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RE: Consolidated Federal Oil and Gas and Federal and Indian Coal Valuation Reform (ONRR-2012-0004)

Subject: Regulation Identifier Number 1012-AA13.

Dear Mr. Southall:

These comments are submitted on behalf of Trapper Mining Inc. ("TMI"). TMI has operated the Trapper Mine ("Trapper") near Craig, Colorado since 1983. Trapper is located adjacent to the Craig Station Power Plant ("Craig Station") and was designed to serve as a mine-mouth fuel supply for the plant in the early 1970s. During its operation, Trapper has produced coal from four different federal coal leases as well as from other non-federally owned coal properties. Substantially all the coal produced from Trapper was historically sold to the owners of the Craig Station under the Craig Station Fuel Agreement (established on March 1, 1973, and expired on June 30, 2014). More recently, the coal produced at Trapper is sold to the owners of TMI for use at the Craig Station under the terms of the Craig Station Long-Term Coal Supply Agreement established January 1, 2010, and extending through December 31, 2020.

Trapper Mine and Craig Station ownership structure:
There is substantial overlap between the TMI and Craig Station ownership structures. Trapper and the Craig Station are operated as separate and distinct businesses and the percentage of controlling ownership divided amongst the owners varies between the two entities. The four owners of Trapper are also part-owners of the Craig Station where the coal produced at the Trapper Mine is consumed. The four owners consist of an investor-owned utility, a wholesale generation and transmission utility, and two power supply entities that are political subdivisions of states. Their ownership interests in Trapper correspond to their obligations to purchase coal under the Craig Station Long-Term Coal Supply Agreement dated January 1, 2010, and their interests in the electricity produced by Craig Station's units 1 and 2.

Trapper Mining Inc. reorganized corporate structure:
In 1998, TMI reorganized its corporate structure and made the decision to henceforth conduct business as a cooperative. TMI notified the Minerals Management Service ("MMS") (predecessor to ONRR) of this change and proposed certain revisions in its coal valuation methodology approach for royalty calculation purposes. MMS responded on August 12, 1998, acknowledging the change in TMI's corporate organization and accepting the proposed revisions in the coal valuation approach formula with certain specified changes ("MMS Approval Letter"). Approval was given at that time to value Federal coal production consumed under non-arm's-length conditions using a cost of production plus a return on investment component for mine investment. This cost based non-arm's-length valuation procedure reasonably approximates the fuel costs reported by all of the participants (both investor-owned and cooperative electric utilities) to either the public utility commission or their member boards. TMI has abided by these approved valuation formulas since they were established in cooperation with MMS. An audit of TMI's 2011-13 royalty reports and payments by the Colorado Tax Auditing and Compliance Division, dated October 17, 2014, confirms that TMI has been following the approved regulations for reporting and paying federal coal royalties.

Trapper Mining Inc.'s issues with ONRR's proposed royalty valuation:
One of the ONRR's justifications for proposing new Coal Royalty Valuation Rules is that the federal coal "industry and marketplace have changed dramatically." For TMI and the Craig Station, this is not the case. As the 40-year history of the Trapper Mine and coal sales to the owners of the Craig Station demonstrate, no significant change in the market for Trapper Mine's coal, or the terms of its sale to the owners of the Craig Station for electric generation, or the ownership of Trapper itself, has occurred and no change is anticipated. While changes in federal coal sales markets may have occurred elsewhere (i.e. particularly with respect to federal coal sales to non-mine mouth power generators), those changes have not taken place at Trapper nor are they likely to.

TMI recommends that the proposed regulations acknowledge stable market arrangements such as Trapper enjoys and then either grandfather or exempt such arrangements from the strict application of the new regulations in favor of using proven and existing formulas like those found in the MMS Approval Letter. Such grandfathering or exempting clause would most likely fit in proposed rule 1206.258 as a binding, pre-effective date valuation determination.

Throughout the entirety of its operational history all of the coal produced by TMI from Trapper has been delivered by truck to the Craig Station. Following delivery, the coal is fed through a primary crusher and then further processed at Craig Station to produce electricity. None of the coal mined at the Trapper Mine is sold to other buyers. There are no facilities at either Trapper or at the Craig Station to accommodate coal deliveries from Trapper to other power plants or buyers.

Trapper calls attention to its long-term and stable relationship with its buyers (who are also its owners), and the collaborative development of the non-arm's-length rules that have historically been applied to its federal coal sales. Trapper has followed the appropriate rules regarding non-arm's-length sales and reported coal valuations and royalties due accordingly. Those rules also encompass reporting the cost of primary crushing performed at the Craig Station after the coal is delivered.

TMI encourages ONRR to carefully consider the historical context and reasoned development of the existing valuation regulations and to refrain from revising valuation methodologies that have proven to be effective, reliable and logical in their application. The existing methodologies well reflect and account for the historical and current circumstances at Trapper while the newly proposed regulations will be difficult if not impossible to apply in any logical, consistent and accountable fashion.

The most significant concern in the proposed rules is incorporating the new concept of valuing coal for royalty purposes, not as coal, but as electricity. For example, proposed regulations 1206.252(b) and (c) stretch coal royalty valuation calculations far beyond the transactions they were originally intended to address. They attempt to adapt concepts developed for an entirely different industry, the geothermal industry, by incorporating reference to 30 CFR Subpart H as the means to determine generation and transmission deductions from the gross value of electricity sales. They raise the need for extremely complex calculations by the coal buyer/electric generator and its affiliated electricity purchasers who have nothing to do with mining federal coal.

It also appears that an underlying assumption is that these arrangements artificially reduce the price for Trapper coal. During the past several years, TMI has received solicitations to bid on providing coal to the fifth owner of Craig. The fact that TMI did not receive the contract implies that Trapper's price is not the lowest delivered price fuel for the Craig Station. A non-arm's length agreement does not automatically ensure the fuel supply is the cheapest one available.

Whatever marginal royalty income this regulation may generate for the ONRR, it will be far more than offset by the cost of accounting to comply with it. Even ONRR's analysis shows that the marginal revenue would be minimal if not negative. The Cost Analysis at 80 F.R. 633 states that ONRR expects the changes to federal coal royalty valuations to change royalty revenue by plus or minus $1.06 million. The median value is zero. The Cost Analysis at 80 F.R. 639 states that royalties paid on federal coal from coal cooperatives constitute 1-2% of federal coal royalties paid. So, the expected effect of 1206.252(b) and (c) is no change in 1-2% of federal coal royalties.

Rules 1206.252(b) and (c) should not be adopted. They will create additional costs for federal coal producers and their affiliated buyers while producing no marginal revenue for ONRR.

Yours sincerely,

James Mattern
President and General Manager