STATEMENT OF

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DEPARTMENT OF THE INTERIOR

Before the

SUBCOMMITTEE ON ENERGY AND MINERAL RESOURCES
COMMITTEE ON RESOURCES
HOUSE OF REPRESENTATIVES

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Madam Chairman and Members of the Subcommittee, the Minerals Management Service (MMS) appreciates the opportunity to testify today on its Fiscal Year (FY) 1999 budget request. This request reflects our best assessment of monies needed to carry out critical MMS programs during the upcoming year.

MMS is requesting $222.5 million, which is approximately $14 million more than appropriated to date for FY 1998. The $14 million increase includes: continuation of a proposed $6.7 million FY 98 supplemental for additional manpower and scientific information needed to maintain vigilant oversight of the Outer Continental Shelf (OCS) and provide timely service to industry; and an additional $7.2 million for FY 99 to meet legislative and workload increases (including reengineering initiatives).

In formulating its request, MMS looked closely at its ongoing operations and recently increased responsibilities. The MMS budget request for FY 1999 reflects the need for additional funding balanced against savings gained from past and ongoing efforts to streamline operations and find more efficient ways of doing business.

BACKGROUND

Prior to discussing MMS's budget request in some detail, it is important to put that request into perspective by providing a brief overview of the agency and its programs as well as the benefits derived from those programs.

MMS has two clear missions:

- management of the Nation's OCS mineral resources in an environmentally sound and safe manner; and
- timely collection, verification, and distribution of mineral revenues from Federal and Indian lands.

The OCS mission is carried out by the Offshore Minerals Management (OMM) Program and the revenue collection and distribution mission by the Royalty Management Program (RMP). The Directorates of Policy and Management Improvement and Administration and Budget provide policy and administrative support for the MMS mission.

MMS programs clearly benefit the Nation and protect the public's interests. They contribute significantly to the Nation's energy supply and provide economic benefits and an enhanced lifestyle for the people of the nation:

- From an energy standpoint, MMS currently manages more than 27 million acres of Offshore Federal lands which account for approximately 27 percent of domestic natural gas production and 18 percent of U.S. oil production. To date, the OCS has produced over 120 trillion cubic feet of natural gas and over 11 billion barrels of oil. The OCS is estimated to contain more than 50 percent of our Nation's remaining undiscovered natural oil and gas resources.
- From an economic standpoint, MMS collected and distributed over $6.2 billion to the Federal Treasury, States, Tribes, and Indian allottees in fiscal year 1997, the largest sum it has ever collected in a fiscal year, and $92 billion since 1982. This makes MMS the manager of one of the Federal Government's greatest sources of non-tax receipts.
- In FY 1997, U. S. citizens benefited from MMS disbursements of over $600 million in revenues to 36 states. This sum is the largest it has ever returned to states, which will be used for schools, roads, and other public works or placed in general funds and used as needed. Additionally, over $1 billion in OCS revenues are deposited each year into the Land and Water Conservation and National Historic Preservation Funds to acquire, restore, and create parks, rivers, wildlife preserves, wilderness areas, and recreation facilities, and to restore and preserve national historic sites for future generations. Since 1982, MMS has distributed $2.2 billion to 29 Indian tribes and 20,000 individual mineral owners (allottees).

MMS's programs and priorities are driven by its commitment to operating in the collective best interests of its many customers, including U.S. taxpayers, States, Indian Tribes and allottees, and the energy industry. Vitally important to this commitment is obtaining fair market value for resources removed from lands under our jurisdiction. Significant investments are proposed for both the Offshore Program and the Royalty Management Program to ensure that MMS remains capable of fulfilling its core regulatory responsibilities and continues to provide the high levels of service its constituencies have come to expect. These investments, which are proposed both in the context of a 1998 supplemental request and the 1999 President's Budget, are modest compared to the revenue return they will generate. Furthermore, these investments will be fully covered with increased offsetting receipts, thereby allowing MMS to reduce its direct appropriations significantly.

CHALLENGES AND ACCOMPLISHMENTS

Although MMS is a relatively young agency it continually changes to respond to the changing business and governmental climate. Many of the changes in MMS organizations and functions are internally initiated, designed to improve program efficiency and effectiveness. Other changes are in response to an array of external forces including industry, States, local governments, Tribes, Indian allottees, and environmental and public interest organization's needs and desires. Arguably, the most dramatic changes are being made in response to external driving forces challenging MMS everyday to keep pace. These challenges come from many sources:

- ✓ Evolving Offshore Technology
- ✓ Changing Energy Markets
- ✓ Emerging Global Markets
- ✓ Compelling Safety and Environmental Challenges
- ✓ Transforming Legislation
- ✓ Increasingly Sophisticated Constituencies
- ✓ Advancing Information Technology
- ✓ Challenging Governmental Initiatives

Evolving Offshore Technology. The OCS industry is employing new technologies and moving farther offshore into deeper waters. As industry makes this important transition, MMS faces the challenge of keeping pace with the new technology and adapting its regulatory regime to satisfy its Congressional mandate and serve as an effective steward of the public resources.

