

July 28, 2008

BLM Releases Proposed Rule for Oil Shale Leasing Program

On July 23, 2008, the U.S. Department of the Interior, Bureau of Land Management (“BLM”) issued a proposed rule to establish a commercial leasing program for federally owned oil shale and associated minerals located in a 16,000 square mile area in Colorado, Wyoming and Utah.

Under the Energy Policy Act of 2005 (“EPAAct”) and other statutory authorities, the Secretary of the Interior is authorized to establish regulations for a leasing program to encourage the development of oil shale resources. Although the substance produced from oil shale rock is different than conventional crude oil, it can be refined and converted into synthetic crude oil. Estimates from the American Association of Petroleum Geologists indicate that the United States holds more than 50 percent of the world’s oil shale resources, containing the equivalent of 1.5 to 1.8 trillion barrels of oil.

The Proposed Rule

The proposed rule is detailed and should be examined carefully by any party interested in seeking an oil shale lease for development or exploration. Nevertheless, many sections of the proposed rule have requirements similar to BLM’s existing mineral leasing programs. This Legal Alert provides a brief overview of the following key components: (1) the leasing process; (2) financial obligations; and (3) development or exploration plan requirements.

The Leasing Process

BLM has proposed to adopt a leasing process that would be very similar to other Department of Interior mineral leasing programs (e.g., coal). In addition to the process for obtaining commercial leases, BLM has also proposed separate, more streamlined procedures for obtaining exploration licenses that would not authorize extraction except in limited amounts necessary for experimental or demonstration purposes. Commercial leases would be subject to the following requirements and restrictions:

- All leases would be subject to a competitive bidding process.
- The required minimum bid would be \$1,000 per acre.
- The maximum oil shale lease would be 5,760 acres, as established by the EPAAct, while the rule would establish a minimum lease of 160 acres.
- The initial lease term would be 20 years with the possibility of renewal if an annual minimum production requirement is met.
- The minimum production requirement would be based on the lessee’s approved plan of development.
- Lessees would have to meet diligent development milestones or make payments in lieu of production.

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Financial Obligations

Recognizing the unique challenges involved in developing oil shale resources, BLM seeks to establish a flexible approach that will encourage commercial development and ensure a fair return to the United States. Although some rates are mandated by statute, others have been left to BLM's discretion and will not be determined until BLM publishes its final rule.

- *Rental Fees* – For a commercial lease, BLM will charge lessees an annual rate of \$2 per acre. Because the EAct sets the rental rate, BLM has no discretion to revise it.
- *Royalties* – BLM has proposed two options for production royalties, but is also considering a third alternative of a sliding scale rate. BLM will adopt one of these alternatives in the final rule:
 - Option 1: A rate of five percent of the amount or value of production of all oil shale products sold from or transported off the lease.
 - Option 2: A rate of five percent on initial production within a prescribed time frame, with a rate of 12.5 percent thereafter.
 - Option 3: A sliding scale based on the market price of competing products (e.g., crude oil and natural gas).
- *Payments in Lieu of Production* – Beginning in the 10th lease year, BLM has proposed a payment of no less than \$4 per acre per year for lessees that do not meet the minimum production requirement.

Development or Exploration Plan Requirements

In order to ensure responsible development, as well as compliance with federal environmental laws, BLM would require that all operations on oil shale leases be conducted under an approved plan of development or exploration plan. The plan of development or exploration plan would be subject to the following requirements:

- The plan must describe in detail the proposed exploration, testing, development or mining operations to be conducted, as well as the method by which the lessee will conduct the proposed activities.
- The plan must be consistent with the requirements of the lease or exploration license to protect nonmineral resources and provide for the reclamation of lands affected by the operations.
- An initial plan must be submitted within the first two years of the lease issuance date and a final plan within three years of issuance. Failure to submit a plan would result in a penalty of \$50 per acre per year.

Public comments on the proposed rule are due by September 22, 2008. However, under a restriction imposed by Congress, the BLM may not publish a final rule using funds under its current appropriations. Thus, the final rule will not go forward until Congress lifts this restriction.



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If you have any questions regarding this alert, or the services we provide, please feel free to contact any of the attorneys listed below or the Sutherland attorney with whom you regularly work.

Jacob Dweck	202.383.0775	jacob.dweck@sutherland.com
Gerald D. Higdon	713.470.6134	jerry.higdon@sutherland.com
Susan G. Lafferty	202.383.0168	susan.lafferty@sutherland.com
Gerald J. Pels	713.470.6135	gerry.pels@sutherland.com
Dena E. Wiggins	202.383.0499	dena.wiggins@sutherland.com
Daron T. Threet	202.383.0483	daron.threet@sutherland.com
Nathaniel J. Teti	202.383.0868	nathaniel.teti@sutherland.com