


MEMORANDUM

Date: May 18, 2010

To: Controller John Chiang, Chair
Lieutenant Governor Abel Maldonado, Member
Department of Finance Director Ana J. Matosantos, Member

From:  Paul D. Thayer, Executive Officer
California State Lands Commission
100 Howe Ave #100-S, Sacramento, CA 95825-8202

Subject: **Analysis of the April 6th 2010 Plains Exploration and Production Company and Environmental Defense Center Agreement**

Controller Chiang asked the California State Lands Commission staff to review an April 6, 2010 agreement between the Environmental Defense Center and Plains Exploration and Production Company (PXP). Staff has reviewed the April 6, 2010 agreement and, after consultation with the Attorney General's Office, has concluded that it does not resolve our concerns.

At its January 29, 2009 meeting, the California State Lands Commission denied PXP's application for two offshore oil and gas leases in the California Coastal Sanctuary adjacent to Vandenberg Air Force Base in northern Santa Barbara County. PXP and two prominent Santa Barbara County environmental organizations represented by the Environmental Defense Center contended that the leases should be approved because of the public benefits of a confidential written agreement between the two. However, the State Lands Commission was not convinced that achievement of the goals of the agreement was assured and determined that these leases were not in the best interests of the state.

Pursuant to that confidential agreement, the environmental groups, in return for supporting PXP's application for the two oil and gas leases in the California Coastal Sanctuary, sought to achieve certain environmental and public benefits. First, to end, within nine years of approval of the state leases, all production operations on PXP's federal leases at Point Arguello, abandon the wells and remove associated pipelines and onshore support facilities. Second, to end, within fourteen years of the approval of the new state leases, all production operations on PXP's Platform Irene, terminate the federal and state leases it serves, abandon all wells and remove associated pipelines and onshore processing facilities. The Environmental Defense Center claims that the April 6, 2010 agreement will prevent the use of the platforms at Point Arguello and Platform Irene for oil and gas production and therefore, they would be removed. In addition the agreement called for PXP to convey to The Trust for Public Land almost

four thousand acres of environmentally significant property and to provide effective greenhouse gas mitigation.

The two Commissioners who voted to deny the lease application, Lieutenant Governor John Garamendi and Controller John Chiang, based their opposition on four concerns: (1) that the leases would increase the risk of environmental damage to the coast from oil spills, (2) that the federal Minerals Management Service had not agreed to the end dates for oil and gas operations on their leases, thus calling into question the enforceability of those end dates, (3) that approving new leases in the California Coastal Sanctuary would encourage others to seek and the federal government to approve new offshore oil and gas development along the California coast and, (4) that the agreement between PXP and the environmental parties had not been made public.

On April 7, 2010, the Environmental Defense Center announced that its clients and PXP had reached a new agreement that when fully implemented would end existing oil and gas development offshore northern Santa Barbara County. This new agreement dated April 6, 2010 is posted on the Environmental Defense Center's web site (www.EnvironmentalDefenseCenter.org). Although PXP has not submitted a new oil and gas lease application to the Commission, staff anticipates that we may receive one. In the opinion of staff, the April 6, 2010 agreement, although an improvement over the prior one and appropriately made public, does not eliminate the Commission's main concerns with the prior agreement.

The April 6, 2010 agreement has the same oil development and environmental objectives, and is structured along the same lines as the first one. If the new agreement achieves its goals, it would result in the State Lands Commission issuing two new fourteen-year oil and gas leases in the California Coastal Sanctuary. It would also cause the cessation of oil production from platforms Hermosa, Harvest and Hidalgo at Point Arquello within nine years of the initiation of the two new state leases and cessation of state and federal production from platform Irene within fourteen years of the initiation of the two new state leases. Each of the federal and state leases would be relinquished, the wells plugged and abandoned, the pipelines and onshore processing support facilities removed, and almost four thousand acres of environmentally significant lands would be obtained for public use and enjoyment. In addition, the agreement attempts to make it infeasible for the four federal platforms to be used for oil and gas development in the future and seeks to cause their removal. Making these four platforms unavailable for oil and gas development in the future and causing their removal is especially important to achieve. According to the Minerals Management Service, 150 million to 160 million barrels of oil under unleased federal lands can be developed from these platforms using modern extended reach drilling technology.

