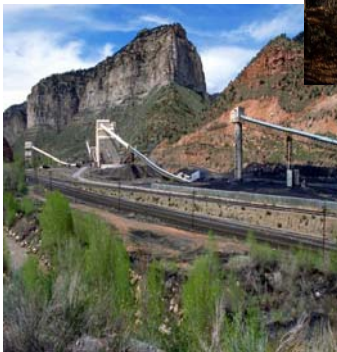


Five-Year Asset Management Segment 1 Strategic Business Plan

November 2008



Minerals Management Service

Five-Year Asset Management Segment 1 Strategic Business Plan

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MMS U.S. Department of the Interior
Minerals Management Service



Associate Director's Message

The Minerals Revenue Management (MRM) Program is entrusted with the collection and disbursement of billions of dollars in Federal and Indian mineral lease revenues. These revenues benefit all Americans. The MRM's fiduciary responsibilities for the Nation's royalty assets have increased as a result of initiatives contained in the Energy Policy Act of 2005 and the Gulf of Mexico Energy Security Act of 2006. This expanded role in national energy initiatives will impact MRM on all operational fronts. The MRM is constantly challenged to improve our processes and procedures and to perform at the highest standard of quality and integrity.

In December 2005, MRM issued the *Strategic Business Plan 2007-2012* to position the Program to meet current and future program challenges and performance expectations. Designed on a foundation of partnership, stewardship, and customer service, the Plan outlines corporate values, guiding principles, and a strategic approach for continuous program improvement. The Plan includes strategic goals, business objectives, and operational strategies for six mission areas - Asset Management, Financial Management, Compliance, Indian Trust, Resource and Information Management, and Production Reporting. The mission areas form the strategic framework for assessment of operations, identification of requirements, and design of business blueprints designed to achieve our strategic vision of excellence in mineral revenue services.

I am pleased and excited to issue this *Five Year Asset Management Segment 1 (Asset Management) Strategic Business Plan*. It arrays a formidable suite of program objectives and management actions. I am confident that working together, the MRM staff and our stakeholders in royalty management, Congress, State and Tribal governments, the minerals industry, contractors, and partnering Federal agencies, we can meet these challenging expectations and continue to be a top tier royalty management program of which all Americans can be proud.

Gregory J. Gould
Associate Director
Minerals Revenue Management

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Executive Summary

The Minerals Management Service (MMS) Minerals Revenue Management (MRM) has developed an Asset Management Business Plan that outlines business principles, objectives, and specific action items that will guide and evolve the MRM Asset Management Program from Fiscal Years (FY) 2008 through 2012.

The Asset Management Business Plan is one of six strategic business planning initiatives MRM undertook beginning in FY 2006. This Plan provides detailed steps for MRM to implement the recommendations from the Blueprint Phase of its strategic business planning efforts.

MRM and Asset Management

In late 2005, the MRM Executive Team (XT) set out fundamentals of asset management for the MRM Program. These fundamentals are:

1. Ensure optimal value is received for royalty assets produced from Federal and Indian lands.
2. Achieve product valuation regulations and rulemaking processes that are dynamic and responsive to market changes.
3. Embrace early certainty concepts as foundational to future valuation agreements and regulations.

The MRM recognizes asset management encompasses both royalties-in-value (RIV) and royalties-in-kind (RIK) and that understanding the contrasting costs and benefits of each approach is critical to making informed decisions on achieving the best return on the assets MRM manages. Because the RIK Program is under its own 5-year business plan, this phase of the asset management strategic business plan only addresses RIV.

Assessment Phase

During the assessment phase of the planning process, the Asset Management Team (Team) analyzed how MRM's existing program met the fundamentals the XT set for effective asset management. The Team reviewed three of MRM's business process areas – maintenance of regulatory reporting requirements and related guidelines to support the MRM business operation; establishment and maintenance of regulatory requirements for valuation of all mineral commodities; and formulation of criteria utilized in the establishment of negotiated agreements. At the conclusion of the assessment phase, the Team recommended the following focus areas for the Blueprint Phase.

1. Identify essential elements for a *strategic/global* approach to asset management (Asset Management Business Model).
2. Identify alternatives to capture, store, and utilize market intelligence.
3. Generate concepts to increase certainty and effectiveness of product valuation rules and regulation development process.

4. Examine features of all valuation rules that need improvements to meet strategic goals.
5. Generate concepts to more accurately reflect market conditions and respond to market changes.
6. Examine options for improving workforce capabilities.

Blueprint Phase

Work in the blueprint phase consisted of a more detailed analysis of the opportunities MRM had in each of the focus areas and the formulation of actions that should be undertaken to move the program closer to the goals the XT established for Asset Management. During this phase, the Team reviewed the valuation regulations for each commodity, conducted benchmarking with a number of organizations, and investigated opportunities for the collection and storage of market intelligence.

Based upon the work in the blueprint phase, the Team recommended the following action items:

1. Establish consistent valuation interpretations under existing regulations.
2. Revise valuation regulations to offer early certainty to industry and MRM.
3. Optimize market intelligence collection and its use in MRM.

The result of the recommended asset management business model is to move MRM's asset management activity to a more proactive program that will allow MRM to have current knowledge of the various markets into which production from Federal and Indian mineral leases flow. This more current market intelligence will help MRM make better informed decisions and make needed changes to its practices and regulations than is now possible.

Implications of Business Model Extensions

The extended asset management business model of the future will require changes in the organization and human resource areas to accommodate the increased capabilities and flexibility envisioned.

Organization. The intended asset management organization structure allows better information collection, storage, and analysis; greater and more consistent policy oversight and regulatory interpretation; and enhanced economic and quantitative analysis of MRM's entire asset management approach. Primary among these changes is the establishment of specific valuation and market intelligence groups that will serve MRM as a whole.

Human Resources. Personnel will be hired or otherwise reassigned. The level of experience and expertise of personnel in the following functional areas will be increased:

- Economic and quantitative analysis,
- Application of valuation regulations,
- Market intelligence, and
- Regulation Writing.

Implementation Stage: Action Items and Timeline

The action items to be undertaken are:

Develop a proposal for reorganization and obtain approval:

- Define functions.
- Define resources needed/develop budget.
- Transfer/hire people.

Revise valuation regulations:

- Develop concept papers.
- Identify studies and analyses needed to support rulemakings.
- Define resources.
- Develop timeline for proposed and final rulemakings.

