

October 19, 2007

The Honorable Harry Reid
Majority Leader
U.S. Senate
Washington, DC 20510

The Honorable Nancy Pelosi
Speaker
U.S. House of Representatives
Washington, DC 20515

Dear Madame Speaker and Mr. Majority Leader:

Our organizations collectively represent the producers, transporters and consumers of natural gas in the United States. Natural gas must be recognized as an indispensable part of the solution to both the energy policy and climate change challenges faced by our country. Most experts agree that the United States will depend heavily upon natural gas in the coming decades, at least, as a “bridge” towards reducing emissions and maintaining energy reliability while other energy technologies are developed and deployed.

That is why our groups have focused on American natural gas supply and infrastructure development. We must ensure that natural gas supplies are adequate to meet growing demand, particularly as Congress moves forward to address climate change. With this in mind, our groups want to register our opposition to H.R. 3221, the House energy bill. The House legislation professes to focus on energy independence; yet, if enacted, the bill would adversely affect American natural gas production and infrastructure development thereby making the supply of this important energy resource even less secure. In fact, 85 percent of natural gas consumed in the U.S. is produced here, making it an undeniably key U.S. energy resource.

The recently announced “Greening of the Capitol” initiative is an instructive example of the challenge facing our nation over the next several decades. As you know, one of the primary recommendations of the initiative was to convert the Capitol Power Plant to natural gas, in order to reduce greenhouse gas emissions significantly while maintaining the operational reliability of the facility. Dozens of electric generators across the United States face the same choice. Natural gas is the most immediate, most reliable option available for reducing power plant emissions, especially as we await the development and commercial deployment of other clean energy technologies. Therefore, it is critical that Congress avoid policies that would reduce natural gas supply availability when those supplies are needed the most to meet our nation’s environmental goals. This particular irony can be seen in Congress’ prior efforts to compensate for declining production from offshore fields, through passage of the Energy Policy Act of 2005. The Act established incentives to spur production in frontier areas, including ultra deep water, ultra deep gas, and offshore Alaska. Repealing these provisions, which is included in H.R. 3221, would inhibit domestic energy production, and be contrary to our country’s energy policy and natural interest

The House energy bill, unfortunately, goes in the wrong direction on natural gas supply. Title VII of H.R. 3221 contains a number of troubling provisions:

Section 7101:

- Repeals or modifies sections of the Energy Policy Act of 2005 that improved the leasing and permitting processes in the Intermountain West. The bill also adds new provisions designed to delay or effectively prohibit access to these federal resources.

Section 7102:

- Extends the deadline for processing applications for permits to drill (APD) established in the EPA Act 2005 from 30 days to 45 days.

Section 7104:

- Frustrates achieving the goals of energy policies adopted in the Energy Policy Act of 2005 by cutting direct funding for permitting Pilot Offices, putting categorical exclusions for limited activities under the management of Council on Environmental Quality rather than the Bureau of Land Management (BLM) land managers and repealing Section 344 and 345 of the Energy Policy

Act that provide for royalty incentives for deep gas production in the shallow water Gulf of Mexico.

Section 7105

- This section would require BLM to amend its Best Management Practice Program, and require public notice and comment prior to any waiver of a lease stipulation in a program that has historically been voluntary. BLM's use of Best Management Practices is addressed by existing guidance documents and is effectively managed at the local district field office and state levels. A waiver of a lease stipulation—the apparent concern of this section—is rarely granted by BLM. This provision would only serve to unnecessarily delay implementation of a decision by BLM.

Section 7106:

- Would modify the appellate process for state consistency determinations under the Coastal Zone Management Act (CZMA) in an unnecessary and potentially confusing way. The current CZMA appeals process encourages intergovernmental cooperation in reviewing major natural gas infrastructure projects; there is no demonstrated reason to alter the process only two years after its enactment.

Section 7201

- Requires increased audits of oil and gas leases in place of compliance reviews. MMS already has a sufficient audit and compliance review program. In fiscal year 2006, MMS completed audits and compliance reviews on 72.5 percent of revenues. MMS data shows that compliance reviews have been a more effective means for returning revenues to the federal government than audits. For every \$1 spent on compliance reviews, MMS has collected \$3.27; however, for every \$1 spent on audits, \$2.06 was collected.

Section 7202

- This section is unnecessary because the existing civil penalties provision contains strong penalties that can be assessed against lessees for failing to comply with leasing laws and regulations, for failing to take corrective action, for failure to make royalty payment, and for knowing and willful violations such as false information. There is no justification for changing the civil penalties code. This new section is adverse because it is unnecessary, confusing and provides an unreasonable penalty for failing to correctly and timely report certain information. This new penalty scheme is ripe for abuse.

Sections 7211 – 7215

- These sections make unnecessary changes in the federal royalty management program. The existing program is effective. For example, these changes would eliminate interest payments from the government when lessees make overpayments, while government retains the right to collect interest on underpayments.