Deepwater operations differ from those conducted in shallow water in that they tend to be:

- Significantly more remote.
- Subject to different environmental conditions.
- Technically more sophisticated.
- Productive at much higher flow rates.
- Typically subject to different economic determinants.

Changing Energy Markets. Over the past several years, energy markets have undergone a significant transformation. Many factors have contributed to this change:

- Deregulation of natural gas production and open access to transportation facilities have created a new gas-marketing environment.

- Invalidity of posted prices historically used to value crude oil production.

- A shift in energy markets from regulatory-based to almost completely market-driven.

Emerging Global Markets. Today's offshore natural gas and oil industry is global in scope. A growing number of nations are opening up their offshore areas to private investment. Many of the companies who operate in the U.S. OCS also operate overseas, thereby spreading their investment dollars between local and international opportunities. The U.S. companies who wish to work abroad want to make sure that when foreign governments implement their rules, a level playing field is established. The concern is that other nations do not exercise undue influence effectively limiting U.S. access to these offshore resources.

Interdependent nations, those with emerging or developed natural gas and oil programs, have a growing interest in establishing international standards for offshore natural gas and oil operations. The expanding scope and effects of international and regionally developed environmental and operational standards on the activities of the domestic industry require increased monitoring.

Compelling Safety and Environmental Challenges. The move into deep water and overall heightened industry activity have increased both the level and complexity of monitoring OCS operations. The number of operators has grown over the past several years from approximately 100 to over 130. Some of these operators are not as experienced and require more oversight. This is coupled with the fact that the offshore industry downsized significantly before the recent increase in deep water activity, which reduced the skilled labor pool. The presence of workers without much offshore experience is placing an added burden on the inspection and compliance program.

Little is known about the deep ocean habitat and the effects of natural gas and oil development upon that habitat. Addressing these information needs is essential to decisionmaking for environmentally sound development.

Transforming Legislation. Over the last few years Congress has passed new legislation and amended existing statutes to reflect constituent's concerns, changes in the oil and gas industry, and changes in the way government should work. The following include some of the more significant legislative actions.

> ***Royalty Simplification & Fairness Act (RSFA):*** Enacted August 13, 1996, RSFA is the first major legislation affecting royalty management since the Federal Oil and Gas

Royalty Management Act of 1982. It challenged MMS to make substantial changes and introduced a host of new requirements including:

- Payment of interest on all Federal royalty overpayments.
- Specific royalty reporting standards for Federal leases and pooling agreements.
- New reporting options for marginal properties.
- New payment liability standards and statute of limitations for Federal leases.

OCS Deep Water Royalty Relief Act (DWRRA): Deepwater royalty relief was initiated to encourage development in the frontier deepwater areas of the Gulf of Mexico. In November 1995, the DWRRA became public law. MMS implemented interim rules less than six months after enactment, and published final regulations in January. Operators, on certain leases, are now able to submit proposals for royalty relief which then must be carefully reviewed by MMS within 180 days.

Oil Pollution Act (OPA) Amendments: Changes in OPA now allow for the amount necessary to meet an offshore facility's oil-spill financial responsibility requirement to be based on the facility's location and the amount of oil that could be released in an oil spill. It also requires MMS to oversee oil spill contingency planning and financial responsibility requirements in State, as well as, Federal waters. MMS will publish a final rule implementing these changes this spring.

Sand and Gravel: An October 1994 amendment to section 8 (k) of the Outer Continental Shelf Lands Act (OCSLA) expanded the Secretary of the Interior's authority for conveying rights to Federal OCS sand, gravel and shell resources. Public work projects, such as restoration of beaches, have created new demands for MMS under this legislation.

Increasingly Sophisticated Constituencies. The MMS has a very active and committed constituency spanning the cultural and economic breadth of this country. A sampling of MMS's daily activities have it involved with:

- Tribes and Indian allottees who receive the mineral revenues generated from the leasing and production of leaseable minerals from Indian lands;
- States that receive a share of mineral revenues from onshore and 8(g) offshore activities;
- Industry as it strives to identify, lease, explore, produce, pay and account for significant natural gas and oil resources from the OCS;

- Coastal states, environmental and citizen groups seeking assurance that all due caution has been exercised in the development of the OCS; and

- Other government officials that oversee the collection and distribution of royalties to the U.S. Treasury, and other matters.

Advancing Information Technology. Twenty-five years ago, hand-held calculators that added, subtracted, multiplied, and divided cost $200. Ten years ago, personal computers were rare in the workplace, and two way radios with relay stations were state-of-the-art. Five years ago, cellular phones were in their infancy, and e-mail was just becoming universally available. Today, the OCS program uses 3-D seismic imagery to "see" fields and to estimate their size, production rates, and the best drilling methods for maximum resource recovery. RMP collects and distributes billions of dollars per year electronically. MMS has expanded access to information of interest to constituents by making it available on its Internet Homepage. Tomorrow . . . .

