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Regulating Exploration on the Arctic OCS: Interior Finalizes Rules for Oil and Gas Exploratory Drilling on the Arctic Outer Continental Shelf¹

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On July 7, almost a year and a half after the proposed rules were published, the U.S. Department of the Interior's (DOI) Bureau of Ocean Energy Management (BOEM) and Bureau of Safety and Environmental Enforcement (BSEE) announced final regulations regarding future exploratory drilling activities on the U.S. Outer Continental Shelf (OCS) in the Arctic.²

The final rule focuses on exploratory drilling operations from floating vessels operating on the OCS within the Beaufort Sea and Chukchi Sea Planning Areas ("Arctic OCS").³ Recognizing the unique operating conditions in the Arctic—extreme environmental conditions, geographic remoteness, and the general absence of fixed infrastructure and existing operations, the final rule is "designed to help ensure the safe, effective, and responsible exploration of Arctic OCS oil and gas resources, while protecting the marine, coastal, and human environments, and Alaska Natives' cultural traditions and access to subsistence resources."⁴ As a result, the final rule imposes a number of new requirements, such as the development of comprehensive plans that account for the challenging Arctic conditions and demonstrate that the operator is prepared to respond to any number of issues that may arise on the Arctic OCS, including ready access to a relief rig to ensure quicker response in the event of an incident.

K&L Gates' Arctic team has been closely following developments in regard to oil, gas, and related infrastructure in the Arctic to assist clients with project development and public policy issues that will influence Arctic development.⁵ Though current market conditions have dramatically slowed interest in developing Arctic oil and gas resources, we expect mid- to long-term opportunities will remain. Companies and investors interested in engaging in

¹ The authors would like to thank Summer Associate Elle Stuart for her substantial contributions to this alert.

² Pending publication in the Federal Register, the Final Rulemaking is available here: <http://www.bsee.gov/ArcticRule/>.

³ 30 C.F.R. § 250.105.

⁴ Final Rulemaking at 1, 15.

⁵ See the Arctic team's previous alert on the proposed rule here: <http://www.klgates.com/en-US/regulating-exploration-on-the-arctic-ocs--us-federal-regulators-propose-rules-for-oil-and-gas-exploratory-drilling-on-the-arctic-outer-continental-shelf-02-23-2015/>.

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Arctic development should understand the new requirements and their direct impacts from a cost, compliance, and enforcement perspective. With offices in Anchorage, Houston, and Washington, D.C., K&L Gates is strategically positioned to help its clients in both transactions and litigation concerning Alaska's vast mineral and oil and gas resources.

Background

The Outer Continental Shelf Lands Act (OCSLA) gives the Secretary of the Interior responsibility for administering the leasing of the OCS and regulating mineral exploration and development operations on OCS leases. In the OCSLA, Congress established a national policy of making the OCS "available for expeditious and orderly development, subject to environmental safeguards, in a manner which is consistent with the maintenance of competition and other national needs."⁶ At the same time, Congress emphasized that the OCS needed to be developed in a safe manner "by well trained personnel using technology, precautions and techniques to prevent or minimize the likelihood of blowouts, loss of well control, fires, spillages, physical obstruction to other users of the waters, or other occurrences which may cause damage to the environment or to property, or endanger life or health."⁷

The Secretary of the Interior has delegated a significant amount of the administrative and regulatory duties for OCS exploration programs to BOEM and BSEE. BOEM reviews individual Exploration Plans (EP), while BSEE reviews the Application for Permit to Drill (APD) to determine whether the operator's proposed activities meet the OCSLA standards that govern offshore exploration and development. Under the extensive OCS oil and gas regulatory regime that is already in place, operators are subject to substantial application procedures and information requirements for exploration, development, and production activities; safety requirements for casing and cementing; regulations surrounding the design, installation, use, and maintenance of OCS platforms; development and implementation of Safety and Environmental Management Systems (SEMS); and preparation and submission of an Oil Spill Response Plan (OSRP).⁸

