Official Business
Department of the Interior
Royalty Policy Committee

DEC 5 2006

Ms. R. M. "Johnnie" Burton
Director
Minerals Management Service
1849 C Street NW
Washington, D.C. 20240

Dear Ms. Burton:

Enclosed is the Final Report prepared by the Royalty Policy Committee (RPC) Oil and Gas Royalty Reporting Subcommittee (Subcommittee) dated October 2006 titled "Final Report on Royalty Reporting For Retroactively Approved Communitization and Participating Areas Agreements." The Report provides recommendations to improve the timeliness of royalty reporting and to reduce the number of prior period amendments associated with retroactively approved Communitization and Unit Participating Area Agreements.

The Report was presented to the RPC by the Subcommitttee at the November 14, 2006, RPC meeting held in Lakewood, Colorado. The full RPC approved the Report. As Chairperson of the RPC, I am officially providing you this Report from the RPC for your submittal to the Secretary of the Interior for his review and acceptance.

Sincerely,

Daniel F. Riemer
RPC Chairperson

Enclosure

Royalty Policy Committee
Oil and Gas Royalty Reporting Subcommittee

Final Report
On Royalty Reporting
For
Retroactively Approved
Communitization
and Participating Areas
Agreements

October 2006

Oil and Gas Royalty Reporting Subcommittee Report on Royalty Reporting on Retroactively Approved PA & CA Agreements September 28, 2006

Subcommittee background

The Oil and Gas Royalty Reporting Subcommittee was formed at the October 28, 2004 meeting of the Royalty Policy Committee to investigate ways to streamline royalty reporting. This is the second issue addressed by the Subcommittee. and it involves the royalty reporting on retroactively approved CA and PA agreements.

Subcommittee members

Chair, Darrell Gingerich	COPAS
Vice Chair – Todd Druse	Ute Mountain Ute Tribe
Lorraine Corona	MMS
Cheryl Crawford	ExxonMobil
Lisa Crothers	Indep. Petr. Association of America
Debbie GibbsTschudy	MMS
Megan Hessee	MMS
Gary Johnson	BLM
Harold Kemp	State of Wyoming
Jack Lougee	State of New Mexico
Gilbert Martinez	State of New Mexico
Jim Morris	MMS
Bob Prael	MMS
Nancy Rodriguez	State of New Mexico
Valdean Severson	State of New Mexico
Jay Spielman	BLM
Fred Watson	ExxonMobil
Pam Williams	Shell
Bob Wilkinson	ConocoPhillips
Carla Wilson	Indep. Petr. Assn. Mountain States

Scope and Objectives

The primary purpose of this review was to investigate ways to improve the timeliness of royalty reporting, and to reduce the number of prior period amendments associated with retroactively approved Communitization and Unit Participating Area Agreements. Currently, prior period amendments are often filed covering time periods of many months to several years.

Special thanks to Lorraine Corona and Jay Spielman whose contributions were critical to the review, and whose documents are the primary source of this write-up.

Communitization Agreements (CA)

Background

Communitization Agreements are often approved several months before a CA 1st production notice is issued. Wells drilled within an approved CA are automatically communitized and royalties on production from these wells should be reported in accordance with the CA allocation schedule regardless of whether or not a CA 1st production notice has been issued.

Previously, MMS – Minerals Revenue Management would ask companies not to report the royalties on the CA until the CA 1st production had been issued. CA leases are often in a terminable rental status until the CA 1st production notice is issued and MRM's system is not setup to handle royalties on a lease that is officially in a non-producing status. This has become a bigger issue in recent years as CBM wells frequently produce water for many months. This water is often accompanied by only a small amount of gas. Royalties are owed on this gas, however a 1st production notice can't be issued until the well is de-watered.

BLM Research

For the period between 1/2003 and 3/2006:

- 1,778 Federal CAs were approved (Exhibit 4).
- 14% were submitted prior to the well being drilled (Exhibit 4).
- 1/3rd were approved within 1 month of receipt (Exhibit 4).
- Almost 90% were approved within 1 year (Exhibit 4).
- While most BLM offices approved fewer than 100 CAs during the past 3 years, 3 offices approved more during the same period with the Wyoming Reservoir Management Group (RMG) having over 900 (Exhibit 4).
- Significant improvement has occurred in the BLM approval times for the Farmington and Wyoming RMG offices during the past 12 months (Exhibits 5 & 6).
- The Montana BLM office had issued Instruction Memorandum back in 1995 & 1996 to streamline the issuing of First Production Memorandums and the unique handling associated with Coalbed Methane Wells (Exhibits 7 & 8).

Subcommittee Recommendations

1. MRM to accept and process all royalty lines received for approved CAs regardless of whether a 1st production notice has been issued. This may require a temporary workaround and potentially a future system change to allow these lines to clear automatically.
2. BLM to refresh and re-issue an Instruction Memorandum (IM) on when 1st production notices should be sent and the IM should include CBM wells.
3. BLM to develop procedure to monitor the timely submission of Communitization Agreements. and actively follow-up with operators.