Challenging Government Initiatives. The National Performance Review (NPR) is a long-term White House initiative to make government work better, but at less cost. Working better means delivering better service to the American public; costing less means accomplishing this goal with fewer staff, tightly controlled budgets, and more efficient operations. To achieve these NPR goals, the President and Vice President challenged the Federal Government to reinvent itself; that is, to improve public confidence in Government operations and to succeed in a balanced budget world. Real reinvention is required -- nibbling around the edges to improve processes and services will not accomplish the goal.

Although daunting, MMS is committed to this initiative and as it meets each challenge it is leaving a string of successes and accomplishments in its wake. To date, we are the recipient of two Vice Presidential Hammer Awards. Our first award recognized our efforts to introduce Plain English into government paperwork, particularly regulations -- an idea since embraced by much of government.

This past year MMS was honored for implementing a series of over 20 innovative achievements during the past two years that improve customer service or streamline operations. A sample of some of the innovations announced during FY 97 are:

- 50 Years of Gulf of Mexico Paleontological and Production Data is available on CD-ROMS.
- MMS Issues New Well Naming and Numbering Standards.
- MMS Implements New Audit Tracking System.
- MMS Offers New, Free Electronic Production Reporting Software.
- MMS Improves Customer Service (RMP consolidates information from 4 separate work areas so that customers can resolve several issues with one call).

Also, during this past fiscal year, MMS published its strategic Plan for 1997-2002. It was developed with input from those who work in the agency and those who work with the agency. The result is a strategic plan with goals and objectives that are clear, measurable, and relevant to MMS's fundamental mission. The plan also establishes performance measures that are an effective means of gauging our success in meeting our goals. It will keep MMS focused on its mission and objectives.

Now I would like to discuss each of the Programs in more detail.

OFFSHORE MINERALS MANAGEMENT PROGRAM

The Offshore Minerals Management (OMM) Program, headquartered in the Metropolitan Washington, D.C. area, with regional offices in Alaska, California, and Louisiana, oversees all OCS minerals activities, from initial lease offerings through exploration, development, production and lease abandonment. More than 27 million acres on the OCS are under active lease.

This program is experiencing a phenomenal rise in activity:

- The Gulf of Mexico (GOM) OCS is currently one of the most exciting exploration and development areas not just the Nation, but in the world, experiencing record levels of exploration and development activities.

- The Beaufort Sea area offshore Alaska is also receiving renewed interest and experiencing increased activity which will likely lead to the first federal offshore production.

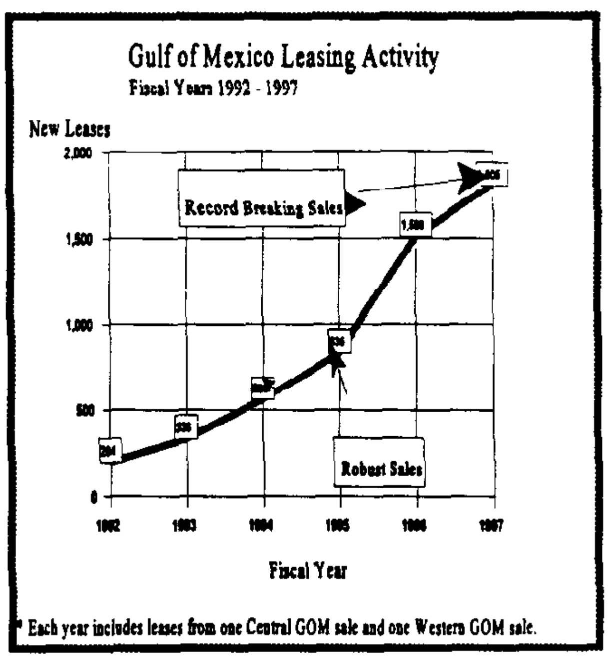
- Off the coast of California industry plans to decommission three of the deepest and largest conventional platforms ever to be removed from the world's oceans. At the same time, there is ongoing production and an effort is underway to determine the best way to pursue development of the remaining existing leases--leases that may hold resources as great as one billion barrels of oil.

- With the enactment of sand and gravel legislation, MMS has received numerous requests to use OCS sand for beach and wetlands restoration projects. This winter's coastal storms will likely generate more activity.

Gulf of Mexico. Advances in technology, along with legislative incentives and world class oil fields, are producing participation in oil and gas lease sales in the GOM that keep exceeding all expectations. During the past two fiscal years four record-breaking sales occurred in the GOM. These four record sales produced over \$2.4 billion in bonuses as compared with \$0.7 billion from the previous four sales. The last record sale, the Western GOM Sale 168, held in August 1997, was 33 percent larger than the Western Gulf sale held a year earlier. Historically, the Western Gulf sales are smaller than the Central Gulf sales. However, this last Western Gulf sale set a record for the largest number of tracts bid on in ultradeep water (800+ meters). Accompanying this has been a record pace in drilling wells and installing new pipelines. Workload will continue to increase as MMS addresses industry's requests to explore and develop these leases.

