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Alabama Oil and Gas Update

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ALABAMA OIL AND GAS UPDATE



By: Shannon Oldenburg, Ted Holt, & Walton Jackson

TABLE OF CONTENTS

I. CASE LAW	271
A. <i>Environmental Group Challenges Offshore Oil and Gas Leasing in the Gulf of Mexico After the Deepwater Horizon Disaster</i>	272
1. Introduction	272
2. Background	272
3. The Environmental Claims	273
B. <i>Environmental Groups Challenge Offshore Oil Exploratory Drilling Plan in the Gulf of Mexico After the Deepwater Horizon Disaster</i>	276
1. Introduction	276
2. Background	276
3. The Environmental Claims	277
II. LEGISLATIVE ACTIONS	278

I. CASE LAW

The following cases are but two of many lawsuits filed by environmental groups challenging offshore oil and gas leasing, exploration, and development in the aftermath of the *Deepwater Horizon* drilling rig explosion and oil spill disaster in the Gulf of Mexico. The first case, filed in Alabama district court, involves agency approvals of lease sales that began shortly before and continued during and after the *Deepwater Horizon* incident, prior to concluding the environmental reviews of the specific impacts of the *Deepwater Horizon* spill. The second case, filed in the Eleventh Circuit, challenges a later phase agency approval of an exploration plan under similar circumstances.

A. *Environmental Group Challenges Offshore Oil and Gas Leasing in the Gulf of Mexico After the Deepwater Horizon Disaster*¹

1. Introduction

In 2011, Defenders of Wildlife (“DOW”) sued the Bureau of Ocean Energy Management, Regulation, and Enforcement (“BOEM”²), Department of the Interior (“DOI”), and Secretary of the Interior Ken Salazar (collectively, the “Federal Defendants”), challenging ongoing authorization of offshore oil and gas leasing and related drilling operations in the Gulf of Mexico.³ DOW’s position was that, in the wake of the *Deepwater Horizon* drilling rig explosion and oil spill in the Gulf of Mexico on April 20, 2010, the Federal Defendants had failed to modify their policies and practices concerning oil and gas leasing and operations in the Gulf as required by the National Environmental Policy Act of 1969 (“NEPA”), the Administrative Procedures Act (“APA”), and the Endangered Species Act (“ESA”).⁴ The court granted leave to intervene as defendants to the American Petroleum Institute, Independent Petroleum Association of America, United States Oil & Gas Association, and International Association of Drilling Contractors (collectively, the “Associations”), and Chevron U.S.A., Inc.⁵

2. Background

Offshore oil and gas leasing is governed by the Outer Continental Shelf Lands Act (“OCSLA”), which establishes a discrete, four-step process for establishing an offshore well: “(1) formulation of a five year leasing plan by the Department of the Interior; (2) lease sales; (3) exploration by the lessees; [and] (4) development and production.”⁶ In April 2007, the Secretary of the DOI issued a five-year plan for oil

1. *Defenders of Wildlife v. Bureau of Ocean Energy Mgmt., Regulation, & Enforcement*, No. 10-0254-WS-C, 2012 WL 1640676, at *5 (S.D. Ala. May 8, 2012).

2. On October 1, 2011, the Bureau of Ocean Energy Management, Regulation and Enforcement (“BOEMRE”), formerly the Minerals Management Service (“MMS”), was replaced by the Bureau of Ocean Energy Management (“BOEM”) and the Bureau of Safety and Environmental Enforcement (“BSEE”) as part of a major agency reorganization. (See <http://www.boem.gov/BOEM-Newsroom/Press-Releases/2011/press09302011.aspx>.) In the interests of simplicity and consistency, the agency is referred to herein as “BOEM” for all purposes, with the understanding that it was actually known by different names at different times relevant to this action.

3. *Defenders of Wildlife v. Bureau of Ocean Energy Mgmt., Regulation, & Enforcement*, 791 F. Supp. 2d 1158, 1161 (S.D. Ala. 2011).