4. BLM to review annually the status of field office approvals for backlog of CAs still needing approval, and for CA approval timelines to identify any prioritization, resource allocation and/or training issues.
5. BLM to identify opportunities where the importance of timely submission of CAs can be communicated to appropriate industry representatives (industry meetings such as RMMLF).

Unit Participating Areas (PA)

Background

Before a PA is approved, the operator must first prepare a discounted cash flow (DCF) analysis. If the DCF is negative, the operator files a report detailing the well economics. If the BLM agrees, the well is 'non-paying' and all production is allocated to the individual tract upon which the well is located.

If the DCF is positive, a PA must be established and the operator must file an application for a PWD (Paying Well Determination), detailing the well economics, and a proposed configuration for the PA. The paying well determinations (PWD) must be completed before the PA is approved. A good producing well requires 3-6 months of production before a PWD can be done. A marginal well can require 6-9 months. Once the PWD is completed and the PA is approved, companies are given 90 days to adjust their reporting. This involves reversing previously reported lease basis lines and submitting lines based on the PA allocation percentages.

BLM Research

- Unit Participating Areas are always approved to be effective retroactively (Exhibit 3).

- Since 1/1/2003, the BLM has approved 86 applications for a new or revised PA, and they have issued 100 'non-paying' well determinations involving over 200 wells in 69 different units (Exhibit 2).

- In most cases, the operator promptly filed the request for PWD and establishment of a PA (Exhibits 1 & 2).

- Based upon the approved Participating Areas reviewed, the average length of time between well completion and PA approval took an average length of 7 months. This number excludes one unit which had 9 PA revisions submitted simultaneously, some of which were effective 12 years retroactively (Exhibits 1 & 2).

- The RMG in Wyoming has researched and made improvements to the CA and PA programs to address Coalbed Methane handling (Exhibits 5).

Subcommittee Recommendations

1. BLM to develop procedure to monitor the timely submission of Unit Participating Areas, and actively follow-up with operators.

2. BLM to review annually the status of field office approvals for backlog of PAs needing approval and PA approval timelines to identify any prioritization, resource allocation and/or training issues.
3. BLM to review the RMG in Wyoming's report (Exhibit 9) to determine if the findings can be applied more universally.
4. BLM to identify opportunities where the importance of timely submission of PAs and PWDs can be communicated to appropriate industry representatives (industry meetings such as RMMLF).

Exhibits

1. Notes for RPC Meeting on Participating Areas – Jay Spielman – March 16, 2006
2. RPC Study – PAs (spreadsheet) – Jay Spielman
3. Reporting on Retroactive Agreements – Lorraine Corona – May 19, 2006
4. Study of Communitization Agreement Process and Processing Times (ppt) – Jay Spielman
5. Wyoming State Office – RMG Response to RPC Recommendations
6. Updated Charts on RMG & Farmington Processing Times (ppt) – Jay Spielman
7. Instruction Memorandum MT-95-023, Policy on Coalbed Methane Wells – Thomas P. Lonnie.
8. Instruction Memorandum MT-96-056, First Production Memoranda for Leases, Unit/Communitization Agreements – Francis R. Cherry, Jr.

March 15, 2006

Notes for Royalty Policy Committee on Participating Areas

Background

The regulation regarding Participating Areas is included as Section 11 in the Model Form of Unit Agreement, 43 CFR 3186.

A participating area is defined as "all land then regarded as reasonably proven to be productive of unitized substances in paying quantities".

Policy/Procedures

The need for a PA is triggered by the completion of a producing well within a Federal Exploration unit, but outside of any established PAs. In most cases, the operator produces the well for 6-12 months before submitting an application for establishment of a PA. This provides a production history with which to perform decline curve analysis, and thus a projection of the well's recoverable reserves.

The operator then prepares a discounted cash flow (DCF) analysis using actual well drilling, completion and operating costs; and actual and projected production volumes. If the calculation results in a negative DCF, the operator files a report detailing the well economics. If BLM agrees, the well is 'non-paying' and all production is allocated to the individual tract upon which the well is located.

However, if the DCF calculation is positive, a PA must be established. The operator files an application for a PWD, detailing the well economics, and a proposed configuration for the PA. The BLM Authorized Officer (AO) reviews the report; the AO will make a paying well determination. If the PWD results in a positive DCF, a PA is needed. A separate PA is established for each horizon. Each PA is serialized, and the pertinent data are entered into the LR2000 data base.

Though consistent within a particular BLM state, the method for determining the size and configuration of a PA varies between states. Often, the Unit Agreement may require a specific process. Four common methods:

-based upon nominal spacing (i.e., for a gas well, a 320 acre PA consisting of the North or South half section, or an East or West half-section);

-based upon the calculated drainage area of the well, which is assumed to be radial, with north-south and east-west tangents drawn on this circle, and the PA consisting of all legal subdivisions included within the tangent;

-based upon the calculated drainage area of the well, with the PA consisting of all legal subdivisions that have at least half of their land area located within the drainage circle; or

-based upon the geological interpretation of the reservoir boundaries, using geological data from all existing wells and available geophysical data.

