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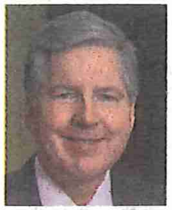
OPINION

ENERGY TRANSITION IS THE NEW LANDSCAPE FOR HOUSTON'S OIL AND GAS INDUSTRY



Bruce D. Oakley

Blake A. Jenkins

BY BRUCE D. OAKLEY & BLAKE A. JENKINS
Guest contributors

As Houston-based energy companies watch President Joe Biden's first six months to get a sense of what challenges and opportunities lay ahead, one thing is clear: the new administration has a laser focus on combating climate change. The question for oil and gas companies is how the president's environmental agenda might shape the energy industry's present and future.

First, the present impact: perhaps the starkest policy shift came just seven days into the president's term when on Jan. 27, President Biden signed an executive order banning new leases on federal lands. Federal lands encompass roughly a quarter of U.S. oil and gas production, predominantly from offshore operations. But the impact of this moratorium is likely to be muted in the near term. More than 30 million federal land acres were already under lease before President Biden's order, giving energy companies bandwidth for future operations. Furthermore, the timeline for offshore drilling requires as much as 10 years of lead up before spudding a well. It would take a sustained federal leasing ban to materially impact the deepwater industry.

Still, even for existing federal leases, operators report a slow down in the process for obtaining new permits. That reduced speed is likely just a portent for changes to come.

The future impact of President Biden's policies holds the greatest weight. Multiple factors suggest a focused movement toward the promotion of renewables over fossil fuels. Part of President Biden's Jan. 27 executive order included a directive to the Department of the Interior to take steps toward doubling offshore wind production by 2030. The president has also directed government agencies to move toward ending fossil fuel subsidies by fiscal year 2022. On Feb. 26, the Biden Administration announced the Social Cost of Carbon (SCC) would be $51 per metric ton, marking a dramatic reversal in the federal government's valuation of the impacts of climate change. That matters because the SCC metric has historically been used to justify Department of Energy (DOE) actions and serve as a standard for state agencies who look to the federal government to quantify the cost of carbon. Indeed, the DOE has announced a multitude of funding opportunities or requests for information during the administration's first six months tailored to meet the president's 2035 target of decarbonizing the electricity grid and the 2050 target of a carbon-free economy. Moreover, all of this emphasis on renewables could weigh on the cost of oil, as markets account for the worldwide demand for a smaller carbon footprint.

These trends place pressure on oil and gas companies to adapt to the changing landscape. Beyond cost-cutting, energy companies are likely to shift capital investments into a less carbon-creating energy portfolio. Unlike the post-2014 market, investors in a post-Covid world could choose to use their resources to take advantage of the net-zero headwinds rather than diving back into traditional oil and gas investments. Energy companies can start to leverage this trend by directing their own research and growth toward renewables so that investors are enticed to be a part of that transition.

Of course, such opportunities may be more easily realized by upstream companies, while drilling companies could face a greater challenge in adapting to a world focused on renewable energy. The good news for drillers is that, in the near term, demand for petroleum is predicted to increase as the world comes out of the pandemic. Regulations affecting shale plays could also shift the focus toward deepwater drilling.

Looking further out, any transition away from petroleum will take a number of decades.

The bottom line is that the Biden Administration is likely to only increase speed in the direction it has started. Despite the challenges, energy companies can foresee and take advantage of the opportunities the transition to carbon reduction affords.

Bruce D. Oakley is the managing partner and Blake A. Jenkins is a senior associate at the Hogan Lovells' Houston office; they both practice energy litigation.