through a variety of techniques, including directional drilling, horizontal drilling, subsea completion, and enhanced recovery operations such as gas reinjection. Downstream of extraction and collection, oil and

³⁸ While OCSLA does contemplate reporting or data collection in certain instances, those instances are limited. For example, the Secretary of Interior may obtain data and information from public sources, or purchase such information from private sources, to assist in the preparation of an environmental impact statement and in making other evaluations under OCSLA. 43 U.S.C. § 1344(g). Importantly, this provision mandates no reporting by private entities.

gas production are generally separated and treated to meet individual pipeline quality specifications. By-products (such as free water and other contaminants) are removed from the hydrocarbon streams and, in accordance with MMS regulations, either re-injected into subsea formations or otherwise disposed of. Multiple platforms may be connected, with gas being transferred back and forth between platforms to facilitate the economically optimal provision of the various treatments. Sometimes such facilities are wholly owned by one company, but in many cases joint ventures and facility sharing arrangements are negotiated among producers holding interests in the production in order to enhance efficiency and to share risks. Additionally, multiple other agreements exist in the production arena, including leasing arrangements, geophysical agreements, exploration agreements, joint development agreements, drilling agreements, operating service agreements, and production-handling agreements.

These contractual relationships, as well as ownership interests and operating responsibilities, are constantly changing. Similarly, the configuration and use of production-related facilities are in constant flux as production volumes and reservoir characteristics change. For example, production facilities and platforms are integrated with feeder lines, such that points at which oil and gas are “first collected” or “first separated, dehydrated, or otherwise processed” vary and change over time.

Periodic reports on these complex facilities and services by the various operators and/or interest holders – for each production platform or complex in the GOM – would be a massive undertaking for the reporting entities, as well as for the MMS in collecting and processing the information. These burdens are magnified by the constant changes to the physical configurations of facilities, the services provided, the rates of production, commodity prices, ownership interests, and operating responsibilities.

The burdens attendant with a reporting regime encompassing production-related facilities and services cannot be justified. The production industry in the OCS is highly competitive. For over fifty years, production activities in the GOM have been effectively pursued in a competitive environment, governed by the terms of oil and gas leases with MMS and the commercial agreements among producers holding lease and working interests. There is simply no need for regulatory intervention, particularly via a burdensome reporting regime, in this competitive environment.

2. MMS Should Adopt an Informal Hotline Mechanism to Enhance its Complaint Process.

Indicated Producers support the creation of an informal hotline mechanism, in order to provide entities perceiving a violation of OCSLA with an opportunity to seek the assistance of MMS personnel to resolve disputes relating to discrimination or a denial of access to pipelines in the OCS.

MMS should consider modeling any hotline mechanism it adopts on FERC's Enforcement Hotline. As FERC explains on its website, "[M]arket participants and the general public [can] informally call, email or write the Hotline to complain or report market activities or transactions that may be an abuse of market power, an abuse of an affiliate relationship, a tariff violation, or another possible violation by a FERC regulated entity."³⁹ Generally, an aggrieved party will call the Hotline, Hotline Staff will listen to and assess the problem, Staff will then call the alleged violators, and, in the course of these communications, attempt to resolve the dispute. FERC's website indicates that its Hotline has been used to informally resolve disputes in matters within FERC's jurisdiction without litigation or other formal, lengthy proceedings.

³⁹ Available at <http://www.ferc.gov/cust-protect/enforce-hot.asp>.

An MMS hotline mechanism would carry with it several benefits, including the expeditious resolution of issues without costly proceedings. Such a mechanism would also avoid imposing unnecessary burdens on agency and industry participants; that is, as discussed below, more formal, procedure-intensive courses of action – complete with discovery and hearing with the right to present and cross-examine witnesses – could be reserved for the more complex or contentious cases.

3. A Carefully Structured Complaint Process Would Effectively Ensure Open and Non-discriminatory Access.

For issues that cannot be resolved through an MMS hotline process, MMS should put in place a formal complaint mechanism. With a more formal complaint process in place as a back-up, MMS and industry participants would have the ease and convenience of informal resolution, but the availability of a more formal process for more contentious or complex cases.

