



# United States Department of the Interior

## MINERALS MANAGEMENT SERVICE

Royalty Management Program  
P.O. Box 5760  
Denver, Colorado 80217-5760

IN REPLY REFER TO:

ARD/FB/RIK  
Mail Stop 3131

FEB 18 2000

Federal Express  
Overnight Delivery

Dear Operator:

The Minerals Management Service (MMS) has selected one or more offshore Gulf lease(s) that you operate to be included in a Small Refiners Royalty-in-Kind( RIK)contract in which we will take crude oil royalties in kind beginning April 1, 2000. Please notify all payors and working interest owners of this change.

This letter provides the procedures and establishes the terms and conditions under which the United States (Lessor) will take royalty oil in kind. Our authority is the Outer Continental Shelf Lands Act at 43 U.S.C. 1353, and the royalty provisions contained in your Federal lease(s). For the purposes of this letter, royalty oil means the Federal lease production multiplied by the lease royalty rate. The volumes of crude oil taken in kind by the MMS shall reflect and be consistent with the MMS' prior grants of all end-of-life royalty relief.

### Term

The Lessor will take all royalty oil from the properties listed in the Operator Schedule of Federal Leases (Enclosure 1) beginning on the 1<sup>st</sup> day of April 2000 and through and including the last day of the month subsequently designated by the Lessor as the date of termination. The Lessor will provide the Lessee and Operator with a minimum 45-day prior written notice of termination of in-kind status. The RIK contract will have a 6 month term with an automatic evergreen clause subject to a 90-day termination clause.

### Royalty Oil Delivery

You must deliver all royalty oil from the selected leases, including royalty oil from newly producing wells on these leases or newly producing leases added to commingling agreements. Royalty oil must be placed in marketable condition at no cost to the Lessor. Marketable condition means the condition generally acceptable to purchasers in the field or area. Questions regarding marketable condition should be directed to the Lessor's Point of Contact.

The delivery point for royalty oil produced from the selected leases is listed in Enclosure 1. The Lessor shall have custody, possession, and responsibility for royalty oil beyond the delivery point. Delivery will be at reasonable times and intervals but not later than the month following the month of production. Usually, this delivery will be daily.

#### Fulfillment of Royalty Obligations

Delivery of the accurate volume of royalty oil (taking into account the effects of normal operational imbalances) in accordance with the terms of this letter will satisfy in full the Lessee's royalty obligation to the Lessor.

All rent or minimum royalty obligations remain the responsibility of the Lessee. If the Lessee owes minimum royalties, MMS will issue a bill. The Lessee will have 30 days to review the bill and make payment or appeal the bill.

#### Lessor Obligation to Take

The Lessor agrees to take 100 percent of the royalty oil delivered for the account of the Lessor or its designee at the delivery point. The Lessor, using customary industry practices will exercise reasonable efforts to minimize imbalances with you and other lessees.

To facilitate timely and accurate custody transfer of royalty oil, the Lessor will communicate with you and make arrangements for the transfer of royalty oil from the delivery point(s). The Lessee will incur no royalty-related penalties because of the Lessor's failure to take delivery of oil volumes as communicated by the Operator.

#### Communication with Lessor

No later than 8 calendar days before the first day of each month, you must notify the Lessor of the daily royalty oil volumes anticipated for the following month of production. You may make other arrangements for timely notification only if acceptable to the Lessor. The Lessor understands that any such estimate is not a warranty of actual deliveries to be made but is provided to facilitate planning.

You must also use reasonable efforts, consistent with industry practice, to inform the Lessor as soon as practical regarding significant changes in oil production levels and/or royalty shares anticipated for project properties.

### Balancing Account and Imbalances

Requirements for handling imbalances are outlined below:

- Imbalances will be determined monthly based on the difference between the royalty share of production and the actual volumes delivered. These imbalances will be maintained at a lease or agreement level.
- You, as the Operator, must provide the lease imbalance statement to MMS no later than 45 days after the end of the month of production, unless MMS approves an alternative timeframe for submission of the statement. Should the information not be available due to no fault of the Operator, then the Operator will provide an estimate.
- Deliveries for the month following the month when the imbalance statement is due will be adjusted, if necessary, to provide for volumetric make-up of the monthly imbalances.
- Imbalances occurring at the end of the RIK contract term will be settled through adjustments in royalty-in-kind deliveries if acceptable to Lessor and Lessee. Only after all reasonable efforts have been made by both parties to settle the imbalance volumetrically will a mutually agreed upon cash settlement be determined based on the value of the oil at the lease during the last month of the contract term for the net barrel imbalance.

