Regulation Review

Offshore Drilling Blowout Prevention Rule

APRIL 15, 2015

The Department of the Interior (DOI) recently released a proposed rule that seeks to update requirements for well-control equipment known as blowout preventers (BOP). The proposal would implement increased levels of “oversight over the design, fabrication, maintenance, inspection, and repair of critical equipment.” DOI based its standards off of findings made in the aftermath of the Deepwater Horizon spill. The unofficial, pre-publication version of the proposal is 264 pages.

BREAKDOWN

- Compliance Costs: $883.2 Million
- Testing Savings: $1.54 Billion
- Net Savings: $656.6 Million
- Paperwork Burden: 16,753 new hours

ANALYSIS

While the rule’s new requirements do bring substantial direct compliance costs, one procedural tweak essentially creates net savings on the cost-benefit ledger. This adjustment would move “workover” and “decommissioning” operations BOP testing from 7-day intervals to 14-day intervals. This would harmonize such testing procedures with the schedule for “drilling and completion operations.” This adjustment potentially saves drilling operations time in terms of both preparing for tests and restoring the otherwise forgone productivity during testing periods. DOI estimates that such a shift provides $1.5 billion in cost savings over a 10-year period. It is also important to note that, due to the learning curve from the proposal’s other compliance requirements, the first year will see net costs of nearly $11 million.

Assuming these estimated savings are accurate, this could be an example for other agencies in how simple, yet significant, adjustments can affect the overall balance of a rule. It is certainly important for this proposal because without these time savings, its alternative cost-benefit calculations are in the red. Two other potential benefit options DOI posits include the reduction in either oil spill risk or rig worker fatality risk. The agency provides benefit estimates in a range of 0 to 20 percent risk reduction for either category. However, even at the 20 percent level for both benefit classes, a cost-benefit ledger without the time savings produces a 10-year net cost of nearly $120 million.

Although DOI estimates net cost savings, in the Regulatory Flexibility Act (RFA) analysis, the agency does designate concede that it would “have a significant economic impact on a substantial number of small entities.” Interestingly, DOI does include actual thresholds for this designation. A ‘‘substantial number” is when the “number of small entities impacted by the rule is equal to or exceeds 10 percent of the relevant universe of small entities.” A ‘‘significant economic impact’’ is “when the total annual cost associated with the rule is equal to or exceeds 1 percent of annual revenue.” Many other agencies generally do not provide such clear, quantified definitions. DOI estimates that small entities make up 69 percent of the “relevant universe,” and face cost-to-revenue figures as high as 2.78 percent.

Considering these drills are offshore, it is difficult to provide a clear, state-based geographic breakdown of which areas face the highest burdens. However, using data for the North American Industry Classification System (NAICS) codes 211111 (Crude Petroleum and Natural Gas Extraction) and 213111 (Drilling Oil and Gas Wells), one can better illustrate what DOI’s per-entity estimates mean to most drilling rigs’ bottom lines. DOI estimates that, thanks to 25 separate requirements, the average annual per-entity costs will be $678,388.

According to the Bureau of Labor Statistics (BLS), the average annual wages for all workers in NAICS codes 211111 and 213111 are $88,960 and $55,440 respectively. Thus, the per-entity costs essentially equal the costs of 7.6 employees in the former and 12.2 in the latter. According to Census data, the percentages of establishments with less than 20 and less than 10 employees are as follows:

NAICS Code	**Percentage with <20 Employees**	**Percentage with <10 Employees**
211111	87.6%	78.3%
213111	71.7%	60.8%

The BLS and Census data also necessarily include land-based drilling operations. However, the general trend would suggest that for most affected entities, their individual cost burden under this proposal equates to most of the costs they face – in some cases even more – to staff just one “establishment.”

This proposed rule appears to have some positive steps on a regulatory best practices level. While the new compliance costs are substantial, DOI has found a way balance them by refining past requirements to find cost savings. Additionally, the agency provides a reasonable RFA analysis that includes clear metrics of what constitutes “a significant economic impact on a substantial number of small entities.” These are both worthwhile, though often elusive, goals for other agencies.