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Secretary Norton Announces Major New Incentive For Deep Gas Production in the Gulf of Mexico

With natural gas prices climbing sharply this winter and production in many areas of the Gulf of Mexico declining, Interior Secretary Gale A. Norton today proposed new incentives for energy companies to increase deep natural gas production in the gulf.

Under the proposal, the Interior Department's Minerals Management Service would provide royalty suspension incentives when companies take the risk of exploring and developing deep gas deposits in shallow-water areas they have already leased.

"American families have felt the pinch of higher natural gas prices in recent months because demand is outpacing supply," Norton said. "We need to respond by encouraging production of deep gas resources that otherwise are financially risky for companies to explore and develop."

The price of natural gas -- a clean burning energy source -- spiked last winter, placing an additional financial burden on families. The increased production spurred by the incentives will save America's families and other consumers an estimated $280 million a year over the next 15 years.

The Energy Information Administration forecasts the demand for natural gas will increase by 30 percent in the United States over the next 15 years, with supplies only available to meet 70 percent of this need. Production from deep wells on existing leases in the shallow water gulf is one of the most attractive sources of additional natural gas to help meet the near- and mid-term energy needs of the nation. MMS estimates that undiscovered gas resources of up to 20 trillion cubic feet may underlie this "frontier" area.

There are about 2,400 existing leases in the area targeted for relief in the proposed rule. Although natural gas from the OCS currently provides about 25 percent of domestic production, the contribution from the shallow water area has been declining precipitously over the past five years. While the shallow waters of the Gulf have been actively explored, relatively few wells have penetrated depths below 15,000 feet due to the high cost and risk associated with such wells. Since infrastructure is already in place, in terms of platforms and pipelines, MMS anticipates that production could come on line relatively quickly.

Under the rule, lessees would be eligible for royalty relief on their existing leases if they are willing to drill for new and deeper prospects more than 15,000 feet below sea level.

"There is a clear and significant gap in the projection of domestic natural gas demand and the available supply," said MMS Director Johnnie Burton. "This new rule seeks to stimulate domestic production in the near term from our most abundant and easily accessible areas."

The proposed incentive program provides the following:

- A royalty suspension on the first 15 billion cubic feet of gas produced from a well drilled and completed between 15,000 feet to less than 18,000 feet below sea level or on the first 25 BCF from a well drilled and completed 18,000 feet or deeper below sea level. To encourage companies to drill early, authorized drilling could commence immediately. This deep production must start before five years after the effective date of the final rule. One royalty suspension volume is available per lease.

- A royalty suspension supplement of 5 BCF, applied to future production of gas or oil from any drilling depth on that lease, is allowed for an unsuccessful well drilled to a target reservoir 18,000 feet or deeper. This dry hole incentive is aimed at helping to offset the high risk associated with drilling that deep. Two royalty suspension supplements are available per lease prior to production from a deep well.

- A well drilled after the date of the proposed rule and before five years after the effective date of the final rule may qualify for either incentive, if the lease has not had any deep gas production from wells drilled prior to the proposed rule. Any royalty suspension volume or supplement earned must be applied only to production occurring after the effective date of the final rule, even if this production actually started between the proposed and final rule.

MMS has included a deep gas royalty incentive for new leases since March 2001. MMS proposes to allow lessees to exercise an option to replace their existing deep gas royalty terms on leases acquired from sales held after January 1, 2001, with the terms in the final rule on this initiative.

The rule provides for a 60 day comment period. MMS plans to hold a workshop during the comment period, the date of which will be announced shortly.

MMS is the federal agency in the U.S. Department of the Interior that manages the nation's oil, natural gas, and other mineral resources on the outer continental shelf in federal offshore waters. The agency also collects, accounts for, and disburses mineral revenues from federal and American Indian leases. These revenues totaled more than $6 billion in 2002 and nearly $127 billion since the agency was created in 1982. Annually, nearly $1 billion from those revenues go into the Land and Water Conservation Fund for the acquisition and development of state and federal park and recreation lands.

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MMS Internet website address: **http://www.boem.gov**