A PA may also include non-producing lands which are necessary for unit operations (such as an injection well).

Whatever method is employed, the well costs and production revenue from the well are allocated to all of the tracts within the PA proportionally (i.e., in a 320 acre PA, a 160-acre tract will be allocated 50% of the production revenue, and 50% of the well costs). The effective date of the PA is the date of first production.

The AO's decision generally occurs within a week or two of the operator submission, but is often well over a year after the well has been completed. **Section 11 of the Model Form requires the Unit Operator to 'impound' all monies (except Federal royalty) derived from the well until a PA or PA revision is approved (unless the owners of committed working interests establish a mutually-acceptable alternative).** Thus, after approval of a PA or PA revision, Federal royalty amounts will have to be adjusted by the MMS based upon the Exhibit "C". {On March 24, 1995, MMS issued a PAAS Alert on retroactive reporting of wells moved between leases and agreements. We are not sure if this Alert is still in effect.}

A PWD must be prepared each time a new well is completed outside of a PA. In many cases, a separate PA is established for these new wells. In other cases, the initial PA is revised to include new acreage. If a well is completed within an existing PA, no PWD is necessary, but the well may prove up additional acreage that could expand the PA.

In many cases, when an exploratory unit is being actively developed, the operator has several wells for which a PWD has not been made. The operator may submit several PWDs simultaneously. Each could result in revision of the PA boundary, and each PA revision is effective on the well completion date. If the wells are completed in the same month, they may all be included in a single revision.

The Minerals Management Service receives a copy of all BLM correspondence that affects royalty allocations within unit PAs. The MMS then tracks individual unit agreements and PAs. Each time a PA is revised, MMS must update its system to ensure that the royalties paid to Federal and Indian lessors is correct.

Research Results

We queried BLM's LR2000 'database' to gauge the number of PAs approved since January 1, 2003. During that period, BLM approved 86 applications for approval of an initial PA, or an expansion of an existing PA. Over the same period, BLM issued over 100 'non-paying' well determinations, involving over 200 wells in 69 different units. {Note that LR2000 only contains data on Federal leases and units.}

In most cases, the operator has promptly filed the request for PWD and establishment of the PA. In those cases, the PA may be approved within 12 months of the well completion date. The overall average between well completion date and PA approval is about 18 months.

However, some operators do not promptly file their applications. For the Rosa Unit in NM, the operator filed requests for nine revisions of the PA on the same date. When approved, the revisions affected production occurring as long as 12 years earlier. Each PA revision affected past production, and required the operator to prepare a new Exhibit "C" detailing the tract participation schedule. Omitting the Rosa Unit from the calculations, the average time between well completion and PA approval is about 7 months.

Conclusions

We believe this study, though incomplete, demonstrates that there is not an onerous burden on MMS to perform recalculations of royalties allocable to Federal leases located within PAs that have been established or revised. In addition, we believe that the requirement to file a PWD provides an incentive for the operator to continue diligent development of the unit area.