Alaska. MMS is reviewing the development and production plan for the Northstar project off the coast of Alaska. This project promises the first oil from the Federal OCS off Alaska. Production is expected to commence in 1999 or 2000. Additional development should follow as the completion of pipeline infrastructure makes development of more projects financially viable. Another plan for development of the Liberty prospect is also currently under review. Technical and environmental challenges of working in the Arctic stress the need for careful oversight to ensure safe operations.

California OCS. Industry plans to remove some California OCS platforms shortly after the year 2000, which include the deepest and largest structures ever removed from the world's oceans. The MMS and the California State Lands Commission have worked closely to develop a plan for the environmentally safe removal of offshore platforms. This is an issue that has captured the attention of the international community because of interest in international platform removal guidelines and the technological complexity of the undertaking. California Offshore Oil and Gas Energy Resources (COOGER) Study: The COOGER study is an unprecedented cooperative research effort, planned and managed through a consortium of State and local government agencies, the oil and gas industry, environmental groups and MMS. The COOGER study addresses long-standing questions regarding the ability of local communities and public agencies to deal with the cumulative onshore issues associated with offshore development. As partners, key stakeholders can develop a broader understanding of the possible future oil and gas development and the associated onshore constraints which may limit how and when offshore development occurs. We anticipate the study to be completed in mid 1998.



Sand & Gravel. Demand for OCS sand is rising due to continued State concerns over coastal erosion and the environmental concerns involved in using nearshore sands. There is also a growing need for offshore sources of construction aggregate material. Amendments to sections 8(k) and 20(a) of the OCSLA in 1994 provide for negotiated agreements in lieu of competitive bidding for obtaining OCS sand, gravel, or shell resources for certain public works projects. The MMS and coastal States use a cooperative approach toward mineral resources development questions. States and the MMS engage in jointly funded cooperative studies to identify the need for, and availability of, OCS sand resources for beach nourishment purposes. When warranted and when funds are available, environmental studies are developed and conducted within the identified sites. Both types of studies provide the information base needed for negotiated agreements. No separate funding has ever been provided for these new undertakings.

While the Nation is reaping significant economic and energy benefits from increased OCS activities, MMS is facing many new challenges as a lessor and regulator.

Safety

MMS is committed to ensuring that industry maintain an excellent safety record as the level of activity increases in both amount and complexity. Unless this record is maintained, industry will not be able to go forward with its ambitious plans for the GOM because the public will lose confidence in the integrity of the program. In addition, the Nation will lose the significant contributions that the Offshore Program makes to the economy in the form of revenues and secure supplies of oil and natural gas.

Our commitment to safety in FY 99 includes updating regulations to reflect current best practices, increased training and stepped-up inspections. MMS oversees drilling and production facilities on the OCS using both scheduled and unannounced inspections. To maximize resources, MMS uses different strategies and techniques, which includes random sample and high-risk profile inspections, and cooperative inspections with other organizations. MMS will impose civil and criminal penalties whenever warranted and may go as far as to disbar operators from OCS activities if poor performance is sustained.

Environmental Projects

The commitment to environmental stewardship becomes more challenging each year with the increase in activities at all phases -- leasing, exploration, production, and decommissioning. MMS's environmental processes integrate requirements of the National Environmental Policy Act (NEPA) into planning for OCS oil and gas lease sales, with the commitment to environmental protection continuing throughout the life of each lease. This past year, MMS held a Deep water Workshop and formed a Deep water Subcommittee of its OCS Scientific Committee to help define environmental studies needs for deep water. Information provided by the studies will be used to prepare environmental impact statements and environmental assessments, to develop lease stipulations, and to evaluate plans for exploration, development and oil spill response.

- **Planned Studies for FY 1999**

  GOM Region - Rapid technological advances and recently passed legislation have resulted in a rush to develop both deep water and subsalt oil and gas resources. To meet the information needs created by this new development, the MMS is joining with other Federal, State, and academic institutions in an attempt to provide the information needed in the most cost-effective manner.

  Of special concern are the positive and negative effects of onshore facilities and infrastructure needed to support deep water activities, may have on Gulf coast socioeconomic conditions. A good example of this is the study, "A Socioeconomic Analysis of Port Expansion at Port Fourchon," awarded to document the growth of OCS support activities in the Port Fourchon, Louisiana, area. This study will also develop a model of the economy of the area that will allow the projection of future economic effects of OCS activities. Other studies on these potential impacts and on the potential impacts to water quality, air quality, and wetlands are planned. Our studies are contributing to basic scientific knowledge, as illustrated by the discovery of a new species by MMS-funded scientists -- ice worms that live on gas hydrates in the deep water Gulf.

