Department of Planning and Budget
2010 Fiscal Impact Statement

1. **Bill Number:** SB601

   House of Origin __ Introduced _X_ Substitute _X_ Engrossed

   Second House __ In Committee __ Substitute __ Enrolled

2. **Patron:** Wagner

3. **Committee:** Finance

4. **Title:** **Royalties from offshore drilling.**

5. **Summary:** This bill requires that 70 percent of any revenues and royalties paid to the Commonwealth as a result of offshore natural gas and oil drilling shall be deposited to the general fund, 20 percent of revenues are to be appropriated to the Virginia Coastal Energy Research Consortium and 10 percent of revenues are to be appropriated to the localities of the Commonwealth for improvements to infrastructure and transportation.

6. **Fiscal Impact Estimates:** Preliminary.

7. **Budget Amendment Necessary:** No.

8. **Fiscal Implications:** This bill apportions revenues and royalties received by the Commonwealth from offshore drilling for natural gas or oil. While this bill does not directly generate or expend any resources, it anticipates that these resources will be received.

   According to the Department of Mines, Minerals and Energy (DMME), the following actions on a federal level would need to align for Virginia to receive royalties from offshore drilling:

   (i) The Secretary of the federal Department of the Interior is scheduled to decide in the summer of 2010 whether to move ahead with offshore oil and gas leases in Atlantic waters under the federal Minerals Management Service's (MMS) 2007-2012 offshore oil and gas leasing plan. The Secretary would have to decide affirmatively to move ahead for any royalties to be received. The MMS' five-year plan includes the proposed Lease Sale 220 in Virginia waters.

   (ii) The MMS has indicated that the proposed Lease Sale 220 may not occur at the current intended date of November 2011, because the process to complete the environmental impact assessments and public comments may go beyond the scheduled November 2011 sale date.

   (iii) Federal authority under the Outer Continental Shelf Land Act would have to be granted to allow states to share revenue from offshore drilling (other than for the Gulf of Mexico and Alaska, there has not been any federal authority granted for revenue sharing for offshore drilling); it is unclear whether revenue-sharing for states on the Atlantic coast will be allowed by Congress.

(iv) Virginia has remained in the MMS' 2007-2012 offshore oil and gas leasing plan, and would have to be a part of future leasing plans.

(v) Companies would have to respond with interest to any offering of a lease. Companies did respond with interest to the November 13, 2008, Call for Information and Interest/Nominations and Notice of Intent to Prepare an Environmental Impact Statement issued by MMS. Companies would have to bid on blocks (geographic divisions of offshore area) under any MMS lease offering and develop the lease through to production.

In addition, there are other uncertain factors to consider as to if, and when, any revenue could come to Virginia from offshore drilling. These uncertainties include: (1) the amount of gas and oil, that exist off the Atlantic coast, (2) the worth of any oil or gas deposits, and (3) should revenue sharing come to the Atlantic coast, the question as to how much will be allowed, and how that portion will be shared with other states. Further insight into each of these uncertainties is explored, below:

(1) Of the area of Virginia's coast proposed for the lease sale for which the MMS has issued a call for information, MMS estimates that 130 million barrels of oil and 1.14 trillion cubic feet of gas (Tcf) could exist in the drillable 2.9 million acre zone that covers water depths ranging from 100 feet to over 10,000 feet. However, the MMS acknowledges that these estimates were generated based on old data, as the last oil and gas drilling activity offshore of the Atlantic coast took place in the late 1970s and early 1980s. Therefore, while these are the best estimates that exist, both DMME and MMS emphasize their high degree of uncertainty.

(2) The price of oil has ranged drastically recently, from \$145/bbl in the summer of 2008, to as low as \$36/bbl in early months of 2009, to the current price of \$75/bbl. Natural gas prices have followed a similarly drastic path, ranging from \$13/thousand cubic feet in the summer of 2008 to \$5/thousand cubic feet now. It is unknown what the market values will be for these commodities if there are any recoveries from the Atlantic in future years.

(3) DMME reports that, based on the MMS prediction of economically recoverable resources in the area, it is possible to estimate the level of revenues to the federal government, but not to Virginia, as it is unsure what percentage of revenue sharing, if any, might be authorized for states. Currently, there is no revenue sharing for the Atlantic coast, but in the Gulf of Mexico, 37.5 percent of revenue generated from new leases since 2006 is shared with all coastal states, based on a formula taking into account the distance of individual revenue-generating leases from each eligible state.

Assuming that all uncertain factors to drilling are removed, and applying rough estimates for the uncertain factors set-out above, it is possible to calculate very high-level assumptions about any possible future revenue.

While it is difficult to accurately predict the price of energy in the distant future, considering the steady upward trend in the price of oil and natural gas over the previous 10 years, DMME suggests a future average price of $90.0/barrel of oil and $9.5/thousand cubic feet of natural gas is the best estimate available. Utilizing these price estimates, and applying the MMS estimate of the presence of 130.0 million barrels of oil and 1.14 Tcf of natural gas off of the Atlantic coast, the potential value of oil existing off the Atlantic coast is $11.7 billion, and of natural gas, $10.83 billion, for an estimated total of $22.53 billion.

From this rough estimated total, the federal government could collect royalties, which DMME reports is typically one-sixth of the value of production for offshore leases. Assuming the federal government does grant revenue-sharing for Atlantic coastal states, and that it does so at a level similar to that of the Gulf Coast States, all Atlantic coastal states would share 37.5 percent of the federal government's one-sixth royalty collection. Assuming the MMS data is accurate in its estimation that these drilled resources are in closest proximity to Virginia, Virginia may receive a higher share of the shared portion of the federal government's one-sixth share. For projection purposes, DMME roughly estimates that Virginia could receive 80 percent of 37.5 percent share of revenue collected, or 29.6 percent of the total royalty.

At 29.6 percent of the total royalty, according to the above assumptions, it is possible that Virginia could receive a total of $1.13 billion in revenue. Spread out over the lifetime of production, estimated at 20 to 30 years, if all these assumptions are accurate, this could mean a revenue of $37.7 million to $56.5 million a year for the life of production.

Upon collection of these revenues, this bill specifies that 70 percent of these revenues are to be deposited to the general fund for appropriation by the General Assembly. According to the revenue division outlined by this bill, this may result in as much as $26.4 million to $39.6 million per year being deposited to the general fund for the life of production. Additionally, the bill specifies that 20 percent of revenues are to be appropriated to the Virginia Coastal Energy Research Consortium and 10 percent of revenues are to be appropriated to the localities of the Commonwealth for improvements to infrastructure and transportation, for an estimated total to for each designation of $7.5 million to $11.3 million and $3.8 million to $5.7 million, respectively, for the life of production.

9. **Specific Agency or Political Subdivisions Affected:** Department of Mines, Minerals and Energy, Virginia Coastal Energy Research Consortium, localities.

10. **Technical Amendment Necessary:** No.

11. **Other Comments:** This bill is similar to the substitute version of HB756.

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