# INDIAN OIL VALUATION RULE PROPOSAL FOR HIGHER OF GROSS PROCEEDS OR INDEX-BASED PRICE FORMULA

August 15, 2013

# Proposal for a Higher of Gross Proceeds or Index-Based Formula

Value each month would be the higher of:

1) NYMEX CMA applied to each reservation:
- **Plus/minus the roll.** The roll could be included if contracts in the area typically include the roll. For example, Oklahoma contracts generally include the roll and contracts in Ft. Berthold, Wind River and The Navajo Nation do not.

- **Less a designated-area specific percentage for the transportation/location differential** based on the average difference between the NYMEX CMA and major portion at the 25% level (starting from the top) <u>for the previous year</u>.
  - Designated area will be the reservation boundary except for Fort Berthold and Uintah & Ouray Reservations.
  - Separate differentials for each crude oil type within a designated area.
  - The rule would specify the criteria ONRR would use to determine/modify/add designated areas going forward.

2) Gross Proceeds
- No reporting of API Gravity on Form ONRR-2014
- Lessees would report crude oil type monthly on Form ONRR-2014 using the existing product code field.

# Criteria for Determining Designated Area

- Markets served (where)
- Access to Market (how)
  - access to similar infrastructure (e.g., refineries, pipelines, rail lines)
  - similar geography (e.g., no challenging geographical divides such as large rivers)

- Designated area is the reservation boundary except for Fort Berthold and Uintah & Ouray reservations
  - Fort Berthold – 2 Areas: North and South of the Little Missouri River
  - Uintah & Ouray – 2 Areas: Uintah and Grand Counties; Duchesne County.

- If there is significant change in the transportation/location differentials, affected tribes, allottees or lessees/operators may petition ONRR to consider convening a technical committee to review, modify, or add designated areas.

# Transportation/Location Differential Calculation

- The designated area specific percentage for the transportation/location differential would initially be based on the average annual difference between the NYMEX CMA and the major portion at the 25% level (starting from the top), for the previous year.
- The reported gross proceeds would be used by ONRR to monitor and, if necessary, trigger a modification of the reservation/designated area-specific transportation/location differential used in the index formulas.
- **Trigger:** ONRR will monitor sales volumes on a monthly basis and if the gross proceeds portion of total monthly sales volume reported varies +/- 3% from 25% of the total sales volume for the month, then ONRR will revise the differential prospectively starting with the following month.
- Differential Correction:
  - If gross proceeds volumes fall below 22%, ONRR will increase the differential by 10% every month until the gross proceeds volumes fall within the +/- 3%
  - If gross proceeds volumes exceed 28%, then ONRR will decrease the differential by 10% every month until the gross proceeds volumes fall within the +/- 3%