RPC Study on Participating Areas

Used LR2000 for PA actions since January, 2003

Case Recordation No.	Unit Name	Well No.	PA Name	PA Appln Date	PWD Date	PA Appr Date	PA Eff Date	PA acreage	Added acres	Months Before PA Approved	
COC 056158D	Pilgrim	Spencer 22-8	Initial Lewis PA D		3/7/2005	3/7/2005	8/11/2004			5	
MIES 051282A	Spruce	Yates 1-22	Initial Reed City PA A(?)			3/10/2004	11/1/2003			4	
MIES 051282B	Spruce	Yates 1-22	Initial Traverse PA A(?)			10/27/2004	11/1/2003			11	
MIES 053585A	Echo 30 Project?	?				10/6/2005	12/1/2004			9	
NMNM 078407D	Rosa		Initial Fruitland Coal	5/10/2004	12/10/2003	2/23/2005	11/12/1990	320.00		174	
NMNM 078407D	Rosa		1st Revision	5/10/2004	12/10/2003	2/23/2005	9/1/1992			152	
NMNM 078407D	Rosa	involves	2nd Revision	5/10/2004	12/10/2003	2/23/2005	4/1/1993			145	
NMNM 078407D	Rosa	multiple wells;	3rd Revision	5/10/2004	12/10/2003	2/23/2005	9/1/1994			128	
NMNM 078407D	Rosa	Initial PA	4th Revision	5/10/2004	12/10/2003	2/23/2005	9/1/1997			91	
NMNM 078407D	Rosa	consisted of	5th Revision	5/10/2004	12/10/2003	2/23/2005	4/1/1998			84	
NMNM 078407D	Rosa	320 acres.	6th Revision	5/10/2004	12/10/2003	2/23/2005	5/1/1999			71	
NMNM 078407D	Rosa	9th Revision	7th Revision	5/10/2004	12/10/2003	2/23/2005	5/1/2000			59	
NMNM 078407D	Rosa	includes	8th Revision	5/10/2004	12/10/2003	2/23/2005	5/1/2001			46	
NMNM 078407D	Rosa	23,296 acres	9th Revision	5/10/2004	12/10/2003	2/23/2005	8/1/2002	23,296.03		31	981
NMNM 109714A	Samuel Smith		Initial Morrow	8/23/2004	8/17/2004	1/11/2005	6/17/2004	320.00		7	
UTU 063013H	Chapita Wells	805-32X	Initial Mesaverde "D"	5/10/2004	4/27/2004	7/6/2004	10/11/2003	80.00		9	
UTU 063013H	Chapita Wells	861-32	1st Revision "D"	1/17/2006	12/13/2005	1/19/2006	6/1/2005	160.00		8	
UTU 063013H	Chapita Wells	860-32	2nd Revision "D"	2/13/2006	1/24/2006	2/15/2006	7/1/2005	240.00		8	
UTU 063013J	Chapita Wells	628-14X	Initial Mesaverde "F"	9/24/2004	8/24/2004	10/4/2004	11/18/2003	80.00		11	
UTU 063013K	Chapita Wells	806-12	Initial Mesaverde "G"	10/21/2004	10/4/2004	10/25/2004	3/9/2004	80.00		8	
UTU 063013M	Chapita Wells	863-32	Initial Mesaverde "I"	12/23/2004	11/23/2004	12/28/2004	5/7/2004	80.00		8	
UTU 063013M	Chapita Wells	862-32	1st Revision "I"	3/1/2006	1/24/2006	3/6/2006	7/1/2005	160.00		8	
UTU 063013Q	Chapita Wells	830-4	Initial Mesaverde "L"	4/21/2005	3/8/2005	4/28/2005	8/13/2004	160.00		9	
UTU 063013R	Chapita Wells	856-34	Initial Mesaverde "M"	5/18/2005	4/28/2005	6/13/2005	9/5/2004	80.00		9	
UTU 063013R	Chapita Wells	878-34	Initial Mesaverde "M"	1/30/2006	12/13/2005	2/1/2006	5/1/2005	160.00		9	
UTU 063013S	Chapita Wells	879-28	Initial Mesaverde "N"	5/18/2005	5/10/2005	6/13/2005	10/17/2004	80.00		8	
UTU 063013T	Chapita Wells	651-6	Initial Wasatch "F"	6/13/2005	5/26/2005	7/21/2005	11/8/2004	72.30		9	
UTU 063013U	Chapita Wells	multiple	Initial Mesaverde "E-J-K"	8/22/2005	8/4/2005	8/24/2005	12/1/2004	715.84		9	
UTU 063013U	Chapita Wells	multiple?	1st Revision "E-J-K"	9/22/2005	9/7/2005	9/26/2005	1/1/2005	875.84	160.00	9	
UTU 063013U	Chapita Wells	552-30	2nd Revision "E-J-K"	10/20/2005	?	10/21/2005	2/1/2005	995.84	120.00	9	
UTU 063013U	Chapita Wells	895-26	3rd Revision "E-J-K"	12/2/2005	11/3/2005	12/12/2005	4/1/2005	1,035.84	40.00	9	
UTU 063013V	Chapita Wells		Initial Mesaverde "O"	8/15/2005	8/4/2005	8/24/2005	1/11/2005	80.00		8	
UTU 063013W	Chapita Wells		Initial Mesaverde "P"	11/16/2005	10/17/2005	12/1/2005	3/24/2005	80.00		8	
UTU 063013Y	Chapita Wells		Initial Mesaverde "Q"	11/16/2005	10/14/2005	12/1/2005	3/24/2005	79.38		8	
UTU 063015B	Bar-X		Initial Entrada	8/6/2004	8/19/2004	8/19/2004	12/23/2003	1,200.00		8	
UTU 073520B	Ashley		Initial Green River	10/7/2005	10/19/2005	10/19/2005	9/16/2005	32.82		1	
UTU 073520A	Ashley	multiple	13th Revision Initial Green River "A"	1/23/2006	1/26/2006	1/26/2006	10/1/2005	5,563.97	60.29	5	
UTU 080000A	Cane Creek		Initial Cane Creek		10/7/2004	12/20/2004	5/18/2004	715.52		7	
UTU 080250F	Stirrup		Initial Wasatch-Mesaverde "F"	3/25/2005	3/17/2005	4/26/2005	7/6/2004	194.27		10	
UTU 080800A	Wolverine	17-1	Initial Navajo	10/12/2004	10/18/2004	10/18/2004	5/12/2004	160.00		5	
UTU 080800A	Wolverine	17-2	1st Revision	11/22/2004	11/22/2004	11/24/2004	11/1/2004	320.00	160.00	1	
UTU 080800A	Wolverine	multiple	2nd Revision	9/12/2005	9/20/2005	9/20/2005	8/1/2005	480.00	160.00	2	
UTU 080800A	Wolverine	19-1	3rd Revision	10/7/2005	10/5/2005	10/19/2005	9/1/2005	635.41	155.41	2	
UTU 080800A	Wolverine	18-1	4th Revision	12/27/2005	1/25/2006	1/13/2006	12/1/2005	798.77	163.36	1	