The creation of a hotline mechanism does not obviate the need for a formal complaint mechanism. Pipelines would have no incentive to agree to an informal resolution to disputes in the hotline procedure unless they were confronted with the potential that, if the hotline procedure failed to resolve a dispute, aggrieved parties had the option to file a formal complaint.

Each complaint proceeding should be tailored to fit the particular circumstances of the case. That is, the structure should depend on the complexity and the nature of the alleged abuse. For example, a quicker mechanism (*e.g.*, “fast-track processing”) could be an option for parties who, because of the urgency of the issues or for other reasons, need prompt resolution of the issues at hand. In all cases, however, parties should have the right to discovery (including the right to take depositions, to pose interrogatories, and to utilize other traditional tools of discovery), a hearing on the record before an Administrative Law Judge with an opportunity to

present witnesses and to cross-examine adverse 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.

MMS should carefully consider modeling its complaint process on FERC's complaint process, outlined at 18 C.F.R. § 385.206 (with applicable procedures elsewhere in FERC's Rules of Practice and Procedures). Revamped in 1999,⁴⁰ FERC's complaint procedures include "Fast Track procedures," which contemplate expedited action on pleadings by FERC, expedited hearings before an Administrative Law Judge ("ALJ"), or expedited action on requests for stay, extensions of time or other relief.⁴¹ If a hearing is set, FERC's extensive hearing rights and procedures apply,⁴² including discovery procedures (*e.g.*, depositions, data requests, interrogatories and request for production). Indicated Producers encourage MMS to devise a complaint process at least as thorough and balanced as FERC's.

4. In Establishing a Hotline and Complaint Mechanism, MMS Should Adopt Procedures Designed to Protect Confidential Information.

To the extent confidential information is produced during a hotline inquiry or complaint proceeding, MMS should have in place procedures under which parties can seek confidential treatment for material they believe should be protected, much as parties do before FERC. See 18 C.F.R. § 388.112. Section 18(g) of OCSLA, 43 U.S.C. § 1344(g), contemplates

⁴⁰ *Complaint Procedures*, Order No. 602, F.E.R.C. Stats. & Regs. [Regs. Preambles, 1996-2000] (CCH) ¶ 31,071 (1999); *order on reh'g and granting clarification*, Order No. 602-A, F.E.R.C. Stats. & Regs. [Regs. Preambles, 1996-2000] (CCH) ¶ 31,076 (1999); *order on reh'g*, Order No. 602-B, F.E.R.C. Stats. & Regs. [Regs. Preambles, 1996-2000] (CCH) ¶ 31,083 (1999).

⁴¹ Order No. 602-B at 30,972; *see also* 18 C.F.R. § 385.206(h).

⁴² 18 C.F.R. Part 385 Subpart E.

that the Department of the Interior will maintain the confidentiality of information when it obtains privileged or proprietary data.

Materials could be filed under seal, after which MMS would provide notice that a filing was been made. MMS would then assess the claim of confidentiality. If the claim is upheld, the documents would not be available to the public. However, if the claim of confidentiality were denied, then MMS should first give notice to the party claiming confidentiality before disclosing the materials (*e.g.*, at least five days before disclosure; *see* 18 C.F.R. § 388.112(e)) in order to give the party claiming confidentiality an opportunity to appeal. As with issues regarding access and discrimination problems in general, any bright-line test pertaining to confidentiality would likely be unworkable. Accordingly, determinations of confidentiality should be done on a case-by-case basis.

FERC has in place procedures to handle FOIA requests, which procedures include provisions designed to keep under seal materials protected by FOIA exemptions. 18 C.F.R. § 388.108.⁴³ When drafting any regulations that contemplate the filing of confidential or privileged materials, MMS should include provisions insulating such materials from disclosure under FOIA where the materials fall within the exemptions from public disclosure provided under FOIA. *See* 18 C.F.R. § 388.107 (FERC regulations identifying categories of records exempt from disclosure, including privileged or confidential trade secrets and commercial or financial information).

Further, FERC routinely issues protective orders in proceedings where parties provide sensitive documents during the course of discovery and has developed a Model

⁴³ Note that Exemption 4 under the FOIA protects “trade secrets and commercial or financial information obtained from a person [that is] privileged or confidential.” 5 U.S.C. § 552b(4).

