Coastal Impact Assistance

Whereas, the OCS Policy Committee, in approving its 1993 report entitled *Moving Beyond Conflict to Consensus*, recommended that a portion of the revenues derived from OCS program activities should be shared with coastal States, Great Lakes States, and U.S. Territories, and further recommended alternative proposals to provide impact assistance;

Whereas, the OCS Policy Committee at its May 1997 meeting reiterated its support for impact assistance and revenue sharing, recommending that the Secretary of the Interior initiate a legislative proposal in the 105th Congress to implement impact assistance and revenue sharing measures, using as a starting point the previous recommendations of this Committee contained in its 1993 report, *Moving Beyond Conflict to Consensus*;

Whereas at the May 1997meeting, the Minerals Management Service requested the Committee look at the mechanics of how a coastal impact assistance program would work and make recommendations about how to implement such a program;

Whereas the report of the Coastal Impact Assistance Working Group recommends that an OCS impact assistance and ocean/coastal resource protection program be added to, and a concomitant increase in OCS revenues be transferred to a revived and enhanced Land and Water Conservation Fund;

Whereas the report of the Coastal Impact Assistance Working Group proposes the mechanism for implementing such a program;

Now therefore be it resolved, that the Report of the OCS Policy Committee Coastal Impact Assistance Working Group be approved and adopted by the Policy Committee; and

Further, be it resolved, that the Working Group report be sent to the Secretary of the Interior with this resolution; and

Further, be it resolved, that the Secretary of the Interior is urged by the Policy Committee to take timely action to prepare and support draft legislation to implement the recommendations of this report.

Unanimously approved by the OCS Policy Committee: October 29, 1997

Coastal Impact Assistance

Report to the OCS Policy Committeee from the Coastal Impact Assistance Working Group

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Introduction

Throughout the history of the Outer Continental Shelf (OCS) oil and natural gas program, States and local communities have sought a greater share of the economic benefits of OCS development. After the 102d Congress chose not to enact any OCS initiatives, the OCS Policy Committee, in its report *Moving Beyond Conflict to Consensus* (October 1993), recommended:

> **A portion of the revenues derived from OCS program activities should be shared with coastal States, Great Lakes States, and U.S. Territories.**

There are two fundamental justifications for a revenue sharing or impact assistance program. The first is to mitigate the various impacts of OCS activities, and the second is to support sustainable development of nonrenewable resources.

In *Moving Beyond Conflict to Consensus*, the OCS Policy Committee addressed impacts associated with OCS activities. The report stated that, despite strict environmental standards and the program's exemplary environmental record, "OCS development still can affect community infrastructure, social services and the environment in ways that cause concerns among residents of coastal States and communities. " These effects cannot be entirely eliminated and they underscore the fact that, while the benefits of the OCS program are national, a disproportionate share of the infrastructure, environmental and social costs are local.

Impacts include:

- the need for infrastructure, such as ports, roads, water and sewer facilities, to support expanded economic activity accompanying OCS development;
- the need for public services, such as schools, recreation facilities, and other social services, to support the population growth accompanying OCS development;
- the need to mitigate the effects of occasional accidents (e.g., oil spills) or cumulative air, water, and solid waste discharges on coastal and marine resources and on the economic activities (e.g., tourism and fisheries) that depend on those resources;

- The need to mitigate the physical impact of OCS activities (e.g., pipelines, wake wash, road traffic, canal digging, and dredging) on sensitive coastal environments,

- the visual impact on residents and tourists from production platforms and facilities, waste disposal sites, pipeline rights of way, canals, etc.; and

- the costs to State and local governments of effective participation in OCS planning and decisionmaking processes and of permitting, licensing, and monitoring onshore activities that support offshore development.

Addressing these needs would help to strengthen the Federal-State-local partnership that must underlie a reasoned approach to national energy and coastal resource issues, resulting in a more productive OCS program. The breakdown in this partnership is evidenced by the fact that new OCS development is now occurring only off the coasts of Alabama, Alaska, Louisiana, Mississippi, and Texas.

The second justification lies in the concept of sustainable development. In short, a modest portion of the revenues derived from development of nonrenewable resources, such as oil and natural gas, should be used to conserve, restore, enhance, and protect renewable natural resources, such as fisheries, wetlands, and water resources. This concept also underlies the Land and Water Conservation Fund (LWCF), which uses OCS revenues to acquire and develop park and recreational lands nationwide.

These arguments for establishing an impact assistance program are even more relevant today, and this report's recommendations strive to create an equitable program to address these vital needs.