UTU 080800A	Wolverine	20-1	5th Revision	2/8/2006	1/25/2006	2/8/2006	1/1/2006	1,039.77	241.00	1	
UTU 081153A	Wilkin Ridge	12-32-10-17	Initial Mesaverde "A"	8/29/2005	8/12/2005	9/9/2005	6/9/2004	160.00		15	
UTU 081301A	Bull Horn		Initial Cutler&Hermosa	11/17/2005	6/15/2005	12/1/2005	12/15/2004	360.00		12	
UTU 081308A	Big Valley	4ML-32	Initial Wasatch-Mesaverde "A"	12/30/2005	9/12/2005	1/13/2006	6/16/2005	80.00		7	
UTU 081878A	Little Canyon	12-1H	Initial Mesaverde "A"	12/22/2005	1/18/2006	1/18/2006	4/3/2005	160.00		10	
WYW 109416M	Beaver Creek	196	Initial Shannon "A"	12/1/2005	8/4/2005	12/9/2005	3/11/2004	40.00		21	
WYW 113732M	Frewen	23-1	Initial Mesaverde "J"	7/15/2004	11/5/2004	12/13/2004	12/12/2003	160.00		12	
WYW 121148K	Two Rim	9-1	Initial Mesaverde "I"	7/15/2004	11/9/2004	12/11/2004	2/11/2004	160.00		10	
WYW 148333A	Schoonover Rd		Initial Ft Union "A"	4/28/2005	6/1/2005	6/1/2005	8/26/2004	7,280.26		9	
WYW 148333A	Schoonover Rd	multiple	1st Revision	9/19/2005	11/16/2005	11/16/2005	9/1/2004	8,538.95	1,258.69	15	
WYW 148333A	Schoonover Rd	multiple	2nd Revision	9/19/2005	11/16/2005	11/16/2005	10/1/2004	10,114.60	1,575.65	14	
WYW 148333A	Schoonover Rd	multiple	3rd Revision	9/19/2005	11/16/2005	11/16/2005	11/1/2004	10,154.02	39.42	13	
WYW 149561A	Bullwhacker Creek	multiple	Initial Ft Union "A"	7/21/2004	4/1/2004	8/3/2004	3/23/2004	5,719.65		4	
WYW 149561A	Bullwhacker Creek	multiple	1st Revision	7/21/2004	8/3/2004	8/3/2004	4/1/2004	7,557.23	1,837.58	4	
WYW 149561A	Bullwhacker Creek	multiple	2nd Revision	5/20/2005	7/1/2005	7/1/2005	12/1/2004	7,637.23	80.00	7	
WYW 149561A	Bullwhacker Creek	multiple	3rd Revision	5/20/2005	7/1/2005	7/1/2005	1/1/2005	8,599.27	962.04	6	
WYW 149561A	Bullwhacker Creek	multiple	4th Revision	5/20/2005	7/1/2005	7/1/2005	2/1/2005	9,886.94	1,287.67	5	
WYW 151544A	Echeta	multiple	Initial Ft Union "A"	4/22/2005	5/18/2005	5/18/2005	9/21/2004	3,295.20		8	
WYW 152375A	Triangle	multiple	Initial Ft Union "A"	11/12/2004	11/17/2004	11/17/2004	9/1/2004	1,723.86		3	
WYW 152375A	Triangle	multiple	1st Revision		2/1/2005	10/1/2004	10/1/2004	1,933.62	209.76	0	
WYW 152375A	Triangle	multiple	2nd Revision	1/24/2005	2/1/2005	11/1/2004	11/1/2004	3,014.97	1,081.35	0	
WYW 152375A	Triangle	multiple	3rd Revision	2/16/2005	3/16/2005	3/16/2005	12/1/2004	3,416.35	401.38	4	
WYW 154735A	Juniper Draw	multiple	Initial Ft Union "A"	6/1/2004	4/14/2004	2/24/2005	4/14/2004	2,440.00		11	
WYW 154735A	Juniper Draw	multiple	1st Revision		6/1/2004	2/24/2005	6/1/2004	2,640.00	200.00	9	
WYW 154735A	Juniper Draw	multiple	2nd Revision	1/24/2005	7/1/2004	2/24/2005	7/1/2004	2,960.00	320.00	8	
WYW 156984A	Seaver		Initial Lewis/Mesaverde "A"	8/31/2005	11/16/2004	10/12/2005	3/19/2004	140.00		19	
WYW 157349A	Stone Cabin		Initial Muddy "A"	3/31/2005	1/26/2005	8/15/2005	10/25/2003	160.00		22	
WYW 157349B	Stone Cabin		Initial Lance/Meeteetsee "B"	3/31/2005	7/12/2005	7/12/2005	12/24/2003	40.00		19	
WYW 157388A	Owl Creek Valley		Initial Lance/Lower Fort Union "A"	4/13/2005	8/12/2004	5/18/2005	11/24/2003	90.00		18	
WYW 157478A	Doty Mountain		Initial Mesaverde "A"	6/14/2005	7/15/2005	7/15/2005	2/1/2005	3,244.14		5	
WYW 158113A	Spotted Horse	multiple	Initial Fort Union PA "A"	3/1/2006	3/8/2006	3/8/2006	6/22/2005	3,462.09		9	
WYW 160315A	Remington	multiple	Initial Ft Union "A"	3/9/2005	5/6/2005	5/6/2005	1/1/2005	10,186.19		4	
WYW 160315A	Remington	multiple	1st Revision	3/30/2005	5/6/2005	5/6/2005	2/1/2005	10,893.28	707.09	3	
WYW 160315A	Remington	multiple	2nd Revision	5/13/2005	5/19/2005	5/19/2005	3/1/2005	13,030.27	2,136.99	3	
WYW 160315A	Remington	multiple	3rd Revision	5/19/2005	6/9/2005	6/9/2005	4/1/2005	14,150.27	1,120.00	2	
WYW 160315A	Remington	multiple	4th Revision	8/4/2005	10/7/2005	10/7/2005	5/1/2005	15,573.09	1,422.82	5	
WYW 160315A	Remington	multiple	5th Revision	10/3/2005	10/7/2005	10/7/2005	6/1/2005	16,606.50	1,033.41	4	
WYW 160315A	Remington	multiple	6th Revision	10/3/2005	10/7/2005	10/7/2005	7/1/2005	18,369.97	1,763.47	3	
WYW 160315A	Remington	multiple	7th Revision	10/3/2005	10/31/2005	10/31/2005	8/1/2005	20,089.97	1,720.00	3	
WYW 160315A	Remington	multiple	8th Revision	12/8/2005	12/19/2005	12/19/2005	10/1/2005	20,226.93	136.96	3	
WYW 160315A	Remington	multiple	9th Revision	12/23/2005	1/12/2006	1/12/2006	11/1/2005	20,451.86	224.93	2	
WYW 160315A	Remington	multiple	10th Revision	1/20/2006	2/28/2006	2/28/2006	12/1/2005	21,081.90	630.04	3	
									all units	1555	18 mo. Avg
									omitting Rosa Unit	575	7 mo. Avg