Optimize market intelligence collection and use in MRM:

- Develop a plan for inventory of existing market intelligence data.
- Establish a schedule for investigating options to obtain, store, and retrieve data.
- Create RIK/RIV liaison.
- Develop plan for inventory and maintenance of royalty assets.
- Develop a plan for automated support.
- Monitor markets to keep valuation regulations current.

The overall timeline of the Plan is designed to allow MRM an opportunity to complete the organizational changes, process improvements, and personnel enhancements during the first and second years. After the second year, the performance measurement processes should be fully operational. When the permanent asset management framework is operational and MRM has put in place the necessary resources, it will be in a better position to take advantage of market intelligence in the conduct of both RIV and RIK business processes. All the specific goals and objectives are designed for completion by the end of the five-year business plan cycle.

1. Asset Management

The MRM is entrusted with ensuring that the American public and Indian lessors receive a fair and appropriate return for oil, gas, and other minerals produced from Federal and Indian leased lands. The MRM collects, accounts for, and disburses billions of dollars in mineral revenues annually. Disbursements in FY 2007 totaled over \$11.6 billion. Historically, most of these revenues have been received in the form of royalty-in-value (RIV) cash payments made by mineral development interests.

In recent years, MRM has been opting to take and receive an increasing proportion of oil and gas mineral royalties in the form of royalty-in-kind (RIK) production payments. This is

particularly true for the royalty asset stream generated from Federal oil and gas leases on the Outer Continental Shelf. In FY 2007, MRM took about \$4 billion of royalties in kind.

This Asset Management Business Plan provides the overall business principles and objectives and the management actions that will help guide the RIV Program for FY's 2008 through 2012. Implementation of this Plan will result in the highest level of efficiency and effectiveness for the RIV component of the Federal Government's management of mineral royalties.

Governing Federal statutes and oil and gas and other minerals lease terms provide the Secretary of the Interior with the responsibility for collecting royalties. The Secretary is charged with ensuring that royalties are based upon the fair market value of the minerals produced. As discussed above, payments may be received either in-value or, in the case of oil and gas, in-kind. These options give MRM flexibility in managing the Nation's royalty assets and the opportunity to maximize revenues through choosing RIV or RIK for any given lease. The MRM constantly strives to improve the efficiency and effectiveness of the processes under each option.

The MRM Asset Management Strategy is to conduct a systematic and deliberative inventory and analysis of the Federal and Indian royalty portfolio to select the option that provides the best return to the public and Indian lessors. Included in the analyses are all potential benefits of each option. The MRM also strives to continually evolve its business practices to reflect increased certainty and decreased administrative costs for the public and industry so that the chosen asset management method will optimize returns and efficiencies for the public.

The MRM Business Plan for RIK is currently in place and addresses time periods through 2009. This Asset Management Business Plan will focus on RIV through 2012. The MRM XT set the following fundamentals as the cornerstone of MRM's asset management approach:

1. Ensure optimal value is received for royalty assets produced from Federal and Indian lands.
2. Achieve flexible, consistent, and timely product valuation regulations and rulemaking processes that are dynamic and responsive to market changes.
3. Embrace early certainty concepts as foundational to future valuation agreements and regulations.

2. Current Regulatory Climate

The Team analyzed the valuation regulations for each commodity for which royalties are received in order to determine how closely the existing regulations meet the fundamentals set by the XT.

Eight key product valuation rules provide guidance and instructions to lessees on how to value royalties from Federal and Indian mineral leases. These regulations ensure that the Federal Government meets the statutory mandate of receiving fair market value. Some of the

rules are recent; others have not been substantially modified since the initial broad-scale efforts of MRM to draft product valuation regulations in the 1980's.

The table below lists the regulations currently in effect and their publication: dates:

Commodity	Publication of Initial Rule	Last Update
Federal Oil	January 15, 1988 Revision of Oil Product Valuation Regulations and Related Topics; Final Rule	May 5, 2004 Federal Oil Valuation Final Rule
Federal Gas	January 15, 1988 Revision of Gas Royalty Valuation Regulations and Related Topics; Final Rule	March 10, 2005 Federal Gas Valuation Final Rule
Indian Oil	January 15, 1988 Revision of Oil Product Valuation Regulations and Related Topics; Final Rule	December 17, 2007 Indian Oil Valuation; Final Rule *Negotiated Rulemaking Committee in progress
Indian Gas	January 15, 1988 Revision of Gas Royalty Valuation Regulations and Related Topics; Final Rule	October 19, 2000 Amendments to Gas Valuation Regulations for Indian Leases
Federal Coal	January 13, 1989 Revision of Coal Product Valuation Regulations and Related Topics; Final Rule	August 22, 1990 Federal Coal Product Valuation, further modified on February 12, 1996 Revision of Valuation Regulations Governing Oil and Gas Transportation and Processing Allowances, and Coal Washing and Transportation Allowances; Final Rule
Indian Coal	January 13, 1989 Revision of Coal Product Valuation Regulations and Related Topics; Final Rule	No Update
Geothermal	November 8, 1991 Revision of Geothermal Resources Valuation and Related Topics	May 2, 2007 Geothermal Royalty Payments, Direct Use Fees, and Royalty Valuation
Solid Minerals	January 13, 1989 Revision of Coal Product Valuation Regulations and Related Topics; Final Rule	August 30, 2001 Solid Minerals Reporting Requirements

Figure 1. MRM Product Valuation Regulations Currently in Effect

The MRM's 1988 valuation regulations were written to achieve market value based upon transactions between independent, non-affiliated parties. The Department of the Interior has long held the belief that the values established in arm's-length transactions are the best indication of market value. Therefore, the 1988 rules reflected that belief.

Since those rules were written, although the Secretary's responsibility to determine the royalty value of minerals produced has not changed, the industry and marketplace have changed dramatically. As discussed below, these industry changes as well as litigation have necessitated changes to MRM's valuation regulations. Indeed, MRM has already amended the Indian gas and Federal oil valuation regulations to simplify those rules and provide early certainty by including valuation based on publicly available prices.

At the time the 1988 rules were developed, producers most commonly sold natural gas at the wellhead to natural gas pipeline companies, which transported and sold the gas to local distribution companies. However, in the mid-1980s, a series of rulemakings by the Federal Energy Regulatory Commission (FERC) resulted in deregulation of certain pipeline systems. As a result, industry began selling directly to end users or distributors and pipelines provided only transportation services. Producers created marketing affiliates to which they initially transferred production. In situations involving sales to affiliates, the Federal gas valuation rules require value to be determined by the first applicable in a series of benchmarks.