4. *Id.*; National Environmental Policy Act of 1969, 42 U.S.C. §§ 4321, 4331–4335, 4341–4347 (2009 & Supp. 2012); Administrative Procedures Act, 5 U.S.C. §§ 551–559, 701–706 (2008 & Supp. 2012); Endangered Species Act of 1973, 16 U.S.C. §§ 1531–1544 (2008).

5. See *Defenders of Wildlife v. Bureau of Ocean Energy Mgmt., Regulation, & Enforcement*, No. 10-0254-WS-C, 2010 WL 5139101, at *1, *4 (S.D. Ala. Dec. 9, 2010).

6. *Defenders of Wildlife*, 2012 WL 1640676, at *1.

and gas leasing on the Outer Continental Shelf for the prospective period from 2007 to 2012 (the “Five-Year Plan”).⁷ The Five-Year Plan was supported by extensive environmental review, including an April 2007 Environmental Impact Statement (the “Multi-sale EIS”), a September 2008 Supplemental EIS, and 2007 consultations with the United States Fish & Wildlife Service (“FWS”) and the National Marine Fisheries Service (“NMFS”), in satisfaction of BOEM’s obligations under NEPA and the ESA.⁸ In the spring of 2010, BOEM finalized over 200 deepwater oil and gas lease purchases pursuant to the Five-Year Plan, collectively known as Lease Sale 213, beginning the process before, but completing the sale after, the *Deepwater Horizon* disaster began.⁹

3. The Environmental Claims

At issue in the litigation were bids accepted and approved for Lease Sale 213 after the *Deepwater Horizon* disaster began. DOW contended that once the *Deepwater Horizon* disaster began on April 20, 2010, BOEM was obligated to suspend the bid approval process until (1) a supplemental EIS was prepared that analyzed the environmental effects of the Five-Year Plan in light of the *Deepwater Horizon* disaster and (2) completion of reinitiated consultations with FWS and NMFS for the same reason. BOEM did, in fact, begin preparation of a supplemental EIS in 2010 to update the 2007 Multi-sale EIS and 2008 supplemental EIS; however, the 2010 supplemental EIS was prepared after completion of Lease Sale 213.¹⁰ BOEM also reinitiated consultations with NMFS and FWS in 2010, but those evaluations are still ongoing, and BOEM continued to rely upon the 2007 consultations when issuing approval of both lease sales and exploration plans.¹¹ Of particular importance to the litigation, activities associated with Lease Sale 213 were not terminated, suspended, slowed, or impaired in any way by the *Deepwater Horizon* disaster.¹²

DOW’s position was that the *Deepwater Horizon* disaster revealed “new information” that triggered BOEM’s duty under the ESA, NEPA, and the APA to cease action until completion of the reinitiated consultations (a process that could last several years) and prep-

7. *Id.* at *2.

8. *Id.*

9. *Id.* In all, BOEM accepted at least 331 bids for Lease Sale 213 between the onset of the *Deepwater Horizon* disaster on April 20, 2010, and the conclusion of the lease sale on June 10, 2010. *Id.* at *4.

10. BOEM published its Notice of Intent to prepare a supplemental EIS on November 2010 “to consider new circumstances and information arising, among other things, from the *Deepwater Horizon* blowout and spill. . . .” *Id.* at *16, n.21.

11. BOEM reinitiated consultation with the NMFS and FWS on July 30, 2010, “to examine the effects of the Five-Year Plan . . . specifically in response to the *Deepwater Horizon* incident.” *Id.* at *9. Those consultations are ongoing and may take many years to complete.