Reporting Royalties on Retroactively Approved Agreements
5/19/2006

Communitization Agreements (CA)

Background

Communitization Agreements are often approved several months before a CA 1st production notice is issued. Wells drilled within an approved CA are automatically communitized and royalties on production from these wells should be reported in accordance with the CA allocation schedule regardless of whether or not a CA 1st production notice has been issued.

Previously, MRM would ask companies not to report the royalties on the CA until the CA 1st production had been issued. CA leases are often in a terminable rental status until the CA 1st production notice is issued and MRM's system is not setup to handle royalties on a lease that is officially in a non-producing status. This has become a big issue because CBM wells frequently produce water for months. This water is often accompanied by a small amount of gas. Royalties are owed on this gas, however a 1st production notice can't be issued until the well is de-watered and is producing in quantities sufficient enough for a paying well determination on the lease level.

Resolution

MRM will accept and process all royalty lines received for approved CAs regardless of whether a 1st production notice has been issued.. This will require a temporary workaround and potentially a future system change to allow these lines to clear automatically.

Unit Participating Areas (PA)

Background

PAs are always approved to be effective retroactively. Paying well determinations (PWD) must be completed before the PA is approved. A good producing well requires 3-6 months before a PWD can be done. A marginal well can require 6-9 months. Once the PWD is completed and the PA is approved, companies are given 90 days to adjust their reporting. This involves reversing previously reported lease basis lines and submitting lines based on the PA allocation schedule.

BLM Research

BLM conducted research and provided numbers on the length of time it takes BLM to approve a PA.

BLM determined that since 1/1/2003, they have approved 86 application for a new or revised PA. During that same time they have issued 100 'non-paying' well determinations involving over 200 wells in 69 different units.

In most cases, the operator promptly filed the request for PWD and establishment of a PA. The average length of time between well completion and PA approval can take up to 12 months with the average length of time being 7 months. (This number excludes the Rosa Unit which had 9 PA revisions submitted simultaneously, some of which were effective 12 years retroactively).

The BLM believes these numbers illustrate that the burden on industry to perform recalculations of royalties when PAs are retroactively approved or revised is not onerous. They also believe that the requirement to file a PWD provides an incentive for the operator to continue diligent development of the unit area.