OCS Policy Committee

The OCS Policy Committee was established to provide advice to the Secretary of the Interior through the Minerals Management Service (MMS) on policy issues related to oil and natural gas activities on the OCS. Members represent the coastal States and constituencies impacted by the OCS program. The Committee frequently establishes subcommittees and working groups to look at issues in-depth and report back to the full committee. In its report *Moving Beyond Conflict to Consensus*, adopted in October 1993,

the Policy Committee discussed coastal impact assistance and revenue sharing (Appendix A), asserting that a portion of OCS revenues should be dedicated to maintaining and enhancing coastal infrastructure. It recommended sharing revenues derived from OCS program activities as the appropriate mechanism to achieve this goal. The Committee reiterated its support at its spring 1997 meeting and recommended that the Secretary of the Interior initiate a legislative proposal in the 105th Congress to implement impact assistance and revenue sharing measures using the recommendations in *Moving Beyond Conflict to Consensus* as a starting point. The MMS asked the Committee to look at the mechanics of how a coastal impact assistance program would work. Chairman Palmer appointed the Coastal Impact Assistance Working Group (Appendix B) and asked its members to look at alternatives and make recommendations about how to implement such a program.

Current Use of OCS Revenue

The majority of OCS revenues go into the Federal Treasury where they help pay for Federal programs and reduce the deficit. Also, a portion of those revenues goes into two special-purpose accounts, the LWCF and the National Historic Preservation Fund (NHPF). The LWCF supports parks and recreation through two programs. First, it provides matching grants, on a 50-50 basis, to States and Territories for the planning, acquisition, and development of public outdoor recreation areas and facilities. All 50 states and 6 U.S. Territories have received grants under this provision. Second, it contributes to the purchase of Federal park, conservation, and recreation areas. The fund is authorized at $900 million per year, of which over 90 percent comes from OCS revenues. Congress typically appropriates only a fraction of the authorized money and did not appropriate any money for the State Grant Program in fiscal years (FY) 1996 and 1997.

From FY 1969 through FY 1996, almost $9 billion has been appropriated from the LWCF. The State Grant Program has funded more than 37,000 park and recreation projects, with a total Federal investment of about $3.36 billion. The remainder of the appropriated funds have been for Federal acquisitions.

The NHPF is a 50-50 matching grant program that provides grants

to States and Territories for historic preservation purposes. The NHPF receives all of its funding—$150 million per year—from the OCS program. Since 1969, over $617 million has been spent from the NHPF for projects in all 50 States and in the U.S. Terretories.

Section 8(g) of the OCS Lands Act mandates the Federal Government to share with affected States 27 percent of revenues generated from leasing and development of oil and natural gas resources in the "8(g)" zone. This zone is a 3-mile-wide band of Federal water located directly adjacent to a State's seaward boundary. This provision also mandated a one-time payment to certain coastal States from funds held in escrow and additional payments to these States in installments over 15 years (beginning in FY 1987). The following seven coastal States have received almost $2.5 billion under the section 8(g) provisions of the OCS Lands Act: Alabama, Alaska, California, Florida, Louisiana, Mississippi, Texas. This money is used by the States as they deem necessary, without Federal restrictions.

Historical Background

Since 1945 when President Truman issued a proclamation declaring that the United States had jurisdiction, control, and power of disposition over the natural resources of the OCS, there have been bills introduced in most sessions of Congress to settle jurisdictional matters between the Federal Government and the States over offshore lands. A major factor in this dispute is the equitable sharing of benefits derived from OCS development.

In the mid-1970's, during the heat of the OPEC oil embargo, President Nixon's call for leasing 10 million acres of offshore land for drilling, and the Nation's growing environmental movement, Congress began rewriting the OCS Lands Act (OCSLA). Additionally, in response to an increasing concern among coastal States and communities that, as a result of OCS development, they would be faced with large infrastructure costs, land use commitments for support bases, and potential, irretrievable environmental losses, Congress also addressed the long simmering issue of sharing a portion of Federal revenues from OCS production with adjacent coastal States.

The result of that early Congressional initiative was the enactment, in 1976, of the Coastal Energy Impact Program (CEIP), which was incorporated into the Coastal Zone Management Act (CZMA). The CEIP was a program of grants, loans, and loan guarantees

designed to assist coastal States in addressing the public service and infrastructure costs and environmental expenses caused by coastal and OCS energy activity. It was a complex section of law that, in general, included:

- **OCS formula grants** to be used by coastal States to retire State or local bonds guaranteed under another provision of the program, to pay for public services and facilities resulting from OCS activity, and to prevent or ameliorate the loss of valuable environmental or recreational resources resulting from coastal energy activity.

- **Energy Facility Siting Planning grants** for the planning for economic, social, or environmental costs caused by the siting or construction of new energy facilities in the coastal zone.

- **OCS State Participation grants** to assist States to carry out their responsibilities under the OCSLA.

- **Loans** to States and local governments for new or improved public facilities or public services required as a result of coastal energy activity.

- **Guarantees of Bonds** (and other evidence of indebtedness) issued by States or local governments to pay for public facilities or public services required as a result of new or expanded coastal energy activity.

Individual coastal State allocations under the OCS formula grants section, which most resembled revenue sharing bills considered by Congress in later years, were based on a formula composed of:

- 1/2 for the amount of OCS acreage leased in a year that is adjacent to a coastal State;

- 1/4 for the volume of offshore oil/gas produced in a year that is adjacent to the State; and

- 1/4 for the volume of offshore oil/gas first landed in the State.

Each coastal State with a CZM program or making good progress

toward having a program was eligible for the annual grants. The CEIP funds were appropriated by Congress. Thus, individual State allotments were based on OCS activities but the amount of money available was not. In this sense, CEIP was not a pure OCS revenue sharing program.