12. *Id.* at *4.

aration of the supplemental EIS.¹³ DOW's claims were narrowly focused on whether BOEM violated the ESA, NEPA, and APA by not waiting for completion of the environmental review processes before continuing the Lease Sale 213 activities.¹⁴

Following adjudication of various motions to dismiss pursuant to Rule 12(b) of the Federal Rules of Civil Procedure, the court determined that three of DOW's claims should proceed to trial:

1. The portion of DOW's Claim One alleging that BOEM violated NEPA and the APA by continuing to rely upon the conclusions of the April 2007 'Multi-sale EIS' for Lease Sale 213 after the *Deepwater Horizon* incident without completing a supplemental EIS and Environmental Assessment;
2. DOW's Claim Two, alleging that BOEM violated the APA in Lease Sale 213 by accepting more than 200 bids for new oil and gas drilling leases after the *Deepwater Horizon* spill without first supplementing the Multi-sale EIS; and
3. DOW's Claim Four, alleging that BOEM violated the ESA and APA by failing to ensure that its actions with respect to offshore drilling in the Gulf following the *Deepwater Horizon* incident were not likely to jeopardize the continued existence of endangered or threatened species.¹⁵

The court next turned to resolve DOW's motion for summary judgment, the Federal Defendants' cross-motion for summary judgment, and the joint motion for summary judgment by the Associations and Chevron U.S.A., Inc. as intervenors.

The standard of review for claims brought under the ESA and NEPA are promulgated under the APA. The APA provides that a reviewing court can set aside an agency's actions, findings, or conclusions if they are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with the law."¹⁶ A court may not substitute its own "judgment for the agency's as long as its conclusions are rational."¹⁷ Under this standard, the court was tasked with determining whether BOEM acted arbitrarily, capriciously, or in abuse of discretion when it continued with the Lease Sale 213 bid approval process after the *Deepwater Horizon* disaster began without first completing a new supplemental EIS and the reinitiated consultations.

Defending its actions to continue accepting bids for Lease Sale 213 after the *Deepwater Horizon* disaster commenced, BOEM relied heavily upon the compartmentalized nature of the four-step process

13. *Id.* at *5.

14. *Id.* at *16.

15. *Defenders of Wildlife v. Bureau of Ocean Energy Mgmt., Regulation, & Enforcement*, 791 F. Supp. 2d 1158 (S.D. Ala. 2011).

16. 5 U.S.C. § 706(2)(A) (2008).

17. *Miccosukee Tribe of Indians of Fla. v. United States*, 566 F.3d 1257, 1264 (11th Cir. 2009).

for oil and gas development prescribed by OCSLA.¹⁸ BOEM's position was that its lease approval actions fell discretely within the second stage of the process and, therefore, should be evaluated without regard to any exploration or development that may be approved in following stages.¹⁹ Through this narrow lens, BOEM argued that the mere act of approving lease bids had no significant repercussions for the environment or any endangered species.²⁰

The court agreed with BOEM, finding that the strict, staged structure of the OCSLA development process was fatal to DOW's ESA claim. The act of approving bids for lease sales must be considered as a wholly discrete act for purposes of the "stage-by-stage environmental review process [that] the courts have pegged as being Congress's purpose in establishing the OCSLA framework."²¹ Noting that "[c]ourts have recognized that OCSLA lease sale decisions, in and of themselves, generally do not cause jeopardy to listed species or critical habitat" regulated by the ESA, the court found that DOW had not met its burden to show that BOEM violated the ESA and that it was not arbitrary, capricious, or an abuse of discretion for BOEM to continue issuing leases after the *Deepwater Horizon* disaster without waiting for completion of the reinitiated consultations.²²

With regard to DOW's NEPA claim, the court found, too, that it was not arbitrary, capricious, or an abuse of discretion for BOEM to continue issuing leases after the *Deepwater Horizon* disaster began without stopping to prepare a supplemental EIS:

- (i) BOEM already had the benefit of a comprehensive EIS which, as DOW concedes, covered all aspects of the leasing and development process; and (ii) nothing about the *Deepwater Horizon* event constituted 'new information' that the approval of leases by BOEM would affect the human environment in a manner or to an extent different than that forecast by the original EIS.²³

Again, DOW failed to meet its burden of showing that BOEM acted arbitrarily, capriciously, or in abuse of discretion by continuing to approve bids for Lease Sale 213 in the immediate aftermath of the *Deepwater Horizon* disaster or to wait until after the reinstated consultation and supplemental EISs were completed.²⁴

Holding that BOEM's actions related to Lease Sale 213 did not violate the ESA, NEPA, or the APA, the court denied DOW's motion for summary judgment and granted summary judgment in favor of the defendants and intervenors.