In response to renewed industry interest in exploratory drilling on the Arctic OCS for commercial quantities of oil and natural gas, in February 2015, BOEM and BSEE published a Notice of Proposed Rulemaking in the Federal Register, entitled "Oil and Gas Operations in the Outer Continental Shelf – Requirements for Exploratory Drilling on the Arctic Continental Shelf."⁹ After receiving letters from over 100,000 individual commenters, consulting with Alaska Native Tribes, considering key components of Shell's 2012 and 2015 Arctic exploratory drilling programs, and conducting extensive environmental and safety analyses, BOEM and BSEE published the final rule that builds on an already very extensive regulatory environment to include additional measures tailored to the unique operational and environmental conditions of the Arctic OCS.¹⁰

⁶ 43 U.S.C. § 1332(3).

⁷ 43 U.S.C. § 1332(6).

⁸ Final Rulemaking at 29.

⁹ 80 Fed. Reg. 9916 (Feb. 24, 2015).

¹⁰ Final Rulemaking at 15–16.

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Overview of Final Rule

The Arctic OCS final rule establishes a holistic regulatory framework that is more stringent than the regulations that govern other OCS locations. Importantly, the final rule only applies to Arctic OCS exploratory drilling activities that use mobile offshore drilling units (MODUs) and related operations during the open-water drilling season (typically late June to early November). The final rule does not apply to exploratory drilling on the Arctic OCS using other drilling technologies, including shallow water drilling from gravel islands or the use of a land rig on grounded or land-fast ice. As a result, exploratory drilling operations on the Arctic OCS using non-MODUs technology continue to be subject to the existing OCS oil and gas regulatory regime.¹¹

The final rule seeks to ensure that operators identify operational risks early on, plan to avoid and/or mitigate those risks, and understand and account for the unique challenges of operating on the Arctic OCS. As such, the final rule requires each operator to:

1. Design and conduct exploration programs in a manner that accounts for Arctic OCS conditions;
2. Develop an integrated operations plan (IOP) that addressed all phases of its proposed Arctic OCS exploration program, which must be submitted to BOEM at least 90 days in advance of filing its EP;
3. Have access to and the ability to promptly deploy Source Control and Containment Equipment (SCCE) while drilling or working below the surface casing;
4. Have access to a separate relief rig located close enough to timely drill a relief well in the event of a loss of well control;
5. Have the ability to predict, track, report, and respond to ice conditions and adverse weather events;
6. Effectively manage and oversee contractors; and
7. Develop and implement an OSRP that is designed and executed in a manner that accounts for the unique conditions in the Arctic and that provides the necessary equipment, training, and personnel to respond to an oil spill on the Arctic OCS.¹²

The final rule is estimated to result in new compliance costs for the industry between \$1.74 billion and \$2.05 billion over 10 years.¹³ BOEM and BSEE believe these costs are offset by the “unique significance” of the Arctic ecosystem and the substantial value to be gained if resources can be extracted and marketed economically, and they will not discourage exploratory drilling on the Arctic OCS.¹⁴

¹¹ *Id.* at 4, 15.

¹² Final Rulemaking at 5.

¹³ *Id.* at 17–18.

¹⁴ *Id.* at 18–19.

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New Operational Requirements

The final regulations include a number of revised and new prescriptive and performance-based requirements for operators on the Arctic OCS, including the development of an IOP, access to deployable SCCE and a relief rig, weather and ice monitoring and forecasting capabilities, planning requirements for oil spill response technology, and contractor oversight. Throughout the final rule, the DOI recognizes that there may be alternative pathways to achieve compliance with these new regulations.