During the Carter Administration, modest appropriations were made for the OCS formula, for energy facility siting planning, and for OCS State participation grants; also substantial funds were made available for the loans. The Reagan Administration stopped funding CEIP, and Congress repealed the program in the 1990 CZMA amendments.

Around the same time the Reagan Administration terminated Federal support for CEIP, the Department of the Interior accelerated the oil and natural gas leasing program. Many parties questioned the advisability of terminating programs that provided the States with means to participate in OCS and coastal planning at a time when competing use conflicts were expected to escalate.

As a result, Congress considered a variety of OCS revenue sharing legislation in the early 1980's. The philosophy behind this legislation was that a portion of future increases in Federal revenues from publicly owned nonrenewable ocean energy resources should be allocated to coastal States for the continued sound management of renewable ocean and coastal resources. This legislation tried to balance OCS impacts and coastal zone resource management obligations but did not establish a clear one-to-one relationship between OCS revenues and impacts. Despite growing budget deficits in the early 1980's and strong opposition from the Administration, the House passed ocean and coastal block grant legislation as separate bills in the second session of the 97th Congress in 1982 and in the first session of the 98th Congress in 1983. In 1984, in the second session of the 98th Congress, the proposal was included in a House-Senate conference report on a bill that covered a broad range of fisheries and coastal matters and passed the House by over a three to one margin. But the conference report was killed in the Senate when the Administration opposed it. During the 99th Congress, OCS revenue sharing was added to pending budget reconciliation legislation but was removed before final passage because of a veto threat from the

Administration. Legislative activity on OCS revenue sharing then

ceased for the remainder of the decade.

In 1986, Congress amended section 8(g) of the OCS Lands Act, to provide revenues to States from State-Federal boundary tracts, as discussed above. The 27 percent share of revenues in the 8(g) zone provided for under these amendments was intended to compensate States for possible drainage of oil and gas from State lands and for other costs associated with Federal OCS activity. Revenues are shared, however, only for the first 3 miles seaward of State waters.

In 1991, the Department of the Interior developed a legislative initiative on OCS impact assistance at the request of President Bush. This initiative attempted to link size and distribution of payments more closely to the impact of OCS activities on State and local communities. It proposed establishing an impact assistance fund consisting of 12.5 percent of new oil and natural gas royalties and related revenues. Coastal States and communities within 200 miles of a producing tract were eligible to receive funds, the amount of which was inversely proportional to the distance between the nearest coastline point and that tract.

Following the Bush Administration's proposal in 1991, Congress considered impact assistance as part of the National Energy Policy Act of 1992. The competing versions, part of a larger OCS title, died in conference when the entire title was struck because of House-Senate differences over unrelated provisions directing the buyback of certain existing offshore leases. The proposals included:

- the Senate's proposal of two funds, a larger fund similar to the Bush Administration's proposal and a smaller fund that based shares on coastal population, shoreline mileage, and the number, location, and impact of coastal energy facilities; and

- the House proposal sharing 4 percent of all OCS revenues with States that had coastal zone management plans, with most of the money going to OCS-impacted States, based largely on fixed percentages specified in the bill.

After the OCS provisions were dropped from the National Energy Policy Act of 1992, the OCS Policy Committee created a subcommittee to examine the issues in those provisions. The

Committee endorsed revenue sharing and proposed two funds, each of which would allocate payments by formulas incorporating a number of coastal and energy-related factors (Appendix A).

In the 104th Congress, the Senate Energy and Natural Resources Committee considered a bill (S.575) to create an impact assistance program. The proposal was similar to the Administration and Senate proposals in the 102d Congress. The Senate Committee took no action on the bill.

The primary obstacle to enacting impact assistance legislation during the 1990's has been identifying budget offsets required by the Congressional Budget Enforcement Act (Act) to avoid any net loss to the Federal Treasury. This Act requires that any new program that would increase costs or reduce Treasury receipts must be offset by cost reductions or revenue increases so that there is no net effect on the Treasury, at least during the 5- to 7-year budget scoring window. The Act is a constraint if the revenue sharing proposal is going to be a direct spending entitlement—but it is not if the proposal is going to be an authorization, subject to an appropriation. In the latter case, recent budget resolutions between the Administration and Congress have placed ceilings on the amount that can be appropriated for domestic discretionary programs. It is these ceilings that put constraints on the Interior Appropriation's Subcommittee allocations and, thus, on any revenue sharing proposal subject to appropriations. Whether as an entitlement or an annual appropriation, any impact assistance proposal will compete with other priorities for scarce budget resources.