Another industry change is that many pipelines now charge producers "bundled" fees that include both deductible costs of transportation and non-deductible costs to place production into marketable condition. Both MRM and arm's-length shippers have encountered difficulties obtaining the data from pipelines necessary to allocate the costs between placing the gas in marketable condition and transportation costs. This situation also occurs with processing plants that charge bundled fees including non-deductible costs.

In addition to the industry changes discussed above, litigation has complicated application of MRM's regulations. Indeed, litigation over the meaning of "affiliated" (the presumption of control when an entity owns between 10 and 50 percent of another) in MRM's regulations was effectively invalidated by the court in *National Mining Association v. U.S. Department of the Interior*, 177 F.3d 1, 6-7 (D.C. Cir. 1999). Moreover, in *Vastar Resources, Inc.*, 167 IBLA 17 (2005), the Interior Board of Land Appeals (IBLA) reversed an MMS Director's Decision that had determined that Vastar Resources, Inc., and its purchaser's transactions were non-arm's length because they did not have opposing economic interests. Rather than clarify what "opposing economic interests" means, the *Vastar* decision created confusion over the definition of arm's length.

Finally, litigation over what constitutes marketable condition has made determination of marketable condition increasingly fact specific and time consuming. See *Amoco Production Co. v. Watson*, 410 F.3d 722 (D.C. Cir. 2005), *cert. denied in relevant part sub nom; BP America Production Co. v. Burton*, 126 S. Ct. 1768 (2006), and *Devon Energy Corp v. Norton*, 2007 WL 2422005 (D.D.C. Aug. 23, 2007), *appeal docketed as Devon Energy Corp. v. Kempthorne*, No. 07-5299 (D.C. Cir. Sept. 11, 2007),

The Team examined each of the existing product valuation regulations within the framework of the MRM strategic business guidelines of early certainty, administrative efficiency, and responsiveness to changing markets and litigation. That examination revealed that the following regulations will need amendments to meet the goals of MRM's asset management approach: Federal gas, Indian oil, Federal and Indian coal, and other Federal and Indian solid

minerals. The following existing regulations may also need some revision: Federal oil and Indian gas.

3. Strategic Objectives and Drivers of the Five-Year Plan

The MRM has developed several objectives that are the key strategic drivers of the Plan.

3.1 Establish Values for Royalty Purposes That: (1) Meet Statutory Requirements; (2) are Known with Certainty at the Time of Royalty Payment; and (3) are Dynamic and Responsive to Market Changes

The MRM will develop a methodology to determine fair market value (FMV) for Federal and Indian mineral production and reasonable transportation and processing deductions. The MRM will incorporate the FMV methodology into new valuation regulations. The three objectives of this FMV methodology are:

Objective 1, Valuation: The value for royalty purposes of any mineral product should reflect the current market value. To the extent practicable, these values should be from publicly available sources in the form of major price reporting publications at the most liquid and transparent market centers/pooling points. The MRM would specify which publicly available prices would form the basis for royalties. In areas where publicly available prices are not available, MRM would explore other options for determining market value.

Objective 2, Transportation Deductions: The costs of moving mineral production to locations off the lease (transportation) may qualify as a deduction from the value of that production determined at the distant market. To the extent practicable, MRM would specify allowable transportation deductions through publicly-available means, either pipeline bulletin boards, major reporting publications, or MRM's website if MRM establishes a standard transportation deduction for a particular region or system.

Objective 3, Processing Deductions: The costs of processing gas for the recovery of gas plant products may also be deductible from the value of those products when determining value for royalty purposes. To the extent practicable, MRM would specify allowable processing deductions through publicly-available means. However, the likelihood of this is low. An alternative is to post allowable processing deductions or percentages on MRM's website if MRM establishes a standard processing deduction for a particular region, system, or plant.

Under this approach, the values and deductions for transportation and processing will be reflective of actual transactions occurring in the marketplace and, as such, will be dynamic and responsive to changes in the market. As such, this approach will provide greater transparency and certainty in the valuation of minerals produced from Federal and Indian leases.

3.2 Implement a Systematic Decision Making and Performance Monitoring Process

The MRM will implement systems, processes, and procedures that will improve valuation and compliance processes under the existing regulations and measure performance relative to FMV for all mineral production on which royalties are collected under the revised regulations. Systems and processes currently utilized by RIK's Economic Analysis Office (EAO) have demonstrated success as effective tools for establishing FMV benchmarks and measuring RIK performance against those benchmarks. Under MRM's revised Asset Management Program, MRM will adopt similar systems and processes for measuring RIV performance. This objective would require systems to support data gathering, storage, and analysis of information gathered.

Initially this data will be housed in spreadsheets or other Microsoft applications created by analysts in RIK, Compliance and Asset Management (CAM), and a new organizational component - the Asset Management Group (this new group will be introduced and outlined in section 4.2 below). Long-term, and assuming approval of appropriate funding, MRM Information Technology (IT) specialists will become involved and facilitate the building of a Geographic Information System (GIS)-based market intelligence database. Reliance on existing government GIS-based systems (BLM for onshore, OMM for Offshore) is anticipated as a cost saving measure.

3.3 Reorganize and Staff Key Business Functions to Fully Implement the Permanent Asset Management Program

The MRM will establish an organizational restructure and implement process control functions that are basic building blocks for the permanent asset management framework. Identification of specific skill set requirements and filling those personnel needs will allow MRM to enhance the experience, knowledge, and expertise of its staff and increase its operational efficiency. This approach also will serve to enhance transparency in the asset management decision process. This effort includes inventorying assets, gathering information regarding the markets into which the production from the various areas flows and using that information to modify and maintain MRM's regulations so they reflect market value, provide certainty to MRM and industry, and allow MRM to more effectively administer the RIV and RIK Programs.

3.4 Administrative Expense

Managing administrative expenses is an important element in successfully developing and implementing MRM's Asset Management Program, both in the RIV and RIK Program areas. In fact, the potential for savings of administrative costs between the two options is one of the primary drivers in deciding which option will result in the best return to the public.