18. *Defenders of Wildlife*, 2012 WL 1640676, at *12.

19. *Id.* at *12.

20. *Id.* at *13.

21. *Id.* at *12, *14.

22. *Id.* at *13–14, *19.

23. *Id.* at *19.

24. *Id.* at *20.

B. *Environmental Groups Challenge Offshore Oil Exploratory Drilling Plan in the Gulf of Mexico After the Deepwater Horizon Disaster*

1. Introduction

Defenders of Wildlife v. Bureau of Ocean Energy Management is a consolidated appeal to the United States Court of Appeals for the Eleventh Circuit by Defenders of Wildlife and Gulf Restoration Network. (“Petitioners”) challenging an exploratory drilling plan approved by the BOEM under the OCSLA.²⁵ Petitioners claimed that BOEM’s approval of the Shell Exploration Plan S-7444 (“Shell EP”) violated the ESA and the NEPA.²⁶

2. Background

At issue in the case were actions taken under the third phase of the four-stage process for establishing an offshore well under OCSLA: lease exploration.²⁷

After identifying an area of the Outer Continental Shelf for which it would develop a Five-Year Plan, pursuant to the first phase of the OCSLA process, BOEM consulted with the National Marine Fisheries Service (“NMFS”) and the United States Fish and Wildlife Service (“FWS”) in 2007.²⁸ This consultation was to ensure that BOEM was in compliance with all of its obligations under the ESA with regard to the Five-Year Plan.²⁹ Pursuant to the obligations imposed by NEPA, an Environmental Impact Statement (the “Multi-sale EIS”) was also completed in 2007.³⁰ Based upon the information collected through both the consultation and preparation of the Multi-sale EIS, the Five-Year Plan was approved, and the second (lease sale) phase of the OCSLA process was initiated.

In the wake of the April 20, 2010, *Deepwater Horizon* disaster, BOEM reinitiated consultation with NMFS and FWS, in order to consider “new information” brought to light by the *Deepwater Horizon* disaster.³¹ As the reinitiated consulting is still ongoing, BOEM has

25. *Defenders of Wildlife v. Bureau of Ocean Energy Mgmt.*, 684 F.3d 1242 (11th Cir. 2012); Outer Continental Shelf Lands Act, 43 U.S.C. §§ 1331–1356a (2009).

26. Endangered Species Act of 1973, 16 U.S.C. §§ 1531–1544 (2008); National Environmental Policy Act of 1969, 42 U.S.C. §§ 4321, 4331–4335, 4341–4347 (2009 & Supp. 2012).

27. *Defenders of Wildlife*, 684 F.3d at 1246. The OCSLA establishes a four-step sequence for establishing an offshore well: (1) formulation of a five year leasing plan by the Department of the Interior; (2) lease sales; (3) exploration by the lessees; (4) development and production. *Id.*

28. *Id.* at 1248.

29. *Id.*

30. *Id.* at 1247.