  Pacific Region - In the Pacific Region, monitoring of the coastal marine environment and onshore socioeconomic impacts will be conducted through partnerships with the State and local governments, and through the Coastal Marine Institutes at the University of California at Santa Barbara. An additional partnership in the Pacific Region with Scripps Institute of Oceanography and the State of California will allow MMS to collect needed information on physical oceanographic processes in the Santa Maria Basin-Santa Barbara Channel area at a substantially reduced cost.

  Alaska Region - Studies in the Alaska Region will be designed to provide information for management decisions associated with the Beaufort Sea and Cook Inlet plans for lease sales, exploration, and development. Physical oceanographic data will be collected, and much-needed research on the fates and effects of oil in the arctic marine environment will be conducted through the CMI at the University of Alaska at Fairbanks. With increased industry interest in the Beaufort Sea, studies of bowhead whales and other subsistence species will be conducted to protect those important mammals.

  Sand and Gravel - The rapidly expanding interest for using sand and gravel resources from the OCS will require environmental studies as coastal States continue to enter into cooperative agreements with the MMS for use of these resources. In addition, there is also interest by commercial firms and local jurisdictions in the use of sand and gravel for construction projects.

International Activities

MMS, as one of the most technologically advanced regulators in the world, continues to expand its collaborative projects with other technologically advanced regulatory countries to promote safe and environmentally sound oil and gas operations, worldwide. There is a growing interdependence among nations with developed oil and gas programs, as well as a need for emerging nations to develop regulatory regimes that facilitate, or at a minimum, do not discourage, investment from foreign companies. Because of its regulatory expertise and its record of environmentally sound and safe operations, MMS is increasingly being called upon to assist and participate in international forums and projects that further our Nation's foreign policy goals. MMS's international efforts focus upon:

- Technical and information exchanges with advanced and emerging nations (e.g., Canada, the United Kingdom, Norway, Russia, and China);
- Providing technical advice to the State Department on a broad spectrum of international activities (e.g., Arctic Council, Convention on the Law of the Sea, London Convention 1972, International Convention for the Prevention of Pollution from Ships, Gore-Chernomyrdin Commission, and negotiations with Mexico regarding the boundary in the "Western Gap"of the Gulf of Mexico) that can affect domestic offshore oil and gas regulatory responsibilities; and
- Participating in regional/international meetings and forums that address the need to integrate sound science into the regulatory process (e.g., a workshop on platform decommissioning and artificial reefs planned with Indonesia, Malaysia and Thailand; a workshop on oil-spill response scheduled by India; a meeting of the Western Hemisphere Oil and Gas Environmental Forum).

ROYALTY MANAGEMENT PROGRAM

While headquartered in Washington, DC, RMP has its primary operations in Lakewood, Colorado, with field offices in Texas and Oklahoma and resident auditors throughout the United States. With sophisticated computerized accounting systems, RMP processes more than 200,000 transactions each month from over 26,000 producing Federal and Indian leases. RMP coordinates its royalty management efforts with MMS's Offshore Minerals Management Program, the Bureau of Indian Affairs, the Bureau of Land Management, the Office of the Special Trustee, the U.S. Forest Service, the Army Corps of Engineers, and the U.S. military. RMP also works closely with State governments, Indian tribes and allottees, and industry to improve overall royalty management.

The Federal Government is the largest mineral royalty owner in the United States. MMS is responsible for ensuring that, on average, over $4 billion in annual revenues from Federal and Indian mineral leases is collected, accounted for, verified, and disbursed to appropriate recipients in a timely manner. In FY 1997, annual revenues exceeded $6 billion. In addition to a broad range of financial services, MMS also pursues a comprehensive compliance strategy that includes an automated verification program to validate the accuracy and timeliness of revenues paid, and an audit program staffed by MMS, State and Tribal auditors. Since the establishment of RMP in 1982, these compliance efforts have resulted in the collection of $2 billion in revenues that would not otherwise have been captured.

The business environment in which MMS administers royalty payments is similar in many respects to private and State land minerals owners. However, in scale of activity, and variety and complexity of lease terms, it is significantly more challenging.

Royalty Management Program Reengineering

An outward focus on dynamic market conditions is needed in today's RMP processes, priorities, and systems. MMS plans to shift to a market-focused business environment by reengineering the royalty management program. Royalty management reengineering is a top priority for MMS for the new millenium. Our objective in FY 1999 is to begin to implement new core business processes and support systems. Although this is largely an internal effort, MMS expects the outcome to have substantial impact on our stakeholders and have involved them in this effort. We expect major improvements and savings by focusing on royalty management from a process rather than a functional perspective. Current royalty management operations are rigidly organized around and focused on functions and tasks and measure performance by outputs, akin to an assembly line manufacturing model. Our reengineering effort focuses on redesigning processes that can yield benefits much greater than attempts to improve the operations within a functional area. Through royalty reengineering, MMS expects to see dramatic improvements in both efficiency and royalty compliance.

