Minutes

Indian Oil Valuation Rule - Public Workshop
Oklahoma City, Oklahoma
March 8, 2005

As announced in the Federal Register on February 22, 2005, the Minerals Management Service (MMS) held a public workshop in Oklahoma City, Oklahoma, on March 8, 2005, concerning the valuation of crude oil produced from Indian oil and gas leases.

Eight industry and six Indian representatives attended the Oklahoma City workshop. A summary of the comments received at the Oklahoma City workshop is outlined below.

In the introductory remarks at the workshop, MMS reiterated that the February 1998 proposed Indian oil valuation rule and the January 2000 supplementary proposal have been withdrawn because of the passage of time and market changes that have occurred since their publication.

The MMS also reiterated that the agency has begun a new rulemaking process regarding the royalty valuation of crude oil produced from Indian oil and gas leases. Comments from the Oklahoma City, Oklahoma, Albuquerque, New Mexico, and Billings, Montana, workshops will be considered in the new rulemaking process.

Should MMS adopt certain Amendments to the Federal Oil Valuation Rule in the New Indian Oil Valuation Rule?

As stated in the Federal Register notice announcing the public workshops, one of the workshop goals was to obtain public comment on whether certain amendments to the Federal oil valuation rule promulgated in May 2004 should be adopted in the new Indian oil valuation rule—for example, using New York Mercantile Exchange (NYMEX) prices adjusted for location/quality and transportation costs for oil that is not sold at arm's-length, and using 1.3 times the Standard & Poor's (S&P) BBB bond rate as the rate of return when calculating non-arm's-length transportation costs.

Indian comments:

- The Indian representatives at the Oklahoma City workshop stated that they were concerned about the lack of Indian representation at these public meetings.

Industry comments:

- In general, the industry representatives supported using an approach that provides certainty and simplicity, such as index formulas similar to the current Indian gas valuation rule. The index price methodology in the current Indian gas valuation rule enables tribes to opt out of index-based valuation when leases are located in an index zone. Industry suggested that MMS consult with its Royalty-in-Kind group which has performed research using index pricing.

- Industry representatives generally supported using a different approach for certain areas, depending on market conditions; e.g., using NYMEX for Oklahoma Indian leases and evaluating other market center prices or other measures of value for other Indian reservations from which oil does not flow to a market center.

- Industry representatives supported using the 1.3X BBB bond rate and stated that this rate was a compromise in the Federal oil valuation rule; although they believed the rate should be higher.

- Industry representatives were concerned about the administrative burden (reporting efforts and administrative forms filing for transportation allowances) that were required or proposed in previous proposed Indian oil valuation rules. Industry representatives were encouraged by the consideration of adopting provisions similar to those of the Federal oil valuation rule, and they encouraged adopting a new Indian oil valuation rule that has fewer burdens on industry.

The MMS comments:

- In addition to the announcement of the workshops in the <u>Federal</u> <u>Register</u>, MMS also sent over 100 letters to tribes, allottee associations, and the Bureau of Indian Affairs notifying them about the public workshops. The MMS is holding the workshops to obtain input from tribes and individual Indian mineral owners on how MMS should proceed with the rulemaking.

- In 2000, MMS based the Federal oil valuation rule on spot prices available in industry-wide publications with location differentials in those areas. The MMS then modified Federal oil valuation rule in 2004, to change the valuation under certain conditions from spot prices to a NYMEX-based system to better reflect market changes.

<u>Should MMS use Arm's-Length Reported Values for Production from a Reservation or Other Designated Area when calculating "Major Portion" Prices?</u>

Industry comments:

- Industry representatives were very interested in a simplified approach to calculating major portion prices. They would like to see a mechanism for establishing fair market value to provide certainty and not have administrative burdens up front in the reporting process. In addition, industry representatives did not want the major portion process to require lessees to have to go back to previously reported data and pay additional royalties. They did not support a process which would require MMS to perform an assessment after royalties are initially reported and paid. Industry representatives expressed interest in helping develop an index-based methodology.

<u>Should MMS Collect Information to Use in the Major Portion Calculations to Distinguish the Quality of the Oil (i.e., sweet crude, sour crude, yellow wax, black wax)?</u>

Industry comments:

- Industry representatives supported MMS collecting information to use in the major portion calculations to distinguish the quality of the oil (sweet crude, sour crude, etc.). However, they do not support using the Form MMS-4416, Indian Crude Oil Valuation Report, to collect this information.

- Generally, industry representatives favored MMS performing monthly normalization process when calculating major portion using a current published price.

- Industry representatives hope MMS will define “allowable deductions” in the new Indian oil valuation rule.