31. *Id.* at 1248.

continued to rely upon the 2007 consultation when issuing approval of both lease sales and exploration plans.³²

Pursuant to the third phase of the OSLA process, Shell submitted the Shell EP to BOEM on March 31, 2011.³³ The plan included a “catastrophic spill event analysis,” which took into account “new information” revealed by the *Deepwater Horizon* disaster.³⁴ BOEM conducted a preliminary environmental analysis (“EA”), which examined the Shell EP’s potential impact on the environment.³⁵ This EA relied heavily upon BOEM’s 2007 Multi-sale EIS.³⁶

Based upon the 2011 EA and the 2007 consultation data, BOEM determined that the plan would not violate the ESA.³⁷ BOEM also determined that the Shell EP would not significantly affect the quality of the human environment within the meaning of NEPA and, thus, would not require an EIS. BOEM issued a Finding of No Significant Impact (“FONSI”) under NEPA and approved the Shell EP on May 10, 2011.³⁸

Petitioners participated in the administrative proceedings and filed their petition for review of the Shell EP on June 9, 2011.³⁹ Petitioners Gulf Restoration Network, *et al.*, sought remand for further administrative action, and Petitioners Defenders of Wildlife, *et al.*, sought both vacatur and remand.⁴⁰

3. The Environmental Claims

First, Petitioners argued that BOEM’s decision not to prepare an EIS violates NEPA.⁴¹ Specifically, Petitioners contended that the EA was only a general summary of the environmental impacts of the Shell EP and failed to cite site-specific information.⁴² Petitioners complained that the EA prepared for the Shell EP was simply too similar to an EA prepared by Shell for a different exploration plan in a different area of the Gulf of Mexico.⁴³ Second, Petitioners argued that BOEM’s decision to reinitiate consultation pursuant to its ESA obligations effectively conceded that the 2007 consultations were inadequate for review of exploration plans after the *Deepwater Horizon* disaster occurred in 2010.⁴⁴ Petitioners argued that the inadequacy of

32. *See id.*

33. *Id.* at 1248.

34. *Id.*

35. *Id.* at 1249.

36. *Id.* at 1247.

37. *Id.* at 1247–48.

38. *Id.* at 1248.

39. *Id.* The petition was filed directly to the Eleventh Circuit per 43 U.S.C. § 1349(c)(2). *See id.* at 1245.

40. *Id.* at 1248.

41. *Id.* at 1249.

42. *Id.*

43. *Id.*

44. *Id.* at 1252–53.

the 2007 consultations barred BOEM from approving the Shell EP until after the reinitiated consultations were complete.⁴⁵

The court found against Petitioners on both issues, denying the petition for review. Addressing the first contention, the court disagreed with Petitioners' characterization of the EA as lacking in enough site-specific information to comply with NEPA, and it held that Petitioners had not overcome the extremely deferential "arbitrary and capricious" standard of review prescribed by the APA regarding the agency's factual determinations and decision that no EIS was required.⁴⁶ Rejecting Petitioners' second argument, the court noted that no precedent supported their contention that reinitiating consultation invalidates the conclusions of the prior consultation. Furthermore, the court found there was no specific evidence to establish that any endangered species would be put in jeopardy by the proposed exploration.⁴⁷ As such, the court concluded that BOEM had not acted arbitrarily or capriciously in approving the Shell EP; rather, its decision "reflect[ed] the agency's balance of environmental concerns with the expeditious and orderly exploration of resources in the Gulf of Mexico."⁴⁸

II. LEGISLATIVE ACTIONS

On May 16, 2012, the Alabama Legislature passed Senate Bill 216 ("S.B. 216") that requires submission to the Probate Office of proof of the purchase price or value of the property interests conveyed to support calculation of the privilege tax for recording the instrument of conveyance. S.B. 216 amended section 40-22-1 of the Alabama Code ("Section 40-22-1"), and it applies prospectively to deeds, bills of sale, and "other instruments of like character" that are recorded after the law took effect on August 1, 2012.⁴⁹ Prior to the enactment of S.B. 216, instruments of conveyance could recite nominal consideration, and Probate Offices had the discretion to determine the value of the property being conveyed by, among other methods, accepting statements of value from the recorder. This practice will no longer be allowed.