# Example: Major Portion Array for July, 2012

| Lease Number | Payor/Leasee | Sales Volume | Sales Value | Unit Price | Royalty Rate | Cumulative Volume | Percent of Volume |
|---|---|---|---|---|---|---|---|
| | | | | | | | |
| LEASE A | Company 1 | 2,600.00 | $224,275.15 | $86.26 | 18.75% | 2,600.00 | 4.95% |
| LEASE B | Company 2 | 3,610.00 | $304,494.67 | $84.35 | 18.75% | 6,210.00 | 11.83% |
| LEASE C | Company 3 | 2,877.00 | $242,558.29 | $84.31 | 18.75% | 9,087.00 | 17.31% |
| LEASE D | Company 4 | 4,000.00 | $337,178.10 | $84.29 | 18.75% | 13,087.00 | 24.93% |
| LEASE E | Company 5 | 1,949.20 | $162,446.51 | $83.34 | 18.75% | 15,036.20 | 28.64% |
| LEASE F | Company 6 | 4,070.00 | $338,577.44 | $83.19 | 18.75% | 19,106.20 | 36.39% |
| LEASE G | Company 7 | 2,470.00 | $205,125.22 | $83.05 | 18.75% | 21,576.20 | 41.09% |
| LEASE H | Company 8 | 2,120.00 | $175,861.38 | $82.95 | 18.75% | 23,696.20 | 45.13% |
| LEASE I | Company 9 | 3,420.00 | $283,184.53 | $82.80 | 18.75% | 27,116.20 | 51.65% |
| LEASE J | Company 10 | 2,740.00 | $226,610.55 | $82.70 | 18.75% | 29,856.20 | 56.86% |
| LEASE K | Company 11 | 1,450.00 | $119,570.30 | $82.46 | 18.75% | 31,306.20 | 59.63% |
| LEASE L | Company 12 | 2,710.00 | $223,269.17 | $82.39 | 18.75% | 34,016.20 | 64.79% |
| LEASE M | Company 13 | 3,300.00 | $271,364.06 | $82.23 | 18.75% | 37,316.20 | 71.07% |
| LEASE N | Company 14 | 850.00 | $69,854.13 | $82.18 | 18.75% | 38,166.20 | 72.69% |
| LEASE O | Company 15 | 2,090.00 | $171,581.43 | $82.10 | 18.75% | 40,256.20 | 76.67% |
| LEASE P | Company 16 | 4,210.00 | $345,522.45 | $82.07 | 18.75% | 44,466.20 | 84.69% |
| LEASE Q | Company 17 | 3,460.00 | $283,234.50 | $81.86 | 18.75% | 47,926.20 | 91.28% |
| LEASE R | Company 18 | 1,250.00 | $101,633.03 | $81.31 | 18.75% | 49,176.20 | 93.66% |
| LEASE S | Company 19 | 2,710.00 | $219,626.65 | $81.04 | 18.75% | 51,886.20 | 98.82% |
| LEASE T | Company 20 | 618.00 | $49,847.93 | $80.66 | 18.75% | 52,504.20 | 100.00% |
| | | | | | | | |
| | | 52,504.20 | | | | | |
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| | | | | | | | |

# Example: Reservation X, 2012

| Month | 75% MP | NYMEX CMA | Differential |
| --- | --- | --- | --- |
| January | $75.75 | $89.5785 | $13.83 |
| February | $76.22 | $89.7432 | $13.52 |
| March | $89.04 | $102.9813 | $13.94 |
| April | $96.33 | $110.0385 | $13.71 |
| May | $87.40 | $101.3567 | $13.96 |
| June | $82.43 | $96.2886 | $13.86 |
| July | $83.34 | $97.3405 | $14.00 |
| August | $72.22 | $86.3409 | $14.12 |
| September | $71.65 | $85.6100 | $13.96 |
| October | $72.52 | $86.4281 | $13.91 |
| November | $85.04 | $97.1629 | $12.12 |
| December | $86.58 | $98.5757 | $12.00 |
| Average | $81.54 | $95.1204 | $13.58 |

Average Annual 2013 Differential for Res. X = $\left(\frac{\$13.58}{\$95.1204}\right)$ = 0.1428 = **14.28%**

# Example: Reservation X, 2013

| Month | 2013 NYMEX CMA | Ave. Annual Differential as % | Formula Adjusted Index Price = (1- 0.1428) * (2013 NYMEX CMA) |
|---|---|---|---|
| January | $100.3185 | 14.28% | $85.9930 |
| February | $102.2625 | 14.28% | $87.6594 |
| March | $106.2050 | 14.28% | $91.0389 |
| April | $103.3460 | 14.28% | $88.5882 |
| May | $94.7159 | 14.28% | $81.1905 |
| June | $82.4052 | 14.28% | $70.6377 |
| July | $87.9314 | 14.28% | $75.3748 |
| August | $94.1609 | 14.28% | $80.7147 |
| September | $94.5584 | 14.28% | $81.0555 |
| October | $89.5709 | 14.28% | $76.7802 |
| November | $86.7324 | 14.28% | $74.3470 |
| December | $88.2455 | 14.28% | $75.6440 |

# Example of Differential Adjustment when the Gross Proceeds Volume Fall Below 22% of the Total Sales Volume for the Month