Two goals have been established to "stretch" MMS to achieve results that are impossible under current operating processes. These stretch goals are:

- To ensure that royalty recipients will have access to their revenues within 24 hours of the time MMS receives it. Today, it generally takes 30 days to make revenues available; and

- To ensure royalty compliance within three years. This would cut in less than half the time statutorily allowed.

The RMP reengineering team has already completed a thorough review or "map" of MMS's current business processes. This map confirmed what many already knew, the current processes are complicated. MMS plans to vastly simplify those processes. A draft report summarizing this map has been issued presenting proposed alternative processes and their effects. MMS plans to begin prototyping some of these alternatives early this year.

Valuation of Oil and Natural Gas

Complimentary to reengineering, much of this year has been spent wrestling with the need for new MMS valuation regulations that more accurately reflect market conditions, and provide greater certainty and simplicity to royalty payors, the Federal Government, and other Federal mineral revenue recipients. MMS is currently revising valuation regulations for Federal and Indian oil, gas, and other commodities. These new regulations will help ensure that the public receives fair value for its mineral resources. They are intended to simplify royalty payments, make valuations methods reflective of modern market conditions, offer the industry more flexibility, reduce administrative costs, and maintain revenue neutrality.

Implementation of the Federal Oil and Gas Royalty Simplification and Fairness Act (RSFA)

Congress has passed new legislation and amended existing statutes that are bringing considerable change to the interaction of government with the oil and gas industry. The Royalty Simplification and Fairness Act (RSFA), enacted in 1996, challenged MMS to make substantial operational changes and introduce new process requirements, which make reengineering necessary. MMS has made significant progress in implementing RSFA. Over 20 outreach workshops with State and industry representatives have been held focusing on specific implementation areas. To date we have:

- Published an interim final rule regarding lessee/designee payment responsibility.
- Published a final rule expanding the list of delegable royalty management functions to States.
- Begun paying interest to companies who overpay royalties and accepting interest reporting from companies.
- Completed a host of software changes necessitated by RSFA, including reporting taxpayer identification numbers and 1099 reporting.

MMS has several RSFA regulations in progress and we anticipate that at least three RSFA regulations will be published later in 1998:

- ***Marginal Properties Accounting and Auditing Relief.*** This proposed rule would allow reporters to seek accounting, reporting, and auditing relief for their marginal properties in accordance with RSFA requirements.
- ***Interest/OCS Sec.10 Repeal.*** This interim final rule would allow MMS to pay interest on Federal royalty overpayments and make interest charges and payments more equitable between payor and recipient. It also addresses the repeal of OCS section 10.
- ***Self-Bonding.*** This interim final rule would allow payors to self-bond underpayment amounts under appeal with MMS.

Royalty-in-Kind (RIK)

Another important compliment to reengineering, RMP is continuing to pilot programs to take federal Royalty-in-Kind (RIK). MMS has long been an endorser and developer of novel approaches to royalty management, such as exercising its right to take the federal government's royalty share in kind. In fact, MMS conducted an RIK gas pilot in 1995 and performed a 1997 RIK Feasibility Study. Although the results of the 1995 pilot were mixed (revenues were lost), our interest in pursuing RIK continues. The 1997 Study concluded that, if implemented correctly, RIK in some areas could be workable, revenue positive, and administratively more efficient for all parties.

MMS has established a task force to implement three new RIK pilot programs for natural gas production in the Gulf of Mexico, oil production in Wyoming, and 8(g) natural gas production offshore Texas. We expect to have two pilots ready to begin during this calendar year continuing through 1999. These pilots will allow us to test RIK programs without placing over $4 billion in royalty collections at significant risk. For although we are enthusiastic about the prospects of these programs to provide for administrative relief, given our past results, we are cautious to develop a program that is workable for the Federal government without jeopardizing revenues.

Continuous Improvements

Although dramatic changes are expected from the royalty reengineering project, MMS continually works to improve its royalty management processes through simplifying and streamlining and by taking advantage of advances in information technology. For example:

- Studies and experience show that errors in reporting decrease with electronic reporting. MMS provides free electronic royalty and production reporting software to reporters to reduce data entry costs and increase reporting efficiencies. In FY 1997, electronic reporting increased to 78 percent for royalty lines and 54 percent for production lines. The royalty error rate for electronically reported lines has reduced dramatically to 1.4 percent from 7.4 percent for paper reports.

- In FY 1997, 92 percent of collections ($5.6 billion) was received electronically.

- RMP has made information available to its constituents in a timely fashion by posting it to the MMS home page.

- The RMP network has been upgraded to provide state-of-the art telecommunications capabilities to all MMS users nationwide. These enhancements include access to the State and Tribal Royalty Audit Committee Network (STRACNET) which provides States and Tribes direct access to RMP automated systems, the MMS local metropolitan network, and the MMS-wide area network.

