

Royalty Policy Committee Coal Subcommittee Report November 14, 2006

The Coal Subcommittee met twice since the last RPC meeting. The meetings were well attended by representatives from the MMS, BLM, Navajo and Crow (one meeting) Nations, States, and Industry.

Energy Policy Act of 2005 Update

The BLM and MMS provided progress reports regarding the implementation of the Energy Policy Act of 2005. An initial draft of the proposed rule is currently being circulated internally within the BLM for review and comment. When issued for public comment, the proposed rule will address the topics Instruction Memorandum have been issued. There is not a mandate in the Energy Policy Act to have the rules promulgated by a specific date.

Coal Advance Royalty – Coal Spot Market Definition

Because the Energy Policy Act requires the use of spot coal prices for future advance royalty calculations, the MMS has asked industry to provide information regarding what they consider a spot coal sale to be based upon the term length of a transaction. Industry will provide appropriate comment on the definition of a spot coal sale when the proposed rule is published.

Continuous High-Wall Mining

The BLM has indicated their decision regarding the royalty rate applicable to continuous high-wall mining operations will be part of the proposed rule.

MMS Document Imaging System

The Solid Minerals and Geothermal Compliance and Asset Management Team (“SM&G CAM”) has progressed in developing a process in which STRAC can access valuation decisions, lease information, project files, sales contracts and sales summary information submissions electronically. A contract to provide this access with the appropriate security has been issued with a completion date in FY2007.

The contractor is currently in the process of modifying the InfoStore and ViewStar software to allow access. The timeframe for implementation has not been established, and will be dependant on the completion of the software modification portion of the project and the available SM&G CAM resources to provide testing and training prior to implementation.

Industry views the completion of this project as critical to improving the MMS compliance and audit efforts and reducing industry’s duplication of providing information.

In response to the industry desire to be able to submit the required contracts electronically to the MMS, the MMS is exploring their ability to upload electronic versions of contracts into their current systems.

will look into addressing the information included in the original Statements of Account to enable the reporter to identify the issue period without contacting SM&G CAM.

The cooperation between industry and SM&G CAM has reduced the over 180 day open receivable balance from \$55 million to less than \$1 million in two months.

Coal Compliance Review and Audits

There was continued discussion of the SM&G CAM "Coal Compliance Review Process" and the overlapping audits creating duplicate efforts on industry to provide requested documents.

The SM&G CAM reported the State of Wyoming will perform two compliance reviews in conjunction with their FY2007 audit plan. Utah has indicated they plan to do several compliance reviews of coal lessees. SM&G CAM has also visited New Mexico to discuss the coordination of compliance reviews and audits.

Follow-up Analysis of Identified Audit Issues

To help the Coal Subcommittee gain a better understanding of how the coal compliance review and audit efforts could be better coordinated, it was requested that the SM&G CAM do an analysis of recently completed coal audits to identify the issues that resulted in additional federal royalty being assessed.

The initial analysis of the completed solid mineral audits was included in the Coal Subcommittee's April 26th report to the Royalty Policy Committee. However, the Coal Subcommittee felt additional information from the initial analysis should be developed to help further refine the coordination and to specifically identify coal audit issues. The SM&G CAM has updated their initial analysis by identifying the seven audit issues identified as "cost reported inaccurately" (i.e. unacceptable working capital, interest, sales commission and management fees) and the one audit issue identified as "inaccurate allowance" (i.e. disallowed deductions) were not coal companies.

SM&G CAM has indicated they are continuing to analyze the past audits to provide additional information specific to coal that can be used to define the direction of future coal compliance reviews and audits.

Timeliness of Coal Audit Appeal Resolution

Industry asked if there was any information available regarding the resolution of coal appeals and whether the Agency policy of 33 months for resolution of coal appeals was being adhered to. When RSFA was enacted in 1996, the MMS was required to issue findings for oil and gas valuation appeals within 33 months. Subsequently when the MMS amended the rules for the 33 month time period to issue appeal findings, they excluded coal but established a written Agency policy to adopt the 33 month time period for issuing coal appeal findings.