| Reservation X, July 2013 | | | | | | | |
|---|---|---|---|---|---|---|---|
| Lease Number | Payor/ Leasee | Sales Volume | Sale Value | Unit Price | Royalty Rate | Cumulative Volume | Percent of Volume |
| | | | | | | | |
| Lease A | Company 1 | 2,600.00 | $224,275.15 | 86.26 | 18.75% | 2,600.00 | 4.87% |
| Lease B | Company 2 | 3,610.00 | $304,494.67 | 84.35 | 18.75% | 6,210.00 | 11.63% |
| Lease C | Company 3 | 2,877.00 | $242,558.29 | 84.31 | 18.75% | 9,087.00 | 17.02% |
| Lease D | Company 4 | 4,882.00 | $406,426.50 | 83.25 | 18.75% | 13,969.00 | 26.17% |
| Lease E | Company 5 | 1,949.20 | $162,270.90 | 83.25 | 18.75% | 15,918.20 | 29.82% |
| Lease F | Company 6 | 4,070.00 | $338,827.50 | 83.25 | 18.75% | 19,988.20 | 37.44% |
| Lease G | Company 7 | 2,470.00 | $205,627.50 | 83.25 | 18.75% | 22,458.20 | 42.07% |
| Lease H | Company 8 | 2,120.00 | $176,490.00 | 83.25 | 18.75% | 24,578.20 | 46.04% |
| Lease I | Company 9 | 3,420.00 | $284,715.00 | 83.25 | 18.75% | 27,998.20 | 52.44% |
| Lease J | Company 10 | 2,740.00 | $228,105.00 | 83.25 | 18.75% | 30,738.20 | 57.58% |
| Lease K | Company 11 | 1,450.00 | $120,712.50 | 83.25 | 18.75% | 32,188.20 | 60.29% |
| Lease L | Company 12 | 2,710.00 | $225,607.50 | 83.25 | 18.75% | 34,898.20 | 65.37% |
| Lease M | Company 13 | 3,300.00 | $274,725.00 | 83.25 | 18.75% | 38,198.20 | 71.55% |
| Lease N | Company 14 | 850.00 | $70,762.50 | 83.25 | 18.75% | 39,048.20 | 73.14% |
| Lease O | Company 15 | 2,090.00 | $173,992.50 | 83.25 | 18.75% | 41,138.20 | 77.06% |
| Lease P | Company 16 | 4,210.00 | $350,482.50 | 83.25 | 18.75% | 45,348.20 | 84.94% |
| Lease Q | Company 17 | 3,460.00 | $288,045.00 | 83.25 | 18.75% | 48,808.20 | 91.42% |
| Lease R | Company 18 | 1,250.00 | $104,062.50 | 83.25 | 18.75% | 50,058.20 | 93.77% |
| Lease S | Company 19 | 2,710.00 | $225,607.50 | 83.25 | 18.75% | 52,768.20 | 98.84% |
| Lease T | Company 20 | 618.00 | $51,448.50 | 83.25 | 18.75% | 53,386.20 | 100.00% |
| | | | | | | | |
| | | 53,386.20 | | | | | |

# Example of Differential Adjustment when the Gross Proceeds Volume Falls Below 22% of the Total Sales Volume for the Month

- The gross proceeds volume is highlighted in green on the previous slide.
- The sales volume of the gross proceeds for the month is equal to 9,087 Bbls or 17.02% of the total sales volume (53,386.2 Bbls) for the month.
- This is less then the threshold of 22% of the total sales volume, therefore an adjustment must be made.
- The differential from the initial calculation using the previous year was 14.28%.
- The new differential for August, 2013 will be 10% more then the initial differential of 14.28%; or
  - 14.28% + (14.28% X 0.10) = 15.71%
  - The value for royalty purposes for August, 2013 would be August NYMEX CMA multiplied by (100% - 15.71%): or
    - $94.1609 X (100% - 15.71%) = $79.37