Appeals

In the past, it has taken many years to decide some appeals at the MMS level, followed by many years at the Interior Board of Land Appeals (IBLA). Over the last two years, MMS has made substantial strides in eliminating the backlog of administrative appeals, deciding or resolving more than twice the number of new cases received. We now routinely meet the self-imposed 16-month timeframe for MMS decisions on appeals. This will allow us to meet the 33-month timeframe set out in RSFA for Federal natural gas and oil royalty appeals to be decided by the Department (both MMS and IBLA).

MMS formed teams to reform the appeals process, in keeping with RSFA requirements and Royalty Policy Committee recommendations. The new process will be faster and ensure that States and Indian mineral owners have ample opportunity to participate in the appeals process when the issues affect their revenues. We anticipate a proposed rule will be published later this year.

Involved Constituents

The MMS believes it can best reinvent its activities and serve the needs of its customers by working closely with constituents. They participate in decision making through multi constituent teams of MMS, State, Indian, and industry representatives. Constituents welcome the opportunity to review and recommend improvements to the royalty accounting process through various work groups, negotiated rulemaking committees, workshops, and focus groups.

The MMS established a "205 Delegation Team" composed of State representatives and MMS staff. This team worked to develop a proposed regulation authorizing the delegation of Federal royalty management functions to State governments. Meetings were held with industry in four locations prior to publication of the final rule.

The Royalty Policy Committee includes representatives from States, tribes, Indian allottees, industry, Federal agencies and the public. The RPC has provided recommendations to MMS on a variety of royalty management issues, many of which have been incorporated into the RMP reengineering initiative. Other notable recommendations implemented include:

- Extending the due date by 10 days for production reports submitted electronically.
- Eliminating the need to report drilling wells on the production reports since they are already reported on different forms.
- Eliminating unnecessary status codes from the production report.
- Reducing submission of the Gas Analysis Report - only required if requested by MMS.
- Eliminating unnecessary data fields on the Payor Information Form.
- Establishing a study group for Federal royalty oil taken in kind.

Franchising

The Government Management and Reform Act of 1994 (GMRA) encourages franchising agreements with other organizations. MMS's procurement office has provided their services and expertise to the General Service Administration in the form of procurements valued at $60 million. This track record has generated interest from a broad range of other agencies for similar services.

A cooperative agreement between the Office of the Secretary and MMS has been mutually beneficial. The Office of the Secretary is now provided exceptional personnel service in a timely manner and MMS has received the benefits of professionals within the field of personnel management who have been allowed to stretch to their professional limits.

With those remarks as background, I would now like to discuss our FY 1999 budget request.

FY 1999 Proposed Operating Appropriations/Offsetting Collections
dollars in thousands

Royalty and Offshore Minerals Management	$122,402
Offsetting Collections	$94,000
Oil Spill Research	$6,118
Total	**$222,520**

The largest portion of the MMS operating budget is obtained from the Royalty and Offshore Minerals Management Appropriation (ROMM). Funding from ROMM has been declining since FY 1993. Congress granted MMS the authority to retain a portion of the OCS rental receipts as offsetting collections.. For FY 1999 the authority, now used MMS wide, will rise to $94,000,000.

In addition to appropriations for operations, the MMS receives appropriations for distribution of the States share of onshore mineral receipts. Those permanent appropriations are:

FY 1999 Proposed Permanent Appropriations
(dollars in thousands)

Mineral Leasing Associated Payments *(MLAP)*	606,581
National Forest Fund Payments to States *(Forest Fund)*	3,311
Payments to States from Lands Acquired for Flood Control, Navigation, and Allied Purposes *(Flood Control)*	756
Total	**$610,648**

1998 Supplemental Request

The 1998 MMS request and Congressional action provided a $6.3 million increase in the Offshore Program in response to the surging leasing activity that had occurred in the Gulf of Mexico up to the time of the 1998 budget formulation. As it turns out, actual leasing activity greatly exceeded bullish expectations. The three lease sales conducted since development of the 1998 request were not simply robust, but instead were all record-breakers. This phenomenal leasing has outstripped MMS's ability to effectively perform its regulatory responsibilities to ensure continued safe and environmentally sound development of the OCS.

To not jeopardize continued development of the Nation's OCS resources, with the potential loss of billions in OCS revenues, the Administration has proposed a 1998 supplemental appropriation of $6.7 million that will provide MMS with the additional manpower and scientific information needed to maintain its vigilant oversight of the OCS and provide timely service to industry. MMS delays in bid evaluations, permit reviews, and other required actions are beginning to cause expensive "down-time" for industry and ultimately may delay the receipt of government revenues from the OCS.