Expenses for the RIV Program include direct costs for personnel in all MRM organizational components except for RIK. Expenses for RIV also include the costs associated with 1) issuing and maintaining regulations; 2) receiving payments and reports; 3) running and maintaining automated systems, 4) conducting audits and compliance reviews, including enforcement actions; and 5) all other costs associated with these functions. Documenting and

capturing these administrative expenses under MRM's current programs are essential in determining how much the revised asset management approach will reduce the costs associated with the RIV Program. The MRM has been utilizing an activity-based accounting system since October 2002 to capture and itemize administrative expense information. Thus, MRM is well positioned to undertake these comparisons.

4. Implications for the Program

4.1 Business Model Changes will Affect Organization, Human Resources, and Systems

Implementation of the above business model extensions, along with continued improvements in the RIV Program, will provide MRM with the capability to fully deploy a royalty asset management strategy, and thus achieve the program's purpose/principles and objectives. The program implications associated with installing this full capability include organization, human resource, and systems issues. As discussed below, the organizational change will involve creation of a new group within MRM to handle the asset management functions this Plan contemplates. In addition, to accomplish the Asset Management objectives, MRM will need to reassign certain functions in the organization and undertake an effort to alter certain foundational approaches to its business. This will require a combination of reassigning existing staff and hiring additional staff with skill sets that support the Asset Management strategy. Additionally, MRM will need to develop new information technology systems to support market intelligence information. This will involve utilizing existing royalty support systems in MMS and other government agencies to the extent that they have data systems that will support the Asset Management Strategy.

4.2 Organizational and Business Process Implications

The MRM's first step is to establish the Asset Management Group (AMG), which will initially undertake three areas of activity:

- Establish consistent valuation interpretations.
- Optimize and maintain market intelligence collection.
- Revise valuation regulations to offer early certainty.

As the regulations are revised, these three areas will be consolidated into the first two areas of activity, with the need for revising the regulations being monitored and efforts undertaken to modify regulations as needed.

Figure 2 shows the intended organization structure of a permanent MRM AMG that may or may not include portions of the existing RIK Program component. The main structural changes involve better delineation of valuation functions; greater policy oversight; a separate group to perform market intelligence gathering; and economic and quantitative analysis. The organizational structure is designed to provide an efficient and effective process for the entire MRM Program.

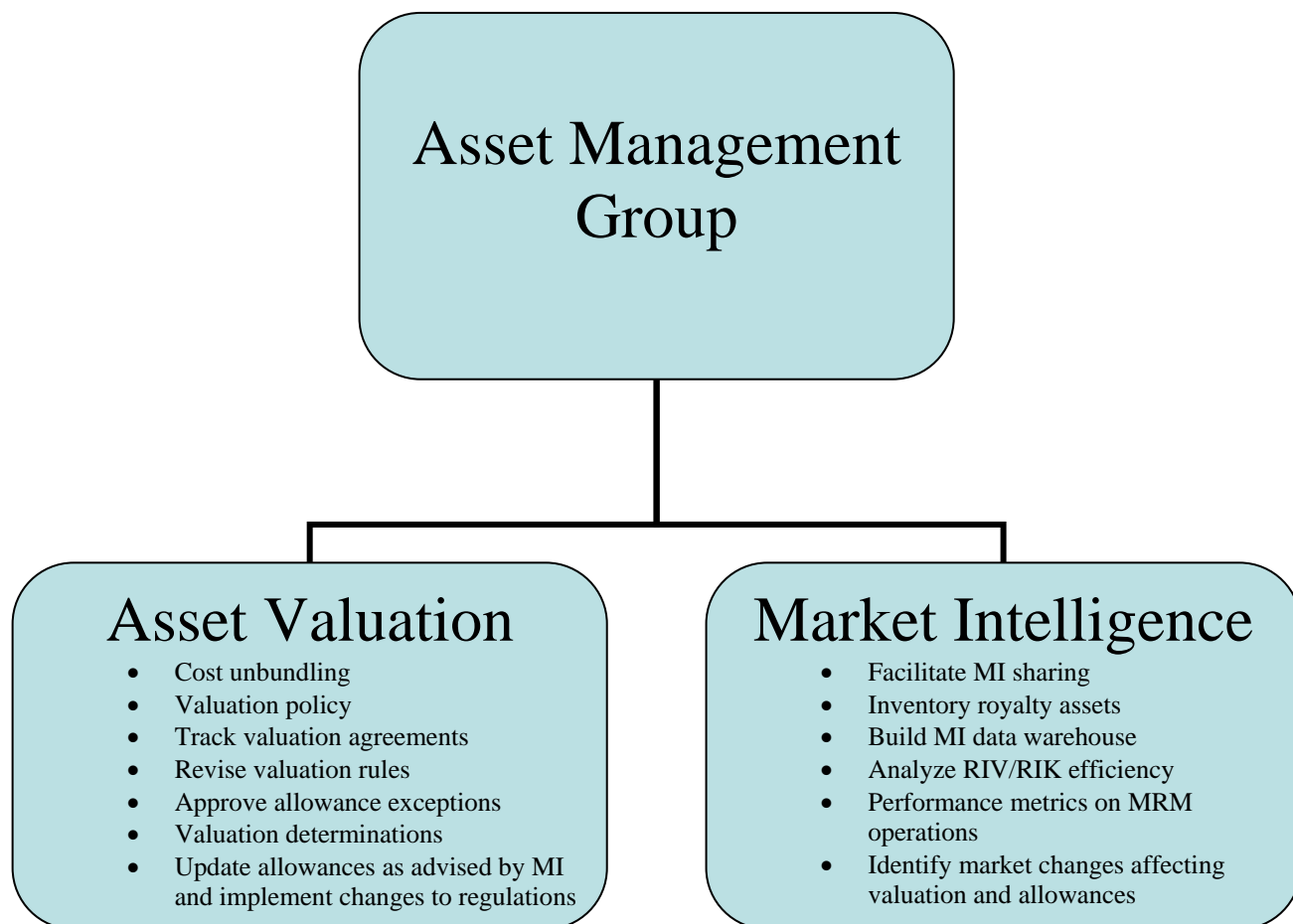


Figure 2. Intended organization structure of MRM Asset Management Group

4.2.1 Asset Management Group: This new organizational component will provide the consistency in MRM’s valuation determinations. This group also will lead rulemaking efforts MRM must undertake to meet the goals outlined by the MRM XT.

The AMG also will provide CAM and RIK with market intelligence. The AMG will begin by assuming the primary role of market intelligence expertise for CAM and utilize existing market intelligence expertise in RIK. This approach will provide a dual benefit of building the expertise level of Asset Management staff and providing a resource for CAM and RIK.