# Example of Differential Adjustment when the Gross Proceeds Volume Exceeds 28% of the Total Sales Volume for the Month

| Reservation X, July 2013 | | | | | | | |
|---|---|---|---|---|---|---|---|
| Lease Number | Payor/ Leasee | Sales Volume | Sale Value | Unit Price | Royalty Rate | Cumulative Volume | Percent of Volume |
| | | | | | | | |
| Lease A | Company 1 | 2,600.00 | $224,275.15 | 86.26 | 18.75% | 2,600.00 | 4.87% |
| Lease B | Company 2 | 3,610.00 | $304,494.67 | 84.35 | 18.75% | 6,210.00 | 11.63% |
| Lease C | Company 3 | 2,877.00 | $242,558.29 | 84.31 | 18.75% | 9,087.00 | 17.02% |
| Lease D | Company 4 | 4,882.00 | $411,525.87 | 84.29 | 18.75% | 13,969.00 | 26.17% |
| Lease E | Company 5 | 1,949.20 | $162,446.51 | 83.34 | 18.75% | 15,918.20 | 29.82% |
| Lease F | Company 6 | 4,070.00 | $338,827.50 | 83.25 | 18.75% | 19,988.20 | 37.44% |
| Lease G | Company 7 | 2,470.00 | $205,627.50 | 83.25 | 18.75% | 22,458.20 | 42.07% |
| Lease H | Company 8 | 2,120.00 | $176,490.00 | 83.25 | 18.75% | 24,578.20 | 46.04% |
| Lease I | Company 9 | 3,420.00 | $284,715.00 | 83.25 | 18.75% | 27,998.20 | 52.44% |
| Lease J | Company 10 | 2,740.00 | $228,105.00 | 83.25 | 18.75% | 30,738.20 | 57.58% |
| Lease K | Company 11 | 1,450.00 | $120,712.50 | 83.25 | 18.75% | 32,188.20 | 60.29% |
| Lease L | Company 12 | 2,710.00 | $225,607.50 | 83.25 | 18.75% | 34,898.20 | 65.37% |
| Lease M | Company 13 | 3,300.00 | $274,725.00 | 83.25 | 18.75% | 38,198.20 | 71.55% |
| Lease N | Company 14 | 850.00 | $70,762.50 | 83.25 | 18.75% | 39,048.20 | 73.14% |
| Lease O | Company 15 | 2,090.00 | $173,992.50 | 83.25 | 18.75% | 41,138.20 | 77.06% |
| Lease P | Company 16 | 4,210.00 | $350,482.50 | 83.25 | 18.75% | 45,348.20 | 84.94% |
| Lease Q | Company 17 | 3,460.00 | $288,045.00 | 83.25 | 18.75% | 48,808.20 | 91.42% |
| Lease R | Company 18 | 1,250.00 | $104,062.50 | 83.25 | 18.75% | 50,058.20 | 93.77% |
| Lease S | Company 19 | 2,710.00 | $225,607.50 | 83.25 | 18.75% | 52,768.20 | 98.84% |
| Lease T | Company 20 | 618.00 | $51,448.50 | 83.25 | 18.75% | 53,386.20 | 100.00% |
| | | | | | | | |
| | | 53,386.20 | | | | | |

# Example of Differential Adjustment when the Gross Proceeds Volume Exceeds 28% of the Total Sales Volume for the Month

- The gross proceeds volume is highlighted in green on the previous slide.
- The sales volume of the gross proceeds for the month is equal to 15,918.2 Bbls or 29.82% of the total sales volume (53,386.2 Bbls) for the month.
- This exceeds the threshold of 28% of the total sales volume, therefore an adjustment must be made.
- The differential from the initial calculation using the previous year was 14.28%.
- The new differential for August, 2013 will be 10% less then the initial differential of 14.28%; or
  - 14.28% - (14.28% X 0.10) = 12.85%
  - The value for royalty purposes for August, 2013 would be August NYMEX CMA multiplied by (100% - 12.85%): or
    - $94.1609 X (100% - 12.85%) = $82.06

# Additional Provisions

- NYMEX and gross proceeds reporting subject to audit
- Notwithstanding any other provision of the rule, if a designated area for a particular crude oil type has insufficient royalty lines at varying prices to determine a differential, the Secretary will (in consultation with Tribes/allottees), determine value with due consideration of lease terms and other relevant matters.

# Benefits of the Index-Based Method to Tribes and Allottees

- ✓ Value would be based on the higher of a NYMEX-based formula equivalent to a 25% major portion from the top or gross proceeds.
- ✓ Indian mineral owners with oil sold above the index-based price keep those higher priced royalties.
- ✓ Indian mineral owners with oil sold below the index-based price will receive additional royalties based upon the calculation
- ✓ Tribes and allottees will have more predictable and transparent information on monies they can expect to receive.
- ✓ Indian royalty owners will receive their revenue from major portion sooner and will see fewer adjustments to entries on their explanation of payments.

# Benefits of the Index-Based Method to Industry

- ✓ Reduced accounting and administrative costs
- ✓ Reduced reporting burden related to API gravity
- ✓ Certainty associated with meeting the major portion and gross proceeds obligation in real time
- ✓ Elimination of prior period adjustments
- ✓ Simplified audits and related expenses
- ✓ Reduced administrative appeals and litigation