### Volume Reconciliation

The MMS will monitor and reconcile production and volumes delivered with additional data, including pipeline data. MMS will reconcile volumes as soon as practicable. Reconciliations will involve communication between you and the Lessor. Upon project termination, you, as the Operator, must issue a final oil imbalance statement. You will settle in accordance with the section "Balancing Account and Imbalances."

### Reporting

You must continue to report crude oil production to MMS on the Oil and Gas Operations Report (OGOR) under current requirements and frequencies as specified in MMS regulations and the MMS *PAAS Reporter Handbook*. You will not be required to report royalty oil for the RIK contract leases on a Report of Royalty Remittance (MMS-2014) for the term during which the Lessor takes royalty in kind, except under provisions described below in this section for transportation and under provisions described above under "Balancing Account and Imbalances." All reporting for non RIK leases will not change.

You must report any transportation allowances, gravity and quality adjustments, and any final imbalances on your Form MMS-2014. You will report separate entries for the allocated volume and values of transportation costs, gravity and quality, and final imbalances for each of the lease(s) identified in Enclosure 1.

### Reimbursement of Transportation Costs

Reasonable transportation cost for the delivery of royalty oil from the lease to the onshore delivery point will be reimbursed by the Lessor. You will be reimbursed only for actual volumes moved through the pipeline and delivered to Lessor at the delivery point. To effect this reimbursement, you must report a transportation allowance on a Form MMS-2014 against each specific lease being taken in-kind for the reasonable cost to move royalty oil to the Delivery Point(s). Please refer to provisions described under "Reporting" for further guidance.

### Gravity and Quality

Gravity and quality adjustments will be based on actual adjustments incurred between the lease and the delivery point. These adjustments will be accounted for as provided under "Reporting".

### Lessor's Designee

At times, the Lessor may act by or through a duly authorized designee. In such event, the Lessor will provide you with prior written notification of its designee(s) including the person to contact. Such notification will include specific duties that will be handled by the designee on behalf of the Lessor. The Lessor also will provide written notification to you when the designee is no longer authorized to act on Lessor's behalf for the purposes of this letter. You are authorized to communicate with the designee as specified in the notification. You will not be required to direct communications to both the Lessor and its designee. For purposes of this letter, if the Lessor notifies you that it will use a designee in the contract, references to Lessor shall refer to the Lessor's designee.

Lessor shall require the designee to agree in writing that the designee is required to comply with all provisions of this letter that are applicable to Lessor when it acts on behalf of Lessor.

### Audit

The Lessor may audit your records regarding all information relevant to volumes and qualities of royalty oil produced, measured, delivered, and, if applicable, transported. The MMS reserves the right to examine your financial records for the subject properties related to any transportation allowances prior to the delivery point.

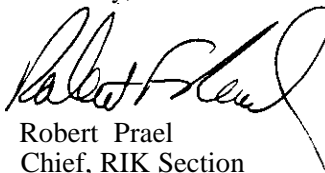
Lessees, Operators, and revenue payors must maintain all records of transactions mentioned in the above paragraph for a period of 7 years from the day on which the relevant transaction occurred unless MMS notifies the record holder of an audit or investigation. When you are notified that an audit or investigation is planned, records must be maintained until the record holder is released in writing from the obligation to maintain the records.

Lessor Point of Contact

Copies of all correspondence between Operator and Lessor should be kept on file by the Operator. Points of contact for the Lessor are included in Enclosure 2.

Lessor acknowledges that you and the other Lessees have given proper notice whenever you communicate with Lessor using the e-mail address, fax number, or telephone number provided. Any telephone communication regarding volumes is to be confirmed by fax or e-mail no later than one business day after telephone communication occurs. The Lessor further agrees to make arrangements to receive such communications regarding oil scheduling issues during normal business hours. Operators and Lessees should communicate with the above points of contact to answer any further questions.

Sincerely,

A handwritten signature in black ink, appearing to read "Robert Prael", with a large, sweeping flourish extending to the right.

Robert Prael  
Chief, RIK Section