After the AMG has built sufficient market intelligence expertise, it will provide input regarding operational efficiency of RIV/RIK decisions. The RIK Program will research and recommend properties for RIK conversions with input from the AMG. Due consideration will be given to:

- MRM administrative costs and resources required.
- Operational efficiency.
- Value received.

Maintaining viable RIV & RIK Programs.
Stakeholder input.

Having Asset Management involved in RIV/RIK decisions will enhance internal controls.

4.2.2 Asset Valuation Group: Since the reorganization of compliance functions into MRM in 2000, valuation determinations previously centralized within MRM have been handled separately by Offshore CAM, Federal Onshore CAM, Indian CAM, and Solid Minerals and Geothermal CAM. The result has been inconsistent interpretations of MRM's valuation regulations, guidance, and policies. Recentralizing these decisions into the new Asset Valuation Group (AVG) will correct this weakness and provide more consistent and accurate guidance to lessees.

The AVG will be responsible for rulemaking efforts MRM must undertake to meet the goals outlined by the MRM XT. The AVG will also centralize several functions that are currently performed by Offshore CAM, Federal Onshore CAM, Indian CAM, and Solid Minerals and Geothermal CAM:

- Review and respond to transportation and processing requests;
- Unbundling of transportation and processing fees;
- Valuation determinations; and
- Issue valuation guidance to MRM and lessees.

One of the most significant challenges for both lessees and CAM has been a trend by pipelines and processing plants to bundle transportation, processing, and other services into undifferentiated costs to move and treat oil and gas production. This practice makes it difficult to accurately identify deductible versus non-deductible costs under MRM regulations. Work is underway to identify the components of these bundled costs for systems in various production areas to provide appropriate guidance for payors, MRM, and state and tribal auditors. The AVG will assume this function from CAM. Centralizing this function will ensure accurate and consistent application of allowance deductions by royalty payors.

The MRM performs cost unbundling analyses on a transportation system-by-system basis. These analyses form an important part of the market intelligence data set. The immediate benefit of this approach will be to enhance the expected values used in audits and compliance reviews conducted by CAM. This work will also provide valuable information to support the allowance methodology for new valuation rules. The new gas valuation regulations may propose using this data to specify deductions or percentages that payors will use in monthly royalty payments. This will promote the goal of early certainty for royalty payors. Once this effort is completed, it will be important to keep track of transportation system changes that will affect the cost structure of allowances.

4.2.3 Market Intelligence: The Market Intelligence Group (MIG) will conduct a high-level inventory of Federal and Indian mineral properties. This inventory will identify basic market intelligence about Federal and Indian mineral production that will include the available market opportunities for sale of royalty production including identification of transportation and processing options, quality characteristics, and a pricing methodology based upon

publically available information to the extent practicable. The MRM would then use that information to meet the Asset Management goal of simplifying its valuation regulations and obtaining early certainty. The AMG would begin using the information gathered for Federal gas as a “pilot.” After the benefits of the inventory for gas production from federal leases has been demonstrated, AMG staff would work with Solid Minerals and Geothermal CAM and Indian CAM to apply this market inventory and information approach to other Federal and Indian mineral production.

Currently, limited procedures have been put in place by CAM to perform the inventory and market intelligence analysis for RIV and for sharing of RIK information and market intelligence. However, the initial inventory and market analysis will form the starting point for an expansion of the processes, procedures, and systems used to share market information across MRM.

In developing a market intelligence database, MRM will give priority to those production areas where significant production occurs and accurate and reliable information is readily available. In addition, specific valuation issues identified by CAM may impact the priority. Finally, the extent to which MRM is able to modify its regulations will significantly impact the design and cost of the system as well as the production areas to which MRM will give priority. The asset management market intelligence tool will be integral to the management of royalty assets as MRM moves forward.

Anticipated benefits include more powerful analytical capabilities for CAM and OE staff in conducting their work. Additionally, the system will enable MRM to more effectively manage royalty assets for the public’s benefit.

The following processes will be undertaken to develop and build a market intelligence database:

- Inventory and catalogue pipelines, processing plants, and crude oil market center data and maintain in an automated data base.
- Assemble index price data by pipeline and crude oil type, including NYMEX and roll pricing - see RIK data files for price records.
- Retrieve RIK system PowerPoint maps for the Gulf and Wyoming and develop additional maps to illustrate and detail market infrastructure and intelligence.
- Designate a common drive area and establish a filing protocol for storing and retrieving market intelligence maps for RIK and CAM personnel.
- Explore options for collecting and assembling market intelligence data onshore:
 - Inventory CAM databases and records.
 - Prioritize major onshore producing regions for gathering market intelligence information; i.e., San Juan Basin, Power River Basin, Greater Green River Basin, Piceance Basin, Permian Basin, Uinta Basin, and Williston Basin.
 - Canvass major onshore pipeline companies for pipeline maps and electronic capabilities for capturing and retrieving pipeline routes and interconnect points.
 - Research pipeline tariff rates, capture, and store.

- Identify and map major gathering systems, marketable conditioning sites, connectivity to Federal leases - gather rate and fee information.
- Identify and locate gas processing plants, determine connectivity to Federal leases.
- Identify and research onshore crude oil markets, capture and store market conditions, pricing trends, including oil storage and terminal sites, refineries, end markets, transportation and exchange patterns from major gathering/collection sites.
- Identify and capture local market influences in crude oil pricing; i.e., Canadian imports, Alaskan crude, pipeline constraints, refinery demands (volume and quality/type).

The MIG will provide information to the AVG so that they may implement changes to the regulations in response to changes in the market.

4.3 Human Resource Implications

The Asset Management business model and new analytic functions will increase the need for qualified staff to perform these activities. The new functions under the AMG will require proficient oil and gas market analysis skills and thorough knowledge of MRM valuation regulations, guidance, and policies. The MRM will need staff with the following experience and expertise in the following functions:

- Oil & Gas market knowledge;
- MRM valuation regulations, guidance, and policies;
- Regulation writing skills;
- Economic and quantitative analysis;
- IT skills; and
- GIS skills.

Specific additions to the market intelligence efforts will be staff experienced in economics/quantitative analysis and a GIS technician. These modest additions to the organization will have a minimal impact to the size of the MRM organization since they will be offset by efficiencies realized by expanded adoption of the asset management approach.

