

Royalty Policy Committee  
Coal Subcommittee Report  
January 17, 2008

The Coal Subcommittee met once since the last RPC meeting. The meeting was well attended by representatives from the MMS, BLM, Navajo Nation, States, and Industry.

**Energy Policy Act of 2005 Rulemaking Update**

The BLM and MMS provided progress reports regarding the implementation of the Energy Policy Act of 2005. The rulemaking regarding the Energy Policy Act of 2005 is delayed until at least March 2008 as other issues, such as the Crandall Canyon mine disaster, has taken priority. There is not a mandate in the Energy Policy Act to have the rules promulgated by a specific date.

The Federal coal advance royalty proposed rule continues to move through the process. The MMS has made revisions to incorporate recent Interior Board of Land Appeal (IBLA) decisions, including the BTU Empire decision (IBLA 2006-21). It is anticipated MMS and BLM will publish the proposed advance royalty rule changes to CFR 30 and CFR 43 concurrently in March 2008.

Section 369 of the Energy Policy Act of 2005 establishes requirements for commercial leasing of oil shale and tar sands. BLM and MMS are working on a leasing rulemaking. The MMS is currently proposing that production and royalty reporting will be handled using the Solid Minerals Production and Royalty Report (P & R) with the Solid Minerals & Geothermal Compliance and Asset Management group overseeing the reporting. The reporting and valuation rules will reside in the MMS regulation.

**Continuous High-Wall Mining**

The issue of the royalty rate applicable to continuous high-wall mining operations has now reached the highest decision making level within BLM. Once the decision is made it will be incorporated into the proposed BLM rule.

**Coal Valuation Non-Arms-Length Benchmarks**

The MMS is preparing a white paper proposing to change the non-arms-length benchmarks in the current coal valuation regulations.

**Compliance Activity Update**

SM&G CAM provided the Subcommittee with an update of the compliance activity completed in 2007 and the work plan for 2008.

The 2007 solid mineral and geothermal compliance activity covered sales year 2004:

- STRAC completed compliance work on over \$163 million of reported royalty

- MMS completed compliance work on over \$373 million of reported royalty
- Representing 84% of sales year 2004 reported solid mineral and geothermal royalties

Planned 2008 solid mineral and geothermal compliance activity covering sales year 2005:

- STRAC has planned to cover \$180 million of reported royalty by way of
  - 6 compliance reviews (2 have already been completed)
  - 24 audits
- MMS plans to cover \$257 million of reported royalty by way of
  - 23 compliance reviews
  - 3 audits

### Interest on Adjustments

SM&G CAM reported they want to be sure a consistent policy is being executed when late payment bills are issued. Therefore, they were requesting an opinion from the Office of the Solicitor on whether adjustment lines reported as a routine price adjustment (adjustment reason code 31 (Arc 31)) on the P & R are subject to interest if underpayments occur. SM&G CAM recognizes that the coal industry must pay royalties on coal shipped each month before the final selling price is known due to adjustments invoiced after the reporting sales month per the terms of the contracts for reasons including, but not limited to, Btu, sulfur, ash, contract indexing factors, state and federal tax and royalty audits.

### Improved Compliance Review Process

As a result of the question relating to whether late payment interest should be charged on routine contract price adjustments, the SM&G CAM is reviewing their compliance review process. SM&G CAM has determined that 60%-70% of the P & R lines reported each month for coal are adjustment lines. Therefore, SM&G CAM has determined the compliance reviews need to be improved to provide more focus on the adjustment lines. SM&G CAM is developing additional compliance review procedures to focus on adjustments and is exploring the development of a compliance process tool to identify adjustment lines. SM&G CAM will continue to work with the Coal Subcommittee to understand the types and frequency of adjustment lines and to develop a review process to validate adjustments are reported timely.

### Accounting and Reference Team Updates

The SM&G CAM Accounting and Reference Team (ART) is responsible for a wide range of reporting, reference and accounting and compliance activities supporting the Mineral Royalty Management program goals.

- **Lease Account Status**—ART completed 16 LAS reviews and preliminary findings identified \$2.4 million of rents, royalties and bonuses as unpaid. ART then verified that \$833,000 of that amount was actually owed. ART will follow-up with the BLM and BIA on the findings through collection.

- **Indian Payment Verification**—Verifying the payments made to the various Indian Tribes and allottees, ART obtains payment data (TPAY) from the Office of Special Trust and/or from Tribal banks to ensure the payment amount matches the royalty receivable reported by the producing solid mineral companies. In FY 2007, ART verified and generated 64 TPAY documents for \$41.8 million of Indian payments.
- **History of Timely Payments**—A review of the history of timely payments requires a review of the reported P & R data and payment data to determine if all the payments due for the prior sixty months were paid on-time or not. ART completed three history of timely payment reviews with two confirming all payments were made timely and one confirming there were late payments within the last sixty months.
- **Pre-Bill Verification Project**—ART performed on pre-bill review during August 2007. \$19.5 million in outstanding pre-bills generated by the Financial Management System were reviewed. Of the pre-bills reviewed, ART determined \$16.8 million, or 86.4% of the total amount reviewed, were invalid. ART notified the Debt Collection Section in Financial Management to delete the invalid bills. The remaining pre-bills are currently being reviewed in conjunction with the Lease Account Status workload.
- **Statement of Account (SA) Review and 180/120 Debt Collection Verification (180)**—The SA is reviewed and the validity of the items included in the SA are documented. The 180 process requires an in-depth review of all past due items by payor. Utilizing both the SA and 180 research/account analysis reviews of invoices totaling \$5.2 million, ART was able to clear \$4.0 million or 76.9% of the invoices either by the payor remitting payment or the correction of the documents submitted. In addition, \$4.3 million On Account Balances were reviewed, with \$2.0 million or 45.6% being cleared.
- **Ready for Treasury Project**—ART reviewed \$965,000 in outstanding bills ready for submission to Treasury for collection. \$953,000 or 98.7% were cleared either by the payor remitting payment, the invoice deemed invalid or a correcting P&R or MMS-2014 was received. ART has submitted \$8,000 for two payors to Treasury for collection.

#### Payment Data Access

Based on their experience in resolving some of the outstanding invoice issues, **industry will request that MMS develop a report or allow access to their account payments that would show how payments submitted to the MMS were applied and to what document(s).** Having access to this information would help in the researching the validity of recently received interest bills and increase industry's ability to effectively communicate to ART on SA issues.

**P&R Access**—SM&G CAM has completed the software development for industry access of their P&R information. It is anticipated instructions on how to initialize accounts and access the portal will be issued sometime in the 1<sup>st</sup> quarter 2008.