Section 7221:

- Preempts ongoing efforts by individual states to address the post-lease surface agreement (split estate) issue basin-by-basin, opting instead for an unwieldy “cookie cutter” approach to local issues.

Section 7222:

- Adds extensive and specific new reclamation requirements to the Mineral Leasing Act that will result in protracted delays as these requirements are litigated by anti-development interests. Adds a new reclamation bonding requirement that will impose additional costs on natural gas development without any record that such bonds are necessary.

Section 7223:

- Adds new federal water management requirements to the Mineral Leasing Act on top of existing state water management requirements. Requires an APD submitted pursuant to a lease to be accompanied by a new federal *proposed water management plan*.

Section 7224:

- Establishes an annual fee, charged per acre of non-production Federal land that is leased for production of oil, natural gas, or coal.

Section 7502

- This section requires DOI to agree to a request by a lessee to amend a Gulf of Mexico lease to include limitations based on price.

Section 7503

- Clarification of authority to impose price thresholds for certain lease sales. This is a legal maneuver by Congress, in which Congress is attempting to assert after-the-fact that DOI always had authority to include limitations based on price in any lease under the DWRRA.

Section 7504

- Section 7504 bans the issuance of leases to companies that hold 98/99 leases unless the company renegotiates to include price thresholds, or pays a conservation of resources fee. This section also has a conservation of resources fee for non-producing leases. In essence, this increases the rental fee because rentals are only due when the lease is not producing. The other problem with this section is that it prohibits a company from obtaining any lease, or any economic benefit from a 98/99 lease, by sale or other transfer, unless the company renegotiates all 98/99 leases or pays the fee on all of those leases. This leasing prohibition would effectively trigger a disruption in the leasing program and could have a severe adverse impact on the Gulf of Mexico leasing program.

Section 7505

- This would repeal the mandatory royalty relief provided for in Sections 344 and 345 of EPLA 2005, for shallow water/deep gas and for deep/ultra deep water production. This would also repeal the extension of discretionary royalty relief to Alaska non-producing leases. This section also repeals incentives for production from non-producing leases in NPR-A where the lessee has made a discovery or where the lessee has diligently pursued exploration. These provisions have an adverse impact and are clearly disincentives to domestic production and energy security.

Section 7604:

- Includes new provisions designed to prevent additional American oil and natural gas development, including prohibitions on developing the Roan Plateau where BLM now is assessing the feasibility of measures designed to ensure environmentally protective production. Also contains language designed to terminate programs that have successfully encouraged the development of America's offshore frontier resources based on no apparent assessment of the consequences to U.S. energy development. The bill includes punitive "conservation fees" to impose costs on producers that have legitimate federal contracts.

Similarly, Title XIII, the revenue title of H.R. 3221 contains adverse tax provisions affecting the development of American oil and natural gas.

Section 13001:

- Repeals the Section 199 manufacturers' tax deduction for the oil and natural gas industry (\$11.4 billion of 10 years) and applies only to investments made in the United States, consequentially hindering the ability of domestic producers to reinvest in American production, American jobs, and American energy.

Section 13002:

- Changes amortization period for geological and geophysical expenditures from 5 years to 7 years (\$100 million over 10 years), reducing available capital for certain large integrated oil companies to reinvest in energy production to provide for America's energy needs.

Section 13003:

- Modifies the determination of foreign oil and natural gas extraction income (\$3.5 billion over 10 years), affecting companies with both upstream and downstream foreign operations.

These provisions are discussed in greater detail in an attachment to this letter.

Before Congress takes steps that will reduce American natural gas supplies, we urge you to examine what such policies, not to mention environmental policies would mean for energy costs for residential consumers, natural gas-intensive industries and power generators. We are puzzled that so far this Congress has focused so little on natural gas. Despite the numerous hearings on climate change and energy policy this year, not a single natural gas industry witness has been invited to testify at a hearing – House or Senate – on future natural gas demand and supply dynamics in a carbon-constrained environment. Given that natural gas accounts for 25 percent of U.S. energy consumption, this is a stunning oversight.

For example, Congress has not examined the fact that ethanol production depends heavily upon natural gas. Therefore, as it debates new alternative fuel mandates, it should be incumbent on the Congress also to address where new natural gas supplies will come from to make possible additional ethanol production. Even more significantly, recent modeling of the McCain/Lieberman climate change legislation (S. 280) sponsored by the Natural Gas Council suggests that a 20 percent increase in natural gas demand by 2030 is quite possible given the need to meet the emissions reduction targets that would be mandated by that legislation. We urge both chambers to consider carefully how these and other policies will affect natural gas demand, so that the nation can develop adequate supplies and infrastructure now and thus avoid future adverse consequences.

Respectfully,

Independent Petroleum Association of America
Interstate Natural Gas Association of America
Industrial Energy Consumers of America
American Exploration and Production Council
Process Gas Consumers Group
U.S. Oil and Gas Association
National Ocean Industries Association
American Petroleum Institute
Natural Gas Supply Association