Protective Order for that purpose.⁴⁴ When it establishes its regulations to address requests by parties for privileged treatment of documents, MMS should also devise a model protective order, similar to FERC's.

If MMS ensures that provisions are in place to address sensitive information in the event informal or formal disputes arise, then industry participants – being assured that their valuable information is protected – will be more responsive in their dealings with MMS throughout the resolution process. The end result will mean that MMS is better equipped to make determinations regarding whether the open and non-discriminatory access provisions of OCSLA have been violated.

As noted above, MMS has no statutory authority to impose the non-discrimination and open access condition on production-related facilities and services. There are sound policy reasons underlying Congress' express directive that the condition applies only to pipelines providing transportation services. If MMS were nevertheless to attempt to apply its non-discrimination and open access requirements to production-related facilities and activities, the need for strong protections for confidential and proprietary information would be particularly urgent. Production-related data is competitively sensitive. Information from which producer competitors could derive, directly or indirectly, information regarding the location, quality, and volumes of oil and gas reservoirs is highly proprietary. If such information were available to producer competitors, they would be able to bypass or avoid the expenditures associated with exploration and design activities, use the information in developing bids for adjacent or nearby leases, and otherwise use the information in such a way as to deprive the producers who developed the information of the value of their investments.

⁴⁴ *Available at* <http://www.ferc.gov/legal/admin-lit/model-protective-order.pdf>.

Accordingly, MMS must devise regulations that protect confidential and proprietary information from public disclosure.

E. Any Definitions Adopted By MMS Should Preserve OCSLA's Limited Reach.

Any definitions MMS adopts for the terms listed in the Notice should be drafted to ensure that the non-discriminatory and open access standard applies only to transportation by pipelines, as clearly envisioned by Sections 5(e) and 5(f) of OCSLA. The Indicated Producers suggest the following with respect to the terms MMS listed in the Notice:

- “*Non-discriminatory access*” and “*open access*” – the definitions of these terms should generally be left to case-by-case application.
- “*Pipelines subject to OCSLA*” – MMS’ definition for such pipelines should only encompass pipeline facilities on the OCS over which MMS has OCSLA jurisdiction and that provide a transportation function. The definition should exclude piping that is production-related (much as MMS’ current regulations define “pipelines,” at 30 C.F.R. § 250.1001, to exclude “[p]iping confined to a production platform or structure”). The definition should exclude production-related facilities including platforms and upstream facilities such as subsea connections and production strings, as well as lines used as part of the production function rather than for the purpose of transporting oil and gas to shore.
- “*Service provider*” – The definition of service provider should not include producers or providers of services in production-related facilities.

F. MMS Should Not Amend Its Regulations In Any Manner Affecting The Amount Of Royalties That Are Due Under Oil And Gas Leases.

MMS should not utilize this rulemaking to amend its regulations in any way that affects royalty valuation. Sections 5(e) and (f) of OCSLA pertain to the obligation of pipelines

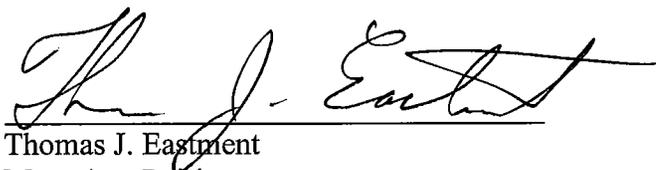
to provide access on a non-discriminatory and open access basis. Nothing in these statutory provisions expressly or implicitly implicate MMS' authority to establish royalty value. Such royalty authority is governed by Section 8 of OCSLA. 43 U.S.C. § 1337(a).

MMS regulations authorize royalty payors to deduct the cost of transportation off the lease. *See* 30 C.F.R. § 206.156(a). Non-deductible costs include the cost of gathering, as defined by MMS in 30 C.F.R. § 206.151, on the lease. The imposition of MMS' authority under Sections 5(e) and (f) does not give rise to the need to amend any of the provisions pertaining to royalty value and transportation deductions.

CONCLUSION

WHEREFORE, Indicated Producers comments on the Minerals Management Service's Advance Notice of Proposed Rulemaking, as set forth above.

Respectfully submitted,



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Dated: June 14, 2004