Recommendation

The Working Group recommends that an OCS impact assistance and ocean/coastal resource protection program be added to, and a concomitant increase in OCS revenues be transferred to, a revived and enhanced Land and Water Conservation Fund

As described in the background section of this report, the LWCF is an existing program funded primarily by OCS receipts and is available to all States and Territories of the United States, subject to appropriations, to apply to the acquisition and management of land and water areas for parks and recreation uses. The Working Group proposes that the LWCF, which currently is authorized at a level of $900 million per fiscal year, be used to distribute annually

payments equaling 27 percent of new OCS bonuses, rents, and royalties to States and Territories that have an approved coastal management plan or that are making satisfactory progress toward such a plan, pursuant to the Coastal Zone Management Act (16 U.S.C. 1451). The revenues would be distributed in accordance with the principles described below. The LWCF authorization would increase by the amount of the impact assistance funds. The $900 million authorization for Federal land acquisition and State grants, and the formula for allocating LWCF moneys between those two programs in accordance with the Land and Water Conservation Fund Act of 1965, as amended (16 U.S.C. 4601), would not be affected.

The Working Group believes that establishment of an OCS impact assistance fund under the umbrella of the LWCF would be appropriate in light of the recent resurgence of interest in the fund. The LWCF is broadly supported by both inland and coastal constituents who recently have been calling for its revival following a dormant period during which total appropriations have been far below authorized levels and no funds have been appropriated for distribution to States since 1995. The Working Group also supports such a revival and would like it to be accompanied by the additional mechanism for making more revenue available to coastal States, Territories, and localities. Thus, the proposed mechanism is intended to support, revive, and enhance the LWCF while ensuring that more funds derived from the marine realm are directed to uses in coastal and marine areas as recommended by the OCS Policy Committee in 1993.

Proposal

Source and Amount of Revenue

- **The amount of additional money to be available from the LWCF each year for distribution to coastal States and Territories and localities would be 27 percent of new OCS revenues**

The source of revenue would be OCS receipts that include bonus payments for leases issued after the proposed impact assistance program is enacted, rentals on all new leases, and royalties and related payments on production resulting from well completions taking place after enactment (i.e., new production on both existing and future leases). The concept of targeting new OCS revenues is consistent with some previous legislative proposals, but the

Working Group's definition of new revenues is more expansive in that it would include royalties paid on new well completions on existing leases with production predating enactment. This reflects the Working Group's view that since each new well completion is a source of impacts as well as revenues—particularly in the case of production from step-outs or new horizons—a portion of the revenues gained from each new completion should be made available to affected States and localities to deal with those accompanying impacts.

The amount of money proposed to be added to the LWCF for distribution to coastal States and Territories and localities—27 percent of new revenues—is based on the percentage considered in some previous legislative proposals, most recently S. 575, as well as the percentage specified in section 8(g) of the OCS Lands Act, as amended (43 U.S.C. 1337), which applies to the distribution of revenues derived from the Federal OCS located within 3 miles of State waters. The impact assistance program would apply only to those leases that are not subject to section 8(g).

- **Authorization of the proposed impact assistance program as an entitlement would be preferable to authorization subject to appropriations**

Funding the proposed program as an entitlement would provide certainty to the recipients that they will have access to this source of revenues in the future which will allow them to issue bonds backed by the revenue stream. The Working Group's preference for an entitlement is based on lessons learned from the history of the CEIP, which was discontinued after several years due to lack of appropriations, as well as the current situation with the LWCF. The Working Group does, however, recognize that in light of current attention to the budget deficit, it might be extremely difficult to obtain funding for an OCS impact assistance program as an entitlement.

Eligible Recipients

- **All coastal States (including those bordering the Great Lakes) and Territories would be eligible to receive revenues**

Inclusion of all coastal States and Territories as eligible recipients would recognize that they form a unified coalition of entities with similar interests relating to their coastlines and, therefore, should not be subdivided when it comes to receiving coastal impact assistance. This proposal also is consistent with the OCS Policy Committee's 1993 recommendation and with the policy of some past OCS bills that a portion of the revenues received from the extraction of nonrenewable resources should be used for the protection of renewable ocean and coastal resources.

- **Coastal counties, as well as local governments that State governors identify as affected by OCS activity, would be eligible and would receive payments directly (rather than passed through the State)**

Local government eligibility for impact assistance is consistent with several previous legislative proposals and with the OCS Policy Committee's 1993 recommendation. Coastal counties (parishes, boroughs, etc.) would be automatically eligible for payments. The governors of coastal States would have the discretion to identify which inland local governments should receive impact assistance, as long as the governor certifies that there are impacts. This is a departure from legislative proposals that stipulated that inland counties must be within 60 miles of the coast in order to be considered for eligibility. The Working Group has consciously eschewed such a requirement so that the governors will have maximum discretion to assure that impact assistance funds are properly directed to the affected communities. The Working Group also would provide an appropriate check on the discretion of the governors by providing localities the right to appeal the governors' decisions concerning eligibility. Distribution of payments among local communities is discussed below in the *Allocation* and *Details* sections.

The recommendation that payments go directly to localities is intended to avoid placing bureaucratic burdens on the State as well as to prevent any associated delays in payments to local governments and problems that could result. The Working Group recommends that consideration be given to using the existing Department of the Interior Payment in Lieu of Taxes program to distribute revenues to eligible localities in order to avoid creating new systems.