Retention of the required human resources can be accomplished through 1) internal hiring or transferring of Federal employees and training over several years; 2) contracting for select skill sets/services for full-time operational work with the AMG; 3) contracting or consulting services with commercial resources; or 4) a combination of these approaches. The following more fully describes the intended approaches to filling human resource needs:

- Handling allowance exceptions and unbundling of transportation and processing costs can be handled by transfer of current staff working in CAM.
- Making valuation determinations will be handled by transfer of current staff working in CAM.
- Adding a GIS technician position will need to be added to the AMG.

- Developing technical expertise needed for revising regulations will be obtained by assigning MRM staff on an ad hoc basis but will also require additional permanent staff positions.
- Consulting with the Office of Solicitor as necessary.

To meet the objectives of the Plan, enhancements to the organizational and human resource capabilities will be necessary. These include organizational structure improvements and expanding capabilities to the human resource base that will bring specific market expertise and experience to the AVG.

Figure 3 below shows the proposed organization of the AMG under the business plan.

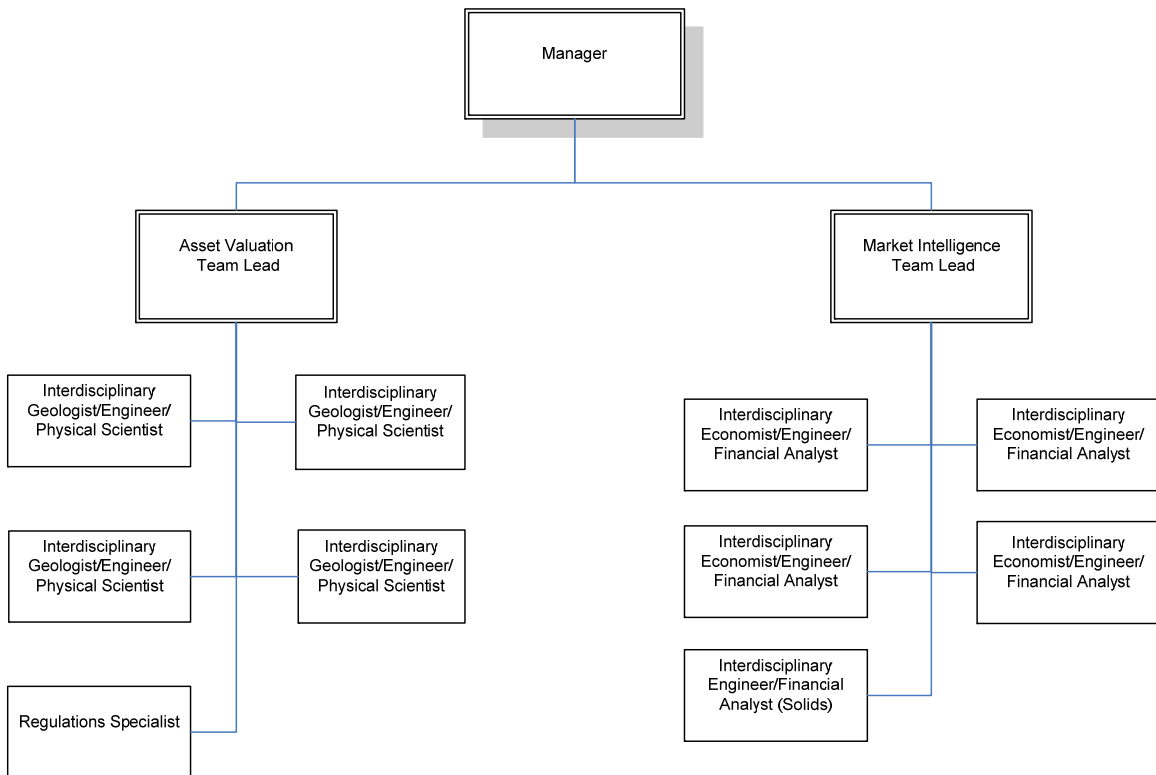


Figure 3. Asset Management Organizational Chart

4.4 Information Systems Implications

Housing of royalty asset valuation data will be initially organized in Excel spreadsheet files. It is envisioned that a system will eventually be designed to house market intelligence data for royalty assets that will be graphically organized in a GIS-based system. The asset management team has consulted with BLM and OMM mapping staff to learn about what currently existing software would be available to organize the data we envision will be needed to inventory market intelligence for royalty assets. Funding for IT requirements will need to be submitted in the FY 2010 budget. We will continue to refine the estimate for resource funding as we further develop the concept for a market intelligence database.

5. Five-Year RIV Business Plan – Timeline and Action Items

5.1 Introduction

This section outlines the specific actions necessary to achieve the principles and objectives outlined above. Implementation of organizational and human resource requirements, necessary control functions, and enhanced asset management strategies comprise the primary action items outlined in the Plan. Each action is accompanied by timing considerations and management accountability.

Performance of these actions together with RIK's 5-year plan will result in achievement of MRM's vision of full deployment of an oil and gas royalty asset management strategy.

5.2 Management of the Business Plan - Overall Responsibility

The MRM senior leadership for the Plan's implementation will be provided by the Associate Director for Minerals Revenue Management (AD/MRM), in close consultation with the XT. The AD/MRM will pursue resources sufficient to implement the Plan.

The AD/MRM will assign an MRM GS-15 manager to manage and coordinate the Plan's implementation. In addition, operational assessments and periodic progress reporting on the Plan's implementation will be carried out by the Quality Control and Training Office.

Critical to realizing MRM's intent to fully deploy a royalty asset management capability is the effective and efficient use of both the RIV and RIK options. As such, MRM managers in RIK and in the RIV compliance/audit program will communicate and coordinate closely so that overall management objectives are achieved.

5.3 Relationship with DOI Strategic Plan and Performance Reporting

Overall Business Plan Timeline

The overall timeline of the Plan is designed to allow MRM an opportunity to complete the organizational changes, process improvements, and personnel enhancements during the first and second years of the plan. After the first year, the performance measurement processes will be developed and fully operational **in FY 2012. All the specific goals and objectives are designed for completion by the end of the five-year business cycle.**

5.4 Components of the Business Plan - Focus Areas

The major action items and timelines for the five-year business plan are outlined below. Specific action items are grouped into seven major focus areas. Each focus area has specific action items with a timeline for completion and assignments of primary responsibility.