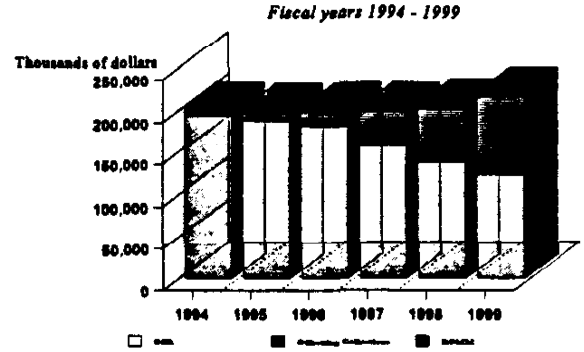
The supplemental request includes approximately $1.7 million in Regulatory Operations to support an expanded inspection and enforcement workforce. The prolific growth in the number of inspectable units in the Gulf of Mexico, and the geographical dispersion of these units over a much greater area, has simply spread the existing inspector force too thin, thus threatening its effectiveness. The additional funding will enable an increased level of field review of plans and applications. The proposed increase will strengthen the regulatory program to better ensure and maintain MMS's commitment to the safe and environmentally sound development of the OCS.

The supplemental request includes $4.8 million in the Leasing and Environmental Program, most of which will support environmental studies focusing on deep water regions of the Gulf of Mexico. Very little is currently known about the deep water topography and habitat in this region. Addressing these information needs is essential to MMS decision-making for environmentally sound development. The rapid pace of deep water leasing has accelerated the need for these studies. Industry has already invested heavily in deep water regions, both in technology development and in bonus bids on deep water leases. This investment, or the environment, could be put at risk if MMS lacks the information it needs to perform such functions as evaluating exploration and development plans, developing appropriate lease stipulations, and evaluating oil spill response plans.

The 1998 supplemental request also proposes $0.2 million in Resource Evaluation (RE). The RE workload related to lease sales and deep water royalty relief has resulted in an increasing backlog of necessary work related to the ongoing exploration and development of existing leases, such as reserves inventory, field determinations, and regional mapping and assessment. Additional personnel are needed to clear up the backlog and enable the Gulf Region to keep up with the downstream RE workload resulting from the record sales.

FY 1999 Budget Request

Minerals Management Service
Funding Sources
Fiscal years 1994 - 1999

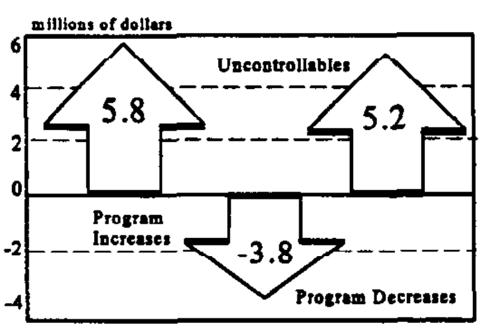


The MMS budget request is approximately $222.5 million, an increase of roughly $13.9 million above the 1998 enacted level of $208.6 million. The $13.9 million increase includes the $6.7 million supplemental discussed above plus a further $7.2 million increase for 1999 to meet legislative and workload increases. The proposed increases are more than covered by raising the cap on offsetting receipts from $65.0 million to $94.0 million. In turn, the request for direct appropriations is only $128.5 million, a decrease of $15.1 million below the 1998 level of $143.6 million. At the 1999 request level, offsetting collections would cover over 40 percent of MMS's operating budget. In addition to the current budget, three permanent appropriations totaling $610.6 million provide States their statutory shares of mineral leasing revenues generated on Federal lands.

The net increase of $7.2 million over the 1998 adjusted level will enable MMS to fully fund its $5.2 million in uncontrollable cost increases. The remaining $2.1 million net increase, coupled with programmatic reductions of $3.8 million, will enable MMS to fund the full-year costs of the proposed 1998 supplemental (an additional $0.8 million), and provide $5 million to initiate a major reengineering effort for the Royalty Management Program (RMP).

The $5 million proposed in 1999 for RMP reengineering will be used to design and begin development of new automated systems to implement redesigned business processes. The RMP faces the dilemma of responding to new legislative requirements, most notably the Royalty Simplification and Fairness Act (RSFA) with aging systems that already exceed accepted life cycle standards. Without this investment, a major risk of system failure and operational instability exists. Furthermore, the RSFA authorized delegation of royalty management functions to States cannot be accommodated with the current RMP systems configuration. RMP modernization is also essential for MMS to continue fulfilling its basic goal of ensuring the timely collection, accounting, verification, and disbursement of mineral revenues and to allow the taking of royalties in kind smoothly. The final result will be a less costly more streamlined program.

Minerals Management Service
Components of Proposed FY 1999 Increase
Total Proposed Increased of $7.2 Million
(assumes FY1998 supplemental is enacted)



The $3.8 million in proposed program

reductions include $1.2 million for the Marine Minerals Technology Centers program. Continuation of this program cannot be covered given the pressing needs in MMS's core mission areas, as discussed above. The request also reflects a general reduction of -$2.4 million to the RMP program that is made possible by improved efficiencies and streamlining. Finally, a savings of -$0.2 is possible in the Offshore Program due to the reduced costs associated with MMS's offshore air quality monitoring activities.

Madam Chairman, this concludes my testimony. However, I will be pleased to answer any questions you or Members may have regarding any aspect of MMS's FY 1998 supplemental or FY 1999 budget request.