IOP: In addition to the EP and the APD,¹⁵ the final rule requires the development of an IOP that addresses all phases of a proposed Arctic OCS exploration, from preparation to in-theater drilling operations to demobilization.¹⁶ The purpose of the IOP is to describe at a strategic level how exploratory drilling operations will be designed, executed, and managed as an integrated endeavor from start to finish.¹⁷ The primary issues that must be addressed in an IOP are vessel and equipment design; overall schedule of operations; mobilization and demobilization schedules; in-theater drilling objectives and timelines; weather and ice forecasting and management; contractor management and oversight; operational safety principles; staging of spill responses assets; and impact on local community infrastructure and workforce.¹⁸ As a conceptual, informational document, the IOP and the activities described in the IOP do not require agency approval.¹⁹ The overall purpose of the IOP is to allow “relevant agencies to familiarize themselves, early in the planning process, with the operator’s overall proposed program.”²⁰

SCCE Capabilities: The types of relief capabilities that are needed to respond to potential crisis events are not generally available in the Arctic. In the aftermath of the 2010 Gulf of Mexico Macondo oil spill, the importance of being able to respond to an incident in a timely manner took on even more importance. Thus, this final rule requires operators who use a MODU when drilling or working below the surface casing to “be able to stop or capture the flow of an out-of-control well” using their own SCCE (such as a capping stack, cap and flow system, and containment dome).²¹ Operators must have access to and be able to deploy SCCE capable of performing in Arctic conditions.²²

Relief Rig Requirement: One controversial element of the final rule is BSEE’s requirement that, as a redundancy, operators have access to a separate relief rig that could fully accommodate an out-of-control well.²³ The relief rig must achieve the performance standard of being able to kill and permanently plug an out-of-control well. More specifically, BOEM and BSEE explain that the operator must be able to “drill a relief well, kill and abandon the original well, and abandon the relief well prior to expected seasonal ice encroachment at the

¹⁵ Additional information must also be filed with the APD. 30 C.F.R. § 250.470.

¹⁶ 30 C.F.R. § 550.204.

¹⁷ Final Rulemaking at 33.

¹⁸ *Id.* at 34.

¹⁹ *Id.* at 35.

²⁰ *Id.*

²¹ *Id.* at 36.

²² 30 C.F.R. § 250.471.

²³ § 250.472.

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drill site” within 45 days.²⁴ BSEE believes that a relief rig is “currently the most reliable option” for plugging an out-of-control well, but the final rule provides flexibility to operators who can establish that alternative technologies meet or exceed the level of protection provided by the relief rig requirements by permitting the use of BSEE-approved alternative technologies.²⁵ Operators also are afforded some flexibility in that the final rule clarifies that the description of relief rig capabilities in the EP need only be detailed enough for BOEM to confirm that the operator has plans in place to conduct its operations in a safe manner. Thus, the EP is meant to obtain only the information that is known at the time of submission regarding the operator’s plans for complying with the relief rig requirements.²⁶

Weather and Ice Forecasting: BOEM and BSEE require that operators include in their IOPs, EPs, and APDs a description of their weather and ice monitoring and forecasting capabilities for all phases of their exploration program. The final rule further requires operators to (1) notify BOEM and BSEE immediately of any sea ice movement that has the potential to affect operations and (2) notify BSEE of the start and termination of ice management activities and submit written reports after completing these activities.²⁷

Oil Spill Response Plan: The final rule notes that OSRPs and related activities should be tailored to the unique Arctic OCS conditions and establishes specific planning requirements to maximize the application of oil spill response technology and ensure a coordinated response system.²⁸

Reducing Pollution: In response to concerns from partners including Alaska Native Tribes, BSEE also requires the capture of all petroleum-based mud and associated cuttings from Arctic OCS exploratory drilling operations to prevent the discharge of such pollutants into the marine environment.²⁹

Contractor Oversight: DOI is requiring that operators provide an explanation in their IOP of how they would apply oversight and risk management protocols to their personnel and contractors. Further, Arctic OCS operators are required to (1) report threatening sea ice conditions and unexpected operational issues that could result in a loss of well control, (2) conduct real-time monitoring of well operations,³⁰ (3) increase SEMS auditing frequency,³¹ and (4) enhance their oil-spill preparedness and response capabilities.³²

Industry Responses

In a press briefing, Interior Assistant Secretary for Land and Minerals Management Janice Schneider stated, “The Arctic rule will raise the bar for safety and environmental protection

²⁴ *Id.*

²⁵ § 250.472(c); § 250.141.