Allocation

- **The amount for which each State and Territory is eligible would be determined by a formula giving weighted consideration to OCS production (50 percent), shoreline miles (25 percent), and population (25 percent)**

The formula proposed by the Working Group is drawn from elements included in previous legislative proposals and the OCS Policy Committee's 1993 recommendation and is designed to distribute revenues logically and equitably. The OCS production factor would be determined based on production activity within 200 miles of a State using the "inversely proportional distance" provision in previous legislative proposals. Under this approach, the amount of oil and natural gas produced from each OCS lease would be calculated along with the minimum distance of each producing lease from a State's shore so that both volume and proximity of production would be considered. Thus, the closer a State is to production, the greater its allocation (e.g., if State A is twice as far from a producing lease as State B, its allocation under the production factor of the formula will be half the size of State B's). The production, shoreline miles, and population factors would be weighted as indicated above in an overall formula that would be applied to each coastal State to determine its share of the available OCS revenues. This approach is intended to ensure that while all coastal States and Territories will receive revenues generated by OCS activity, the majority of those revenues will go to the States and communities adjacent to OCS production and its associated impacts.

- **Each coastal State with an approved coastal management plan (or making satisfactory progress toward one) would receive a minimum of 0.5 percent of the funds available, and those lacking or not proceeding toward such a plan would receive a minimum of 0.25 percent of available funds**

The concept of assuring that each State receives a minimum share of the available revenues is consistent with several previous legislative proposals, and the specific levels proposed are those included in the OCS Policy Committee's 1993 recommendation.

Likewise, the proposed connection between the minimum amount and participation in the coastal zone management program has its roots with the CEIP and has been included in most prior legislative proposals and the Policy Committee's recommendation.

- **Eligible local governments of States within 200 miles of OCS production would be able to receive 50 percent of the funds allocated to the State, and local governments in States not within 200 miles of OCS production would be eligible to negotiate with the State for a share of up to 33 percent of the funds paid to the State**

Provision of a sizable percentage of the available revenue to localities has been a part of all of the legislative proposals developed during this decade and is included in the OCS Policy Committee's 1993 recommendation. The amount distributed to each eligible locality in a State within 200 miles of OCS production would be determined according to the same weighted formula used for eligible States, which would be applied to 50 percent of the State's funds. States not proximate to OCS production would share 33 percent of their funds with local governments that submit applications to and receive approval from the State for projects consistent with the purposes of this recommendation (see *Earmarking* and *Details* sections below). The Working Group considers it logical and equitable to stipulate that a higher share (50 percent) be available to the affected localities of a State adjacent to OCS production and associated impacts. Similarly, it is appropriate to provide that a lower share (up to 33 percent) would be available to localities in those States that are not adjacent to production, since impacts related to the OCS program other than those resulting from production (e.g., responsibilities relating to OCS lease sales and operations plans) are borne primarily at the State government level. Further, any portion of the 33 percent share that a State's localities do not request and receive would revert to that State's use.

Authorized Uses

- **Acceptable uses of funds include mitigating the impacts of OCS activities and projects relating to onshore infrastructure and public services**

Provisions specifying the use of funds were included in the CEIP have been a part of the majority of the legislative proposals that have been considered, and were included in the OCS Policy Committee's 1993 recommendation. The Working Group would incorporate and expand on the eligible use provisions of S. 575, which specified:

> projects and activities related to all impacts of Outer Continental Shelf-related activities including but not limited to—(1) air quality, water quality, fish and wildlife, wetlands, or other coastal resources; (2) other activities of such State or county, authorized by the Coastal Zone Management Act of 1972 (16 U.S.C. 1451 *et seq.*); the provisions of subtitle B of title IV of the Oil Pollution Act of 1990 (104 Stat. 523), or the Federal Water Pollution Control Act (33 U.S.C. 1251 *et seq.*); and (3) administrative costs of complying with the provisions of this subtitle.

The Working Group proposes expanding the S. 575 criteria to include uses related to the OCS Lands Act and to onshore infrastructure and public service requirements resulting from OCS activity. Citing activities under the OCS Lands Act is intended to emphasize that consultation, information review, and other planning activities preceding OCS development and production entail significant expenses, especially for frontier area States and communities. Citing infrastructure and public service requirements is intended to recognize that intensive offshore activity results in onshore demands relating to port facilities, roads and railways, and public service needs such as schools and sewer and water facilities. The Working Group's proposed provisions concerning eligible uses of impact assistance funds are designed to carry forward the general reference of S. 575 to OCS-related uses while highlighting some of the specific monetary needs that are facing coastal States and communities as a result of the OCS program.

Details

- **States and counties eligible to receive funds would be required to submit plans and reports pertaining to use of the money**

The Working Group supports an approach to reporting that would incorporate and expand on some of the provisions of S. 575, which

call for an eligible locality to submit a project plan to the governor for approval before receiving funds and to certify annually the total amount of money spent, the amount spent on each project, and the status of each project. The Working Group also would require annual State certification of spending by localities and an accounting of all revenues received by the State. In addition, the Working Group recommends including a provision to give localities a right of appeal to the Federal administrator of the impact assistance program if a governor is perceived as failing to act promptly or as making unreasonable decisions with respect to a project plan. The proposed approach to reporting is intended to ensure responsiveness and accountability in a way that would not duplicate or complicate existing auditing requirements and, thus, would not be overly burdensome at the local, State, or Federal levels.