5.4.1 Establishing Consistent Valuation Interpretation

The AMG will track future valuation agreements and settlements with future valuation provisions. The AMG will assist CAM with unbundling of gas transportation costs and assume responsibility for transportation and allowance requests. In FY 2009, AMG will transition the responsibility for the cost unbundling project and for responding to valuation determination requests. The strategic advantage envisioned is that AMG will facilitate consistent valuation policy, decisions and determinations for all MRM royalty-in-value matters. Figure 4 below is a time line for transition to the permanent structure to be determined.

Establish Consistent Valuation Interpretations under existing valuation regulations

Implementation Steps	Responsibility	FY2008				FY2009				FY2010				FY2011				FY2012			
		1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4
Review and repond to transporation and processing allowance requests	Assigned MRM Manager					—————▶															
Maintain inventory of future valuation agreements and settlements with future valuation provisions*	Assigned MRM Manager					—————▶															
Organize Asset Management Functions into MRM	Assigned MRM Manager					—															
Assist CAM with transportation and processing unbundling project	Assigned MRM Manager					—															
Assume responsibility for responding to valuation determination requests	Assigned MRM Manager									—————▶											

Figure 4. Timeline for transition of CAM functions

5.4.2 Revise Valuation Regulations to Offer Early Certainty

The first step will be to develop concept papers to summarize proposed revisions to valuation regulations. We envision that it will take several years to draft, propose, and publish final rules. As stated above, Federal gas, Indian oil, Federal and Indian coal, and Federal and Indian solid minerals, need revisions to address markets and legal frameworks that have evolved since the valuation regulations of the 1980’s were written. Federal oil and Indian gas may need minor revisions to address recent market and legal framework changes. Figure 5 below is a timeline of the anticipated course of valuation rule revisions.

Revise Valuation Regulations to Offer Early Certainty to Industry and MRM

Implementation Steps	Responsibility	FY2008				FY2009				FY2010				FY2011				FY2012			
		1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4
Draft concept papers for proposed changes to existing valuation regulations	Assigned MRM Manager			—																	
Research potential effects of proposed rules on existing ICRs whether proposed rules are significant under OMB	Asset Valuation & Rules Group					—															
<i>The following is for an example of a prioritized rule. Additional rules will require additional time</i>																					
Draft proposed rule (includes procedural matters, analysis of potential royalty impacts on stakeholders, cost benefit analysis and completion of any new ICRs)	Asset Valuation & Rules Team					—															
Review process & publish proposed rule	Asset Valuation & Rules Team							—													
Assess comments on proposed rule	Asset Valuation & Rules Team									—											
Draft final rule	Asset Valuation & Rules Team											—									
Review process & publish final rule	MRM/DOI													—————▶							

Figure 5. Timeline for revising product valuation regulations

Because this process relies on interfacing with entities outside the control of MRM, this chart is only an estimate and may differ greatly from the actual time needed to complete this effort. In addition, if valuation rules are revised simultaneously, that too may greatly increase the time necessary to complete the rulemaking processes. Since resources must be shared in the drafting and review stages, it will be imperative to coordinate internal resources to provide adequate time to navigate the steps necessary to research, draft, and review multiple valuation regulation efforts. Identifying and allocating necessary resources to complete this work will be a challenge for management to address. While all reasonable effort will be directed to accomplishing revisions to valuation regulations outlined in the concept papers, we anticipate some rules may not be completed as final prior to the end of the MRM five-year plan, but each rule will be well in process toward completion at the end of the five-year plan with several rules published as final. The priority of published rules will be dependent upon directives set by MRM senior management.

5.4.3 Optimize Market Intelligence Collection

Optimize Market Intelligence Collection and its Use in MRM

In year one, AMG will inventory existing market intelligence data from RIK, CAM, and OE to the extent practical and begin to investigate options to store and retrieve market intelligence. From an internal system perspective, AMG will explore use of the shared directory on the N Drive, linking data from RIK, CAM, and OE, and catalogue and categorize available market information for standardization and consistency for retrieval. In an effort to commence sharing of market intelligence across MRM, AMG will facilitate meetings between OE, CAM, and RIK staff to allow for the interchange of market information.

In years two through three, AMG will assume maintenance of pricing, transportation, and processing cost information from CAM, and begin to analyze its inventory of royalty assets including oil, gas, and coal. It will develop a royalty asset inventory for all basins where MRM administers royalty collection and valuation, and commence implementation of market intelligence data storage system.

A cornerstone to the Asset Management business plan is the inventory of royalty assets from a market prospective. One of the most important efforts that AMG will undertake will be the work to unbundle transportation and processing plant costs for onshore production. The RIK has undertaken these analyses for the bulk of offshore royalty assets and for oil and gas produced in Wyoming. Our intent is to build upon this market intelligence for onshore production using techniques already established by RIK personnel in the course of their work. It is anticipated that members of both the valuation group and market intelligence group will be needed to complete the start up effort. This will have benefits for the valuation staff to increase their understanding of the markets they will oversee. After the inventory has been constructed, the MIG will be responsible for monitoring the inventory for changes and maintaining the database. They will also be primarily responsible for development of a market intelligence system database that will be utilized by all of MRM.

During years three through five, AMG will provide analysis and guidance to MRM management on operational efficiency of RIV and RIK functions. The AMG will use performance metrics for RIV and RIK assets including costs and benefits of both programs to provide quantitative information to MRM management. Figure 6 below is a timeline of the development of asset management functions as they pertain to gathering and storage of market intelligence information.

Optimize Market Intelligence Collection and its Use in MRM

Implementation Steps	Responsibility	FY2008				FY2009				FY2010				FY2011				FY2012			
		1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4
Create OE/CAM/RIK liaison (interim working group while AM develops)	MRM Management																				
Inventory existing market intelligence data	AM Group																				
Investigate options to store and retrieve market intelligence	AM Group																				
Develop market intelligence data storage system	AM Group																				
Assume maintenance of pricing, transportation, and processing cost information	AM Group																				
Study & learn methods used in RIK for analyzing markets	AM Group																				
Analyze market inventory of royalty assets including oil, gas, and coal	AM Group																				
Provide analysis and guidance to MRM management on operational efficiency of RIV and RIK functions	AM Group																				
Develop royalty asset inventory for all basin where MRM administers royalty collection and valuation	AM Group																				
Use performance metrics for RIV and RIK assets including costs and benefits of both programs to provide quantitative information to MRM management	AM Group																				

Figure 6. Timeline for Asset Management Market Intelligence Development

5.5 Organization and Human Resources

The Plan calls for completion of the organizational structure changes within the first year. Specific skill sets and expertise will be acquired or developed in-house over an 18-month window. The extended timeframe allows flexibility in identifying individuals that will provide the specialized expertise required to execute the expanded marketing strategies. The chart below represents the anticipated timeframe for completion of AMG into the MRM organization.

