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RULES PROCESSING TEAM

OCT 16 2000

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Department of the Interior
Minerals Management Service
Mail Stop 4024
381 Eldon Street
Herndon, Virginia 20170-4814

Attention: Rules Processing Team

RE: Minerals Management Service Proposed Rule, Outer Continental Shelf Oil and Gas Leasing. 65 **FR** 55476-55489, September 14, 2000.

Dear Sir or Madame:

BP, and its affliated companies, appreciate and welcome the opportunity to comment on the subject proposed rule for royalty suspensions for leases issued after November 2000. The deepwater Gulf of Mexico offers a tremendous opportunity for the discovery and production of new world class natural gas and oil fields. However, deepwater exploration and development opportunities include a combination of difficult geology, requiring leading edge technology, and very large investments creating unusually high investment risk. Because of these conditions, the economic viability of many of these projects is often in doubt. We believe that the contiuation of royalty suspensions will help industry explore and produce in this uncertain economic environment.

After working through the issues surrounding the current application of royalty relief for the last five (5) years, we believe that the MMS must strive to make this rulemaking for royalty suspensions fair, consistent, simple and concise – the former process remains too cumbersome and complicated. We believe that this rule should be administered following these five (5) fundamental principles:

- Implement the original intent of the law which was designed to make uneconomic deepwater projects economic.
- Refrain from changing the current commercial terms and conditions (e.g. minimum bid, rental rate, royalty rate, term, etc.) for future OCS leases in exchange for royalty suspensions.
- Do not make assumptions for the future based on limited information, i.e., field size, production systems, prices, etc.
- Industry needs certainty, reasonable terms and predictability with as much lead time as practical.
- Industry needs a reasonable and simple administrative process for both pre-enactment leases and eligible leases.

These principles form the basis of our responses to the questions set forth in the proposed rulemaking. Those responses are attached hereto and made a part hereof as Addendum "A".

We appreciate being afforded the opportunity to provide input on this proposed rulemaking. We encourage the MMS to examine other incentives and opportunities in addition to Deepwater Royalty Relief to foster additional exploration and production from the deepwater Gulf of Mexico.

Very truly yours,

Leon Hirsch

Leon Hirsch

enclosure

BP appreciates the opportunity to provide comments on the above referenced Minerals Management Service proposed regulation. Our comments to specific questions asked in the MMS proposed rule follow.

- What factors should we consider, and how should we evaluate these factors, when we choose water depths beyond which bidders still need leasing incentives in the GOM?

Water depth (>1600m) should be the sole criteria because those water depths are still recognized to be "frontier" due to:

- **Limited well control**
- **Limited infrastructure**
- **Limited technological capability (rigs, development systems, transportation, etc.)**

- What elements besides water depth should we consider, and how should we consider them, when deciding how much royalty suspension to offer on new leases?

Several elements impact the risks associated with deepwater exploration & production. However, water depth embodies nearly all of those associated risks. In order to simplify the application of royalty suspensions, MMS should utilize water depth as the sole criteria for relief.

- Which of the following leasing policies would encourage more domestic investment, given equal expected rates of return, and why would it do so? One offering a: (a) Substantial royalty suspension volume coupled with higher than normal royalty rates (*e.g.*, 20 percent) for additional production between specified cumulative production volumes; or (b) Modest royalty suspension volume but with only normal lease royalty rates for production above the royalty suspension volume?

We believe that there should be a "c" alternative – Substantial royalty suspension volumes with current lease royalty rates. The Royalty Relief program should be an incentive based program that encourages development of fields that otherwise would not be developed. There should not be a trade-off of fiscal terms for royalty relief.

- Does the likely increase in bid levels and shift of uncertainty from government to industry that are associated with royalty suspension adversely affect small companies relative to large companies?

Royalty Relief should be an incentive based program that encourages both large and small companies operating in the deepwater Gulf of Mexico to develop fields that would otherwise not be developed.

- Do you agree with our observation that a lease-based royalty relief program, providing a guaranteed royalty suspension volume to each lease regardless of which field it overlies, is preferable to a field-based royalty relief program, providing a royalty suspension volume to be claimed by the earliest producers on a field?

A lease-based approach would be preferable if it accounts for adjustments caused by the inclusion of a lease in a field/unit. Moreover, a lease-based royalty suspension program should (1) define "field/unit" and (2) address royalty suspension volumes for eligible leases and pre-enactment leases in a "field/unit."

- Do you share our expectation that royalty suspension volumes tailored to a typical tie-back development will promote bidding and exploration in the deep water areas that will be available in the next several years?

MMS should utilize royalty suspensions to encourage all types of deepwater developments.

- Is it reasonable to assume between 2 and 3 leases per field will be developed as a tie-back?

Each field is unique and the MMS should not make any assumptions as to field size.

- What benefits would occur for bidders and lessees if we modified the volume suspensions offered on new leases every 3 years as opposed to more frequently?

In order to pursue exploration and production development industry needs certainty and continuity as to the fiscal terms and conditions of OCS leases.

- What effect, if any, would rental obligations during periods of royalty-free production have on the way firms plan and manage a project?

As noted above, we would encourage the MMS not to create any disincentives by changing current fiscal terms and conditions.

- Do you agree with our observation that, given current costs, technology and development options in deep water and the dynamic nature of these factors, the program would benefit from periodic adjustments at the time of lease sales in price thresholds for new leases?

No, economic terms should be constant in order to foster predictability and thus allow industry to make long-term investment decisions.

- Do you believe that adjustments in royalty obligations, other than retroactively for the previous calendar year are desirable? If so, why and what is the nature of the preferred adjustments?

No. Certainty is always preferred.

- Do you agree with our preliminary findings that the applicable price thresholds should be 10 to 15 percent below the levels currently applicable under the Act, *e.g.*, $28 rather than $31 per barrel for oil, and $3.45 rather than $3.90 per million British thermal units?

There should be no commodity price thresholds since a producing field is subject to price fluctuations over the course of its life. Those willing to take the substantial risks associated with deepwater exploration and development should not be additionally burdened with the risk of losing royalty suspension incentives because of commodity price cycles.

- Does the proposed requirement that a lessee with eligible leases issued with a royalty suspension volume notify the MMS Regional Supervisor for Production and Development before starting production impose any meaningful burden on lessees?

No, but we question whether it is truly needed.