- **The program would be administered by the Secretary of the Interior**

The Working Group believes that since the LWCF and the OCS program are managed by the Department of the Interior, the Secretary of the Interior would be the appropriate official to administer the proposed OCS impact assistance program.

Appendix A—*Moving Beyond Conflict to Consensus,* subchapter on Coastal Impact Assistance and Revenue Sharing

Coastal Impact Assistance and Revenue Sharing

Department of the Interior Initiative

Following the President's June 1990 directive to prepare a legislative initiative to provide a greater share of OCS revenues to coastal communities directly affected by new oil and gas development, the Department of the Interior developed and submitted to the 102nd Congress a proposal for providing impact assistance to coastal states and communities located near OCS oil and gas activities. The proposal was based on the view that, despite strict environmental standards, OCS development still can affect community infrastructure, social services, and the environment in ways that cause concerns among residents of coastal states and communities. Since those effects cannot be completely eliminated and other means for obtaining revenue to deal with those effects may be limited, it would be appropriate to provide the states and communities located near OCS development with a greater share of the benefits of development.

Under the department's proposal to the 102nd Congress, impact assistance would have been distributed according to the following formula:

- the amount distributed would have been 12.5 percent of new royalties from each OCS tract;
- the money would have been allocated to all coastal states within 200 miles of a given tract—weighted inversely according to each state's minimum distance from that tract; and
- within each state, 50 percent of the allocation would have gone to the state government, and the remaining 50 percent would have been distributed to eligible counties within 200 miles of the tract from which revenues are generated—weighted inversely according to each county's minimum distance from that tract.

The assistance would have been provided only from royalties on new production starting after the date of enactment and would not have applied to tracts covered under section 8(g) of the OCS Lands Act. Payments to the fund would have started in FY 1993 and payments to state and local governments would have commenced in FY 1994. Eligible counties would have been designated by the governors of affected states, with mandatory inclusion of all coastal counties and discretionary inclusion of other counties within 60 miles of the coast. The payments would have gone directly from the federal government to the state and local governments. The impact assistance payments would have been an entitlement rather than an annual appropriation, and there would have been no earmarking or other restrictions on how the assistance is spent.

Measures Considered by the 102nd Congress

H.R. 776 provided for establishment of the Ocean and Coastal Resources Management and Development Fund to be comprised of 4 percent of the average amount of all OCS revenues generated from the three previous fiscal years and administered by the Department of Commerce. This fund would have been subject to appropriations, and the amount deposited to it could increase up to 5 percent each year. Coastal states—including Great Lakes states, territories, and possessions—would have been eligible for block grants from the fund if they have an approved CZM plan or are making satisfactory progress toward one. All recipients were to receive fixed shares of the fund, ranging from

0.25 percent to 10 percent as specified in the legislation, with a small remainder to be distributed based on production.

Grants from the fund would have been used by states and local governments to manage their ocean and coastal resources and to ameliorate adverse environmental impacts on the coastal zone that are related to energy facilities. Payments from the fund would have been annual, and before states could receive their grants, they would have been required to submit a report describing how the money would be used. At least 33.3 percent of each state's grant would have been allocated to local governments. The states receiving grants also would have been required to submit audits to the Secretary of Commerce. The authority of the Secretary of Commerce to award grants and the authority for the revenue sharing fund would have expired on September 30, 2004.

S. 2166 provided for establishment of two funds. The Coastal Communities Impact Assistance Fund would have been administered by the Secretary of the Interior. The Coastal Resources Enhancement Fund would have been administered by the Secretary of Commerce.

The Coastal Communities Impact Assistance Fund would have been comprised of 12.5 percent of the revenues derived from leases coming on production after the date of enactment. The fund would have been subject to appropriations and capped at $300 million. All states and counties within 200 miles of a producing OCS lease would have received money from the fund in allocations based inversely on their distance from the producing lease. Money from the fund would have been distributed directly to both coastal states (50 percent) and counties (50 percent). Payments were earmarked for natural and environmental resource projects and for purposes related to the CZMA and OPA, as well as for the coastal impact assistance and OCS programs that were part of all the earmarking proposals. Payments from the fund would have been for each fiscal year, and an audit for each year would be required. No expiration date for the fund was provided.

The Coastal Resources Enhancement Fund would be comprised of 4 percent of the revenues from new OCS leases. The fund would be subject to appropriations and would be capped at $100 million. All coastal states (excluding the Great Lakes States) would be eligible for grants from the fund if they have an approved CZM plan or are making satisfactory progress toward one. Grants from the fund would be for state and local government use to manage their ocean and coastal resources and to ameliorate adverse environmental impacts on the coastal zone that are related to energy facilities. Grants to the states would be determined by factoring in shoreline mileage (25 percent), coastal population (25 percent), and number, location, and impact of energy facilities located within the coastal zone (50 percent). At least 33.3 percent of each state's grant would be awarded to its local governments. No audit requirement or expiration date for the fund was provided.