Human Resources Business Plan Implementation

Implementation Steps	Responsibility	FY 2008				FY 2009				FY 2010				FY 2011				FY 2012			
		1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4
Develop Proposed Asset management Organization Chart	AD-MRM																				
Obtain Approval on Proposed Chart	AD-MRM																				
Develop New H.R. Staffing Plan	MRM-Manager																				
Develop Crosswalk to Existing Organization	MRM-Manager																				
Develop/Approve Personnel Staffing Strategy	AD-MRM AD-A&B																				
Develop/Acquire Asset Management Chief	MRM-Manager																				
Develop/Acquire Team Leads for Asset Value and Market Intelligence Teams	MRM-Manager																				
Staff Asset Value Team	MRM-Manager																				
Staff Market Intelligence Team	MRM-Manager																				
Run Ongoing Training Program for Value & Intelligence Teams	MRM-Manager																				

Figure 7. Timeline for Staffing Asset Management Group

To meet the objectives of the Plan, enhancements to the organizational and human resource capabilities will be necessary. These include organizational structure improvements and expanding capabilities to the human resource base that will bring specific market expertise and experience to the AVG. The Plan calls for completion of the organizational structure changes within the first year. Specific skill sets and expertise will be acquired or developed in-house over an 18-month window. The extended timeframe allows flexibility in identifying individuals that will provide the specialized expertise required to execute the expanded marketing strategies. We expect that most of the staff will be transferred from within the MRM to the new organization. This will be Division-level reorganization with the clearance through the MRM Deputy Associate Director, MRM Associate Director, and the Associate Director for Administration and Budget.

5.5.1 Information Systems Improvements and Process Controls

The MRM has a need for an automated system that will allow MRM to collect and store information related to the market value of the various minerals on which it collects royalties. The system would allow MRM to have access to publicly available information from price reporting services for transactions listed at numerous market centers that serve Federal royalty production. The system will also contain a royalty asset inventory for all basins where MRM administers royalty collection and valuation. The system will include analytical tools, reporting functions, and GIS components tied to Offshore Energy and Minerals Management (OEMM) and Bureau of Land Management (BLM) systems. The GIS will provide a consistent, centralized, and cost-effective service for all of Compliance and RIK, as well as provide analysis and guidance to MRM management on the operational efficiency of RIV and RIK functions.

This system is foundational to the Asset Management Business Plan. It also supports the following RPC Royalty Management Subcommittee recommendations:

- Develop a database for gas plant processing (3-16 and 17).
- Provide data for a risk-based compliance strategy (4-9).
- Provide improved communications (5-10).
- Support the oversight of RIK (6-1, 6-2, and 6-10).

The framework for this system will utilize existing MRM production systems to the extent possible. In addition, the new system will be designed to utilize GIS information compiled by OEMM and BLM. Utilizing a market-based approach to data collection will enable MRM to react more quickly to changing market conditions and will require MRM to keep up with market developments as they occur. This will allow for better management of Federal and Indian royalty assets.

6. Performance Metrics and Plan Monitoring

6.1 Business Plan Performance Monitoring

It is important to continually revisit and update the five year business plan and make adjustments and improvements as necessary. Changes in market structure or business

practices require that MRM maintain the five-year plan as a living document that is responsive to these changes. Figure 8 below outlines the process involved in monitoring the five-year Asset Management Business Plan.

Business Plan Performance Monitoring

Action Item	Responsibility	FY2008				FY2009				FY2010				FY2011				FY2012			
		1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4
Measure progress on five-year objectives	EC																				
Review status of action items	AD-MRM																				
Assess/reevaluate assumptions & drivers of five year plan	PAO/AM Mgr.																				
Assess/reevaluate progress on market inventory	AM Manager																				
Assess/reevaluate market intelligence data storage system development	AM Manager																				
Assess/Update Performance Metrics & Performance	PAO/AM Mgr.																				
Develop new five-year business plan	EC																				

Figure 8 Asset Management Performance Review Schedule

6.2 Performance Measurement

The Asset Management Strategy proposed in this Plan assumes MRM will go from the current regulatory scheme of valuation based upon the actual sales, transportation, and processing transactions to a revised scheme where valuation is based on publicly available information or information the MRM may practicably obtain. If MRM does not modify its existing regulations consistent with this revised valuation scheme, it will still benefit from increased market understanding because that information can be used for compliance reviews and auditing royalty payments under the current regulatory scheme.

To properly assess the performance of the assumed revised valuation approach, MRM must be in a position to measure:

- 1) The difference between the values collected under the revised scheme and the old scheme; and
- 2) The difference in the costs of administering royalties under the revised scheme and the old scheme.

Under the plan, MRM will have more accurate knowledge of what the RIV results would have been had MRM not taken the royalties in kind. In addition, the administrative costs of the RIV Program should be less and easier to account for as we expect that there will be less appeals and other litigation under the revised approach. Because the administrative costs associated with appeals and litigation are very difficult to quantify, significantly reducing these costs under the revised valuation scheme will make them immaterial.

Development and implementation of administrative metrics is targeted for completion within the first year. The second year of the Plan will be the baseline year for administrative costs, against which subsequent year administrative costs will be compared. Administrative cost comparisons between RIK and RIV will be enhanced in addition to those already in place as necessary during the first 2 years of the Plan. As regulations are modified, we will adjust administrative cost measures to recognize these changes.

If MRM retains the existing valuation rules, the need to assess performance under new regulations will not be part of the monitoring process, but the other measures outlined above will remain as part of the business plan.

6.3 Communication and Outreach

Effective communication of the future RIV business activity to MRM stakeholders is critical to the success of the Plan. The MRM has a valued and important set of stakeholders with both oversight and partnership roles in the management of mineral royalties. The strategic business direction for the Asset Management Group as published in the Plan will be effectively communicated to these stakeholders who will include congressional entities, states, tribes, industry trade groups, and executive branch offices. In addition, effective communication with MRM employees regarding the nature of the Plan and its interrelationships and synergies with other MRM organizational entities will be critical and ongoing.