²⁶ § 550.220(c)(4).

²⁷ § 250.188(c); § 250.470; § 550.220(c)(2).

²⁸ §§ 254.55, .65, .70, .80, .90.

²⁹ Final Rulemaking at 39; 30 C.F.R. § 250.300 (b)(1)

³⁰ § 250.452.

³¹ § 250.1920.

³² *Id.*

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for any future exploration of Arctic OCS oil and gas resources.”³³ The debate that immediately followed the release of the final rule was whether this bar was high enough or too high.

Some environmental groups allege that the final rule did not do enough, noting that the Interior Department released “minimum regulations” that need strengthening,³⁴ and in one case asserted that “the only ‘safe’ form of drilling for the Arctic and the climate is none at all.”³⁵

Industry groups like the American Petroleum Institute (API), however, have challenged the basis for the final rule. API Upstream and Industry Operations Director Erik Milito released a statement asserting that some of the new requirements “may not improve safety and in fact may inhibit innovation and technological advancements.”³⁶ Similarly, National Ocean Industries Association President Randall Luthi said that although the rule provides some hope to the offshore industry in that they now know the applicable regulatory requirements, the rule “does not accurately reflect current industry capabilities and includes unnecessary requirements, such as same season relief wells, which may not be needed due to the availability of new response and containment equipment.”³⁷ For their part, the Arctic Energy Center stated, “even though the Administration has aggressively pursued a policy that restricts oil and gas development, today’s regulations do signify its recognition that America’s largest energy opportunity—the offshore Arctic—can be explored safely and responsibly.”³⁸

Implications

Given that operators recently have scaled back significantly on investments in Arctic OCS exploration (see Shell’s decision to discontinue their exploratory drilling), the extensive additional requirements set out in the final rules are expected to add significant costs to any future industry activities in the Arctic region. Although BOEM and BSEE recognize alternative and cooperative solutions, such as mutual aid agreements, to meet SCCE and relief rig capabilities and help manage the compliance costs of the new regulations, the final rule nonetheless is likely to further detract operators from investing in the Arctic region, particularly in the short- and medium-term. For future medium- and long-term opportunities, companies will have to consider and likely accommodate these new BOEM and BSEE requirements.

³³ *U.S. Finalizes Arctic Drilling Rule*, MAR. EXECUTIVE (Jul. 7, 2016), <http://maritime-executive.com/article/us-finalizes-arctic-drilling-rule>.

³⁴ Valerie Volcovici, *U.S. Finalizes Arctic Energy Development Regulation*, REUTERS (Jul. 8, 2016), <http://www.reuters.com/article/us-usa-energy-arctic-idUSKCN0ZN27J>.

³⁵ *Id.*

³⁶ Reid Porter, *API: Arctic Rule Could Inhibit Innovation, Technological Advancements and U.S. Energy Leadership*, AMER. PETROLEUM INST. (Jul. 7, 2016), <http://www.americanpetroleuminstitute.com/news-policy-and-issues/news/2016/07/07/statement-on-arctic-rule-proposal>.

³⁷ *U.S. Finalizes Arctic Drilling Rule*, *supra* note 31.

³⁸ James Osborne, *Stricter Rules Put in Place for Arctic Drilling*, HOUS. CHRON. (Jul. 7, 2016, 10:42PM), <http://www.houstonchronicle.com/business/energy/article/Stricter-rules-unveiled-for-Arctic-drilling-8346903.php>.

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