Recommendation of the Subcommittee

A portion of the revenues derived from OCS program activities should be shared with coastal states, Great Lakes states, and U.S. Territories.

The Subcommittee believes that a portion of OCS revenues should be dedicated to maintaining and enhancing coastal infrastructure. Due to changing U.S. demographics, there is increasing stress on infrastructure in the nation's coastal regions. During the 1980's the number of people living on the nation's coasts increased dramatically to the point where over half the total U.S. population now resides in coastal regions. Coastal population is projected to continue to grow well into the next century. Billions of dollars will have to be spent on infrastructure to accommo-

date the increasing needs of coastal residents and industries. It would be most appropriate to use OCS revenues, which are derived from the marine realm, for uses in coastal and marine areas. Such use of OCS revenues also would be consistent with the new administration's emphasis on maintaining and rebuilding the nation's infrastructure. In light of these considerations the Subcommittee has identified the following specific purposes to which OCS revenues should be applied:

- to maintain existing coastal and marine resource programs and protect renewable resources;

- to offset the impacts—both onshore and offshore—of federal OCS oil and gas exploration and development on the nation's coastal areas in recognition that the benefits of offshore oil and gas development are national in scope, but coastal states and localities bear a disproportionate burden of environmental and social costs;

- to strengthen the federal-state partnership so necessary in the pursuit of national energy goals and the protection of state interests in pursuing OCS development and the siting of OCS and other energy facilities in or near the coastal zone, thereby reducing conflict and confrontation and resulting in a more productive OCS program; and

- to provide a uniform, reasoned approach for transferring payments from the federal government to state and local governments instead of having states pursue independent exactions to compensate for OCS related impacts (such actions would inject further uncertainty into the process of OCS leasing and development and provide disincentives to the production of the nation's OCS resources).

The Subcommittee believes that one of the most important purposes of impact assistance relates to fulfilling the needs of coastal states for some financial assistance to be able to participate effectively in the OCS program decisionmaking process. At least part of this assistance should come up front to fund establishment of the regional task forces recommended above and to support formulation, review, and analysis of program proposals under the regional task force approach. Funds also should be committed to studies identified by the regional task forces as critical for decisionmaking. While the bulk of impact assistance should flow to states adjacent to OCS oil and gas exploration and development activities, such funds should not be perceived primarily as an inducement to states to encourage OCS development off their coasts, and OCS leasing off a state's coast should not be a prerequisite for that state's receipt of any revenue.

The Subcommittee recommends adoption of a revenue sharing/impact assistance proposal in keeping with the principles discussed above. Two alternative proposal concepts have been outlined below which would satisfy these principles and may provide valuable insight and guidance for crafting an appropriate revenue sharing/impact assistance program. In the first proposal a portion of the present revenue stream to the federal treasury is allocated to revenue sharing/impact assistance for states and territories. In the second alternative proposal appropriated funds would be put into a trust fund annually and, after a few years of accumulation, the interest would be distributed as an entitlement to states and territories. Over the long run this latter approach would generate a permanent, and increasing, revenue stream without causing federal budget problems in the short run.

Recommended Alternative Proposal Concept I

This proposal establishes two funds for impact assistance. Payments from both funds would be through an entitlement rather than an annual appropriation, and there would generally be no restrictions on uses of the funds. All coastal states, the Great Lakes states and territories would be eligible for participation in both funds. However, the amount of payment from the second fund, Coastal Impact Assistance Fund, would be appropriated based on selected criteria and an allocation formula. The program is outlined below.

General

- Revenue for the two funds will be generated from all OCS bonuses, rents and royalties accrued after date of enactment. The percentage of revenues paid into the funds each year should be fixed between four and 15 percent of the average annual OCS revenues for the previous three years. Payments to states and territories will commence one year after establish ment of these funds.
- Total annual revenues will be divided between the two funds. The Coastal Resources Enhancement fund should receive 50-66 percent of the revenues, and the Coastal Impact Assistance fund 34-50 percent of the available revenues.
- Payments to states or territories from either of these funds requires a 50:50 split of payments between local governments and the state or territory.
- Eligibility of local governments for participation in the program and distribution formulae for revenues from the funds is determined by the Governor of each participating state or trust territory; with mandatory inclusion of coastal counties, boroughs and parishes within 200 miles of OCS tracts from which revenues are generated.

Coastal Resources Enhancement Fund

- All coastal states, Great Lakes states and territories are eligible to participate in the fund.
- Payments from the fund are based on the coastal zone management funding formula from the CZMA. Funding under the CZMA, as a percentage of total CZMA funding, is used to determine fixed shares of the revenues deposited into the Coastal Resources Enhancement Fund to be distributed to each state and territory.
- Coastal states or territories lacking an approved Coastal Zone Management plan would receive a fixed share amount equal to one-half of the smallest fixed share paid to a state or territory with an approved plan, respectively.
- There would be no restrictions on how money distributed from this fund could be spent, with the exception of those states or territories where moratoria are in place. In those states or territories where moratoria are in place that portion of funds paid directly to the state or territory is restricted to ocean and coastal resources research, assesment and management related to the purposes of the OCS Lands Act, CZMA, Oil Pollution Act, Marine Plastic Pollution Research and Control Act, and Marine Protection Research and Sanctuaries Act. However, those funds distributed to local governments, according to the formula determined by the governor, will remain unrestricted.