Royalty Policy Committee

Study of Communitization Agreement Process and Processing Times

Communitization

- Authorized by Sec. 17b of the Mineral Leasing Act of 1920 (August 8, 1946 amendment)
  - Regulations under 43 CFR 3105.2
  - BLM Manual 3160-11
  - CAs are processed by field offices, except in Wyoming, where all are reviewed by the Reservoir Management Group, located in Casper; and Utah, where they are reviewed by the State Office

43 CFR 3105.2

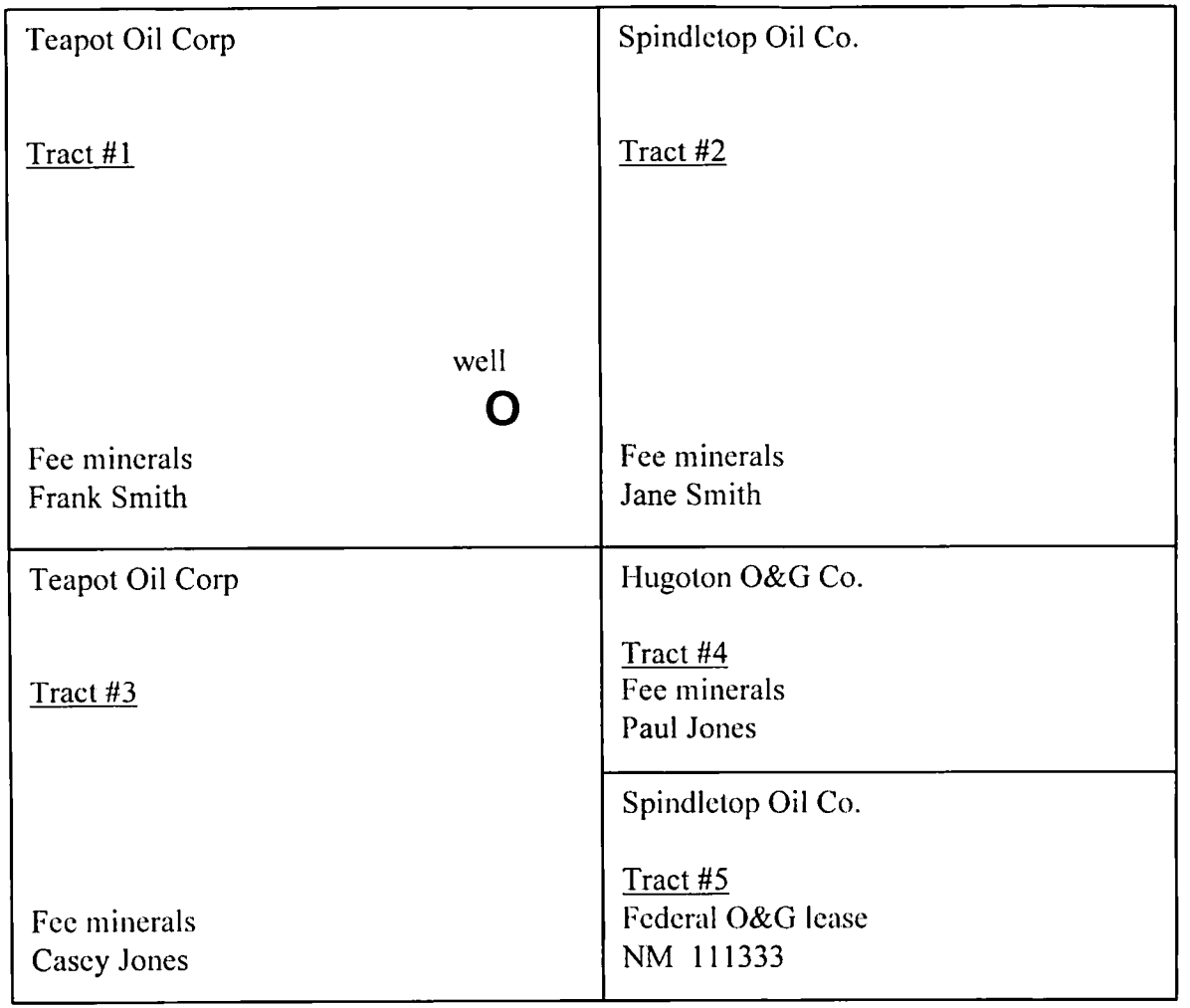
- A Communitization Agreement allows the drilling of a well ". . . when a lease or portion thereof cannot be independently developed in conformity with an established well-spacing or well-development program. . ."
- "Operations or production under such an agreement shall be deemed to be operations or production as to each lease committed thereto."
- CAs are formation-specific; may be overlapping CAs for different spacing configurations

Effect of Communitization

- Concept was developed as a means of preventing over-development of a reservoir (too many wells drilled under the "Rule of Capture"), which was expensive, and damaged the reservoir
- Production revenue and operating costs are allocated to each tract within the CA proportionally to the overall CA acreage
- Within each tract, production and costs are further distributed based upon lease terms (royalty rate) and any outstanding overriding royalty interests
- Unleased Federal or Indian minerals may be included in the CA (allocation is placed in escrow until minerals are leased)
- Pooling in Texas is unusual:
  - tracts in most of Texas are described by metes and bounds
  - the communitized area may be hundreds to thousands of acres, encompassing multiple metes and bounds tracts.