S.B. 216 requires that a "Real Estate Validation Form," developed by the Alabama Department of Revenue, be filed with the Judge of Probate, serving as "proof of the actual purchase price paid for the property, or if the property has not been sold, proof of the actual value of the real or personal property which is the subject of the in-

45. *Id.* at 1253.

46. *Id.* at 1249.

47. *Id.* at 1252.

48. *Id.* at 1253.

49. 2012 Ala. Acts 494.

strument being recorded.”⁵⁰ The tax rate is \$.50 per \$500 in value of the property transferred.⁵¹ Failure to present proof of purchase price or actual value will result in a tax based on the assessed value of the property, plus a penalty of \$100.00 or 25% of the tax actually due, whichever is greater.⁵²

While prior exceptions to Section 40-22-1 remain in effect, as of the publication of this Update, it is unclear whether the changes enacted in S.B. 216 will apply to or affect the recordation of instruments conveying leasehold interests in severable oil, gas, and minerals.⁵³ One point of uncertainty is that S.B. 216 excepted from the requirement to provide proof of value instruments conveying only “leaseholds easements or licenses . . .”⁵⁴ The coupling of the terms “leaseholds easements” in S.B. 216 is almost certainly a typographical error, with a comma omitted that would separate and distinguish “leaseholds” from “easements” in the series. At present, no Alabama court has acknowledged or defined an interest called a “leaseholds easements,” and the Alabama Code exclusively uses the terms “leaseholds” and “easements” as separate and distinguishable property rights in a series.⁵⁵ If the omission of the comma is, in fact, a typographical error, amended Section 40-22-1 would provide an exception to the requirement to provide proof of value for leaseholds, easements, or licenses. Accordingly, under this reading, the procedures and fees for recording oil, gas, and mineral leaseholds would not change. However, conveyances, other than by lease, of severable oil, gas, and mineral interests, would be subject to the requirement to provide proof of the value of the interests conveyed.

The amendment to Section 40-22-1 does not change the Mineral Documentary Tax required by Alabama law,⁵⁶ which is assessed and paid separately from the recording tax. Under the Mineral Documentary Tax statute, any leasehold that grants an interest in, and any deed or other conveyance that transfers, any nonproducing oil, gas, or other mineral interests must be recorded and is subject to the Mineral Documentary Tax. The Mineral Documentary Tax is charged in lieu of ad valorem taxes and is calculated on the basis of acreage, rather than the value of the oil, gas, or other nonproducing mineral interest conveyed.

50. *Id.* A copy of the Real Estate Validation Form may be obtained from [http://www.mc-ala.org/ElectedOfficials/ProbateJudge/ProbateDivisions/RecordsRecording/Documents/Form RT-1 \(Real Estate Sales Validation Form\).pdf](http://www.mc-ala.org/ElectedOfficials/ProbateJudge/ProbateDivisions/RecordsRecording/Documents/Form RT-1 (Real Estate Sales Validation Form).pdf).

51. *Id.*

52. *Id.*

53. Surviving exemptions state that no licensing tax shall be imposed upon: (1) transfer of mortgages upon which mortgage tax has already been paid, (2) “deeds or instruments executed for a nominal consideration for the purpose of perfecting title to real estate,” and (3) re-recording in order to perfect title or correct maturity dates of mortgages, deeds and other instruments executed prior to October 1, 1923. *Id.*

54. *Id.*

55. *See, e.g.*, ALA. CODE § 41-10-239 (2000).

56. ALA. CODE § 40-20-31 (1975).

The days of indicating a nominal sum as consideration and simply informing the Probate Office of the value of oil, gas, and mineral interests conveyed by deed are over, and S.B. 216 clearly requires proof of the value of such conveyances. Although, it appears that oil, gas, and mineral leaseholders will not have to provide proof of value and can continue to record leasehold conveyances as they have in the past. The Mineral Documentary Tax remains in place, unchanged by S.B. 216. Readers should be aware, however, that because of the uncertainties in the new law, it may be subject to different interpretations by Probate Offices throughout the State.