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JEFFREY DUNCAN
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January 11, 2012

Secretary Ken Salazar
Department of the Interior
1849 C Street, N.W.
Washington, D.C. 20240

Dear Secretary Salazar:

I congratulate you and the Department of Interior for December's auction of offshore drilling leases in the Gulf of Mexico, the first such sale since BP's Deepwater Horizon disaster. Under your leadership, the Department has taken significant steps to improve the safety of offshore drilling, and this lease sale (which attracted more than \$337 million in high bids) is testament to how far the Department has come. I believe we will be well served by these reforms as new offshore resources are developed.

I am writing now because when I look at the auction results, I wonder whether the system for auctioning offshore leases is also in need of reform. In recent auctions, most offshore tracts offered at auction do not receive bids, and less than 25 percent of tracts receiving bids attract more than a single bid.¹ I am concerned about the lack of competitive bidding in auctions for drilling rights in the Gulf and elsewhere, and I want to make sure taxpayers are receiving fair value in sales of America's offshore resources.

In the December auction, there were even fewer bids from a smaller number of companies than usual, which is somewhat surprising given what the oil and gas industry has said about its eagerness and ability to undertake massive new development of America's offshore resources. Just 20 companies bid on 191 offshore tracts covering 1.1 million acres, and 80 percent of those tracts received a single bid. More than 3,700 tracts covering 21 million acres received no bids at all. ConocoPhillips, ExxonMobil and BP combined to submit 71 percent of the bids, while 11 other companies submitted fewer than three bids each.

¹ BOEMRE fact sheet supplied to Minority Staff (9/27/2011)

Previous sales of Gulf leases have also seen very little competitive bidding. In the past 10 sales, dating back to August 2005, Interior put up for auction more than 39,000 tracts totaling almost 211 million acres.² Of these, just 3,600 (totaling almost 20 million acres) received bids—not even 10 percent of the tracts offered—and the average number of bids on those tracts was just 1.5 bids. In the auction just before the BP spill, 77 companies submitted 642 bids on 469 tracts covering more than 2.4 million acres. More than 6,400 other tracts offered for sale received no bids. Of the tracts sold, 75 percent (including the most expensive) received only one bid.³

The story is similar in the Arctic. There were more than 5,200 tracts offered in Beaufort Sea lease sales held in 2003, 2005, and 2007. Not even 250 of these tracts received bids. In the 2007 sale, six companies bid on 92 tracts, with only three instances of multiple bids.⁴ And in the 2005 sale, just four companies bid on 121 tracts without a single instance of multiple bids.⁵

Because there is such little competitive bidding, Interior's Bureau of Ocean Energy Management (BOEM) provides a check to ensure the government and the American people receive fair value. Earlier this year, Interior raised the minimum required bid for deepwater tracts from \$37.50 an acre to \$100 an acre. However, even if bids meet or exceed this minimum required amount, they may be rejected. Companies operating in the Gulf are required to provide BOEM with data they have gathered to assess the value of offshore reserves. At the conclusion of an auction, BOEM reviews this information to determine whether high or single bids are adequate. BOEM rejects bids it finds are too low and resells the tracts at a subsequent auction. Such tracts typically fetch higher prices the next time around (because rejections alert the market of a tract's value), but less than 5 percent of tracts are rejected.

As the Ranking Democratic Member of the Committee on Natural Resources, which has legislative and oversight jurisdiction over the Department's leasing activities, I am interested in whether regulatory, legislative, or other reforms might be needed to help maximize the potential for more competitive bidding for leases to drill on the public's lands, and whether BOEM is doing everything possible to effectively ensure that the taxpayers realize a fair value in lease sales. To help me and other Members of the Committee assess these issues, I ask that you please provide a written response to the following questions and provide the following requested information:

1. Why is there so little competitive bidding in offshore lease auctions? Would it be preferable to have more competitive bidding? Why or why not?

² For Gulf lease sale stats, see http://www.gomr.boemre.gov/homepg/lseale/swiler/Table_2.PDF.

³ See BOEMRE Central Gulf of Mexico Lease Sale 213 Information at <http://www.gomr.boemre.gov/homepg/lseale/213/cgom213.html>.

⁴ See BOEMRE Alaska OCS Region Lease Sale 202 Information at http://www.alaska.boemre.gov/lease/hlease/Bid_Recaps/RecapSale202.pdf.

⁵ See BOEMRE Alaska OCS Region Lease Sale 195 Information at http://www.alaska.boemre.gov/lease/hlease/Bid_Recaps/Recap195.pdf.