Example: Proposed well to test the "Viking" formation

Lessee name at top of Tract, mineral owner at bottom



This drawing depicts Exhibit "A", a plat of the regular, 640-acre spacing unit.
Tract #5, the S½ of the SE¼, is the only Federal oil and gas lease within the spacing unit
The operator of the proposed well submitted a Communitization Agreement for BLM to review.

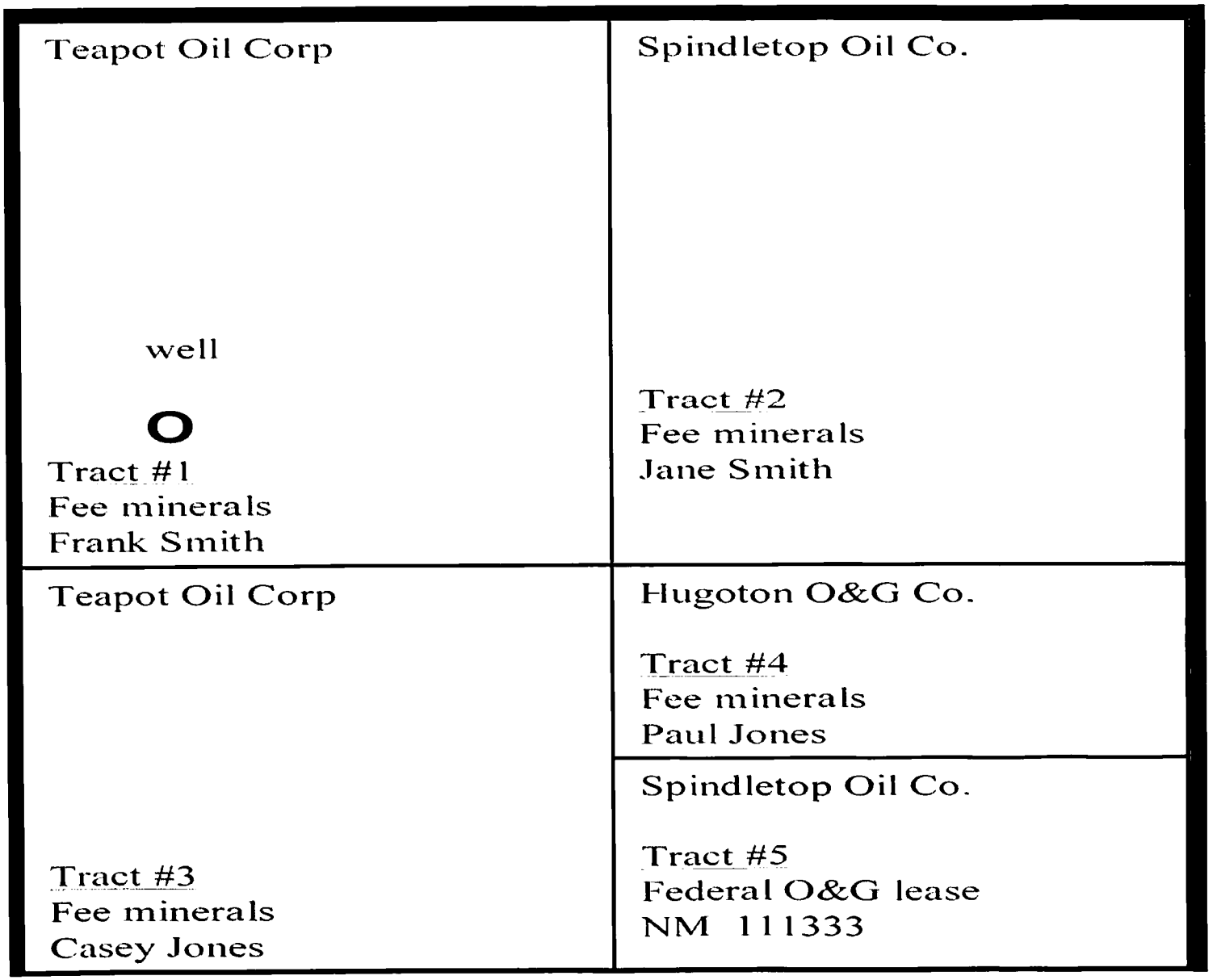
BLM Review of Proposed CA from Previous Slide

- Operator Submits proposed CA and Exhibits
  - Text of the communitization agreement
  - Exhibit "A" is plat of the CA
  - Exhibit "B" is list of Tracts and ownership/lease information
  - Exhibit "C" is allocation formula
- BLM Review ensures that the CA
  - conforms with State (or BLM)-established 640-acre spacing for gas production from the "Viking" Formation, (BLM does not have to adhere to State spacing rules. We may establish our own field rules, and in fact we must make an independent decision regarding spacing of Indian Trust minerals)
  - is in a legal location (proper minimum setbacks from spacing unit boundaries), or an exception location has been approved
  - approval is in the best interest of the USA or the Indian mineral owner

Processing, Continued

- The effective date of a CA is the earliest of-
  - The date approved
  - The completion date of the communitized well