In the April 6, 2010 agreement, the significance and implementation of the end dates for oil and gas production is more fully explained and the enforcement provisions strengthened by giving the state, including the State Lands Commission, the right to enforce its terms. However, nothing in the new agreement requires the state, the State Lands Commission or the Attorney General's Office to intervene, or take any action to

enforce the agreement. Further, if the agreement is not enforceable and achievement of some of its goals legally uncertain, adding the authority for the state to intervene has no value. The major benefit of these new provisions is that the state could intervene to prevent weakening of the April 6, 2010 agreement, particularly with respect to the land donation requirements. Perhaps the most significant change is making the new agreement public. Publication creates a forum for informed comment and debate about the agreement's potential effect on the statewide coastal environment and economy.

Fundamental to the continuing implementation doubts about the new agreement, the Minerals Management Service is not a party and has expressed opposition to those provisions that, if enforced, would interfere with the terms of their leases and cause them to terminate prior to reaching their economic limits. Federal regulations that govern offshore oil and gas leases provide that a lessee can relinquish its lease at any time. Relinquishment terminates an oil and gas lessee's right to produce oil and gas from the lease but continues the obligation to abandon the lease facilities, wells and platforms. Federal regulations do not provide for a lease assignment procedure after relinquishment. Lease assignment is normally done prior to relinquishment and is the Mineral's Management Service's primary way of testing whether older leases are still economic to operate. The Minerals Management Service has several remedies if it chooses to oppose early termination of the leases including amendment of the regulations governing the leases, injunctive relief, civil damages against the lessee for breach of statutory directives to produce a lease to its economic limits and civil damages against anyone who interferes with the lease by trying to enforce the lease termination provisions of the agreement. Monetary damages may not be sufficient for the Service as it sees energy supply as an important aspect of offshore oil development.

In addition, the wells, pipelines and platforms cannot be abandoned without specific permission from the Minerals Management Service. A lessee who initiates abandonment without permission may be subject to severe civil and criminal penalties. Nor can the Minerals Management Service be forced to agree to removal of the platforms if it believes that the platforms can be used to develop other oil and gas resources not currently under lease.

Whether or not the Minerals Management Service will pursue any of these potential remedies is uncertain but it could frustrate the April 6, 2010 agreement's goals by doing so. In the pursuit of clarity, our attorneys have asked the Minerals Management Service for permission to speak with their attorneys about what remedies might be available to it if they chose to oppose premature termination of the federal leases. We were informed that the Department of the Interior's Office of the Solicitor was unwilling to speak with us at this time.

Staff believes that because the federal lease production end dates are so far in the future, the Minerals Management Service's decision to accept or reject them and what action it will take will be made in the future and will be determined by the economic condition of the leases, the opportunities for other oil development from the platforms and the law and regulations existing at the time the decisions are made. As a result of

these uncertainties, staff is concerned that the environmental goals of the April 6, 2010 agreement may never be realized.

Even assuming that all of the environmental benefits envisioned by the new agreement are realized (the leases relinquished, wells, pipelines and platforms abandoned, environmentally significant lands conveyed and substantial lease revenue received by the public), the agreement does not address the problem of the encouragement of new federal leases off California that would come from issuing two new oil and gas leases in the California Coastal Sanctuary. The State Lands Commission and other officials have relied on California's no new lease policy as a basis for opposing these leases.

Further, the new agreement does not address the Commission's concern over the increased risk of oil spills created by oil and gas development at Tranquillon Ridge. This risk and its consequences have been demonstrated in the past off Santa Barbara and are now affirmed by the huge spill in the Gulf of Mexico following the explosion and loss of the Deepwater Horizon platform.

In light of the continued risk of an oil spill from the proposed Tranquillon Ridge leases, the potential encouragement of new federal leases that could be caused by approval of a new state lease, and the lack of assurance that production from the federal leases will end as provided for in the April 6, 2010 agreement, staff concludes that, apart from its publication, the new agreement does not cure the factors that led the Commission to determine that the proposed leases were not in the best interests of the state.