2. Economists who have studied auction formats have advised the government in other contexts to use multi-stage auctions that are designed to encourage competitive bidding. The Federal Communications Commission (FCC), for example, uses a simultaneous multiple-round auction format, conducted through the Internet, for selling electromagnetic spectrum. Bidders first simultaneously submit sealed bids for spectrum licenses. High bids (and high bidders) are then announced at the conclusion of this first round of bidding, and after a set period of time, the auction moves on to a second round in which bidders have an opportunity to beat the high bids from the first round. To do this, they must meet (or beat) a minimum required bid that exceeds the previous high bid by a predetermined percentage or increment.⁶ This process is then repeated until no new bids are received. BOEM is now considering auction formats for selling offshore wind leases,⁷ and in December asked for public comment on a format like that used by the FCC for spectrum.⁸ Notably, BOEM is not considering a format like that used for offshore drilling lease sales. Why is that? Does Interior believe that any of the auction formats under consideration for offshore wind would generate more competitive bidding for offshore drilling lease sales? Why or why not?

3. I am interested in whether a spectrum-like auction format would work for offshore lease sales. One problem in offshore lease sales is the number of tracts put up for auction—it may be difficult for bidding companies to assess the value of several thousand tracts. A multi-round auction could provide a signal to the market about which tracts are valuable and worth investigation. As noted, tracts that are re-auctioned after BOEM has rejected a bid typically fetch higher prices because companies are alerted that others have found such tracts valuable. In a multi-round auction, the number of tracts would be reduced to a far smaller number after the first round—that is, tracts receiving no first-round bids would be eliminated from the sale. Companies could then review and investigate the tracts that received bids and potentially submit higher bids in the next round of bidding. They could even bid on tracts they did not bid on in the previous round. The Outer Continental Shelf Lands Act (OCSLA) directs that auctions for offshore leases be conducted by sealed bid, but it does not otherwise specify an auction format. Under OCSLA, could BOEM choose to hold a multi-round auction in which high bids are disclosed after each round (perhaps withholding the identities of high bidders, if necessary)? If so, would BOEM consider testing such a format in a future offshore lease sale to see how it works? Why or why not?

⁶ For a description of how bid increments are determined, see <http://wireless.fcc.gov/auctions/data/papersAndStudies/SmMethFactSheet.pdf>.

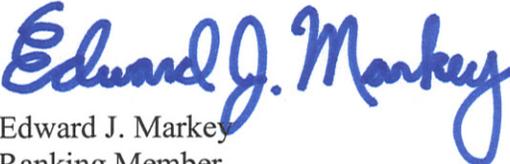
⁷ A description of formats under consideration is available at: <http://www.boem.gov/Renewable-Energy-Program/Regulatory-Information/Renewable-Energy-Auction-Formats.aspx>.

⁸ 76 Fed. Reg. 76174 (Dec. 6, 2001)

4. Companies regularly and carefully review their performance in offshore lease sales. In particular, they look back after exploration and development has occurred to see if they overbid, if bids were on target, or if tracts out-performed bid expectations. Such reviews help guide and improve future bidding. Does Interior regularly conduct retrospective reviews of its performance in evaluating bid adequacy, and if so, how are such reviews conducted? How often do tracts produce greater value than Interior expected in its evaluation of bid adequacy? And has Interior improved its accuracy over time? Please provide the results of any reviews conducted over the last 10 years of Interior's performance in evaluating bid adequacy.
5. It is generally thought that sealed-bid auctions are less susceptible to collusion than live auctions, but collusion can still occur and the lack of competitive bidding raises concerns. The BOEM Regional Director with jurisdiction over a lease sale "may identify an unusual bidding pattern at any time during the bid review process, but before a tract is accepted," according to DOI procedures for determining bid adequacy.⁹ Does BOEM analyze lease sale data to check for unusual bidding patterns that might indicate possible collusion or other anti-competitive behavior? If so, please describe the process for such reviews; how often they occur; any instances where unusual bidding patterns were detected; any instances where BOEM determined collusion or other anti-competitive behavior occurred; and any actions taken by BOEM or its predecessor agencies in response.

Thank you for your assistance in responding to this request. I ask that you please provide this information within 15 days of receiving this request. If you are unable to provide a full and complete response within this timeframe, I request that you provide an interim response which contains such information and analysis as you are able to provide, and which indicates when I can expect to receive a full and complete response. Should you have any questions, please contact Reece Rushing of the House Natural Resources Committee Democratic staff at 202-226-4627.

Sincerely,



Edward J. Markey
Ranking Member
Committee on Natural Resources

⁹ See BOEMRE "Summary of Procedures for Determining Bid Adequacy at Offshore Oil and Gas Lease Sales" at <http://www.gomr.boemre.gov/homepg/lseale/174/FMV174-3.PDF>