Coastal Impact Assistance Fund

- All coastal states, Great Lakes states, and territories are eligible to participate in the fund.

- Revenues from the Coastal Impact Assistance fund would be distributed according to the following fixed share formula. The allocation formula will include the following, equally weighted, factors for each participating state or trust territory:

  - percent of EEZ offshore;
  - shoreline miles;
  - population;
  - number and type of energy facilities;
  - cumulative volume of oil and gas landed;
  - number of producing leases;
  - total acreage under lease;
  - proven reserves;
  - number of acres planned or offered for lease; and
  - percent historical volume produced oil and gas

  Participating states or trust territories will be assigned a value, ranging from 1 to 10, for each of the above factors. The point score for each participating state or trust territory will be converted to a percentage, based on total possible points available, to determine the fixed share of revenues distributed to them for each year.

- The minimum score in the above formula (equal to or greater than 10) will be assigned a portion of the fund equal to 0.5 percent of available revenues for a state or territory with an approved Coastal Zone Management plan. Those participating states or territories without an approved Coastal Zone Management plan would be eligible to receive only a portion of the fund equal to 0.25 percent of available revenues, regardless of point score.

- There is no restriction on the use of payments from this fund.

Recommended Alternative Proposal Concept II

The second alternative proposal alters the mechanism of funding and distribution for OCS impact assistance. Establishment of the two funds described in Recommended Alternative Proposal I remains unchanged. The funding mechanism, however, involves establishment of a trust from which annual appropriations or percentage entitlements would be made to eligible states and territories. Key features are described below.

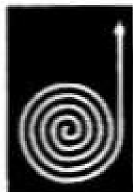
- No payments of OCS receipts would be made directly to any state or territory.

- States and territories would be eligible for distribution of interest earned on deposits of OCS receipts to the two impact assistance funds described in Proposal I.

- Annual deposits of OCS receipts to these two funds would total 12.5 percent of the average of the receipts for the previous 3 years.

- The principal from OCS deposits each year would remain in the corpus of each fund accruing interest. Distribution of interest would be delayed for the first 3 years of the program. Payments from the funds would be authorized to occur on an annual basis thereafter either through an entitlement or annual appropriation mechanism.

- There is no restriction on the use of disbursements to participating states and territories.



Incentives to Industry

Background

The increasing interdependence of the United States national economy and the global economy is nowhere more evident than in exploration and development of offshore oil and natural gas resources. As nations around the world strive for increased energy self-sufficiency, Americans must understand that in many economic endeavors governments, like the private sector, must compete for limited investment capital. In the highly competitive world of natural resource development, contract terms, tax and royalty systems and other elements of a government's *"take"* become factors by which the attractiveness of oil and gas investment in a particular country is judged.

As more and more countries make adjustments in their fiscal systems in order to attract investment in offshore areas, the evidence, including declining federal revenues from the OCS, indicates that the U.S. has become a relatively less attractive place to invest capital. In fact, the U.S. OCS is considered the highest cost oil and gas arena in the world in terms of bonuses, rents and royalties as well as regulatory requirements and resulting delays. Figure 13 indicates the recent trend in Gulf of Mexico OCS activity by showing the number of fields and average reserves discovered each year since inception of the program in 1954.

After three decades of development, the mature shelf areas of the Gulf of Mexico have become economically marginal and thus activity in these areas has become dominated by small independent companies that can operate at lower costs than their major oil company predecessors. At the same time, multinational parents of many major oil companies are labeling U.S. deep water drilling and development as *"excessive risk with limited upside potential,"* and thus are diverting money abroad in pursuit of other opportunities.

There is a tendency on the part of the general public and even citizens knowledgeable about the OCS program to view the Gulf of Mexico as one oil and natural gas province. From an economic and technical viewpoint the Gulf should actually be seen as two hydrocarbon provinces—a developed marginally economic shallow water shelf province and an undeveloped frontier deepwater province with potential for discovery of reserves larger than prospects remaining in the shelf area. The environmental and safety record in both the mature shelf and frontier deepwater provinces has been excellent.

The costs of producing OCS resources increase significantly with water depth. For example, a conventional fixed leg production platform in 800 ft. of water can cost $360 million to construct, whereas a conventional tension leg platform in 3,000 ft. of water may cost nearly $1 billion.

According to Department of the Interior estimates, there are 11 billion barrels of oil equivalent in the Gulf of Mexico in waters of a depth of 200 meters or more. In recent years there have been an estimated 50 deep water discoveries with estimated reserves equivalent to 2.5 billion barrels of oil for which there are no plans for immediate development because proceeding is not economic. Both the Department of the Interior and the Congress have considered incentives entailing some form of royalty relief to increase the economic viability of OCS resources.

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June 18, 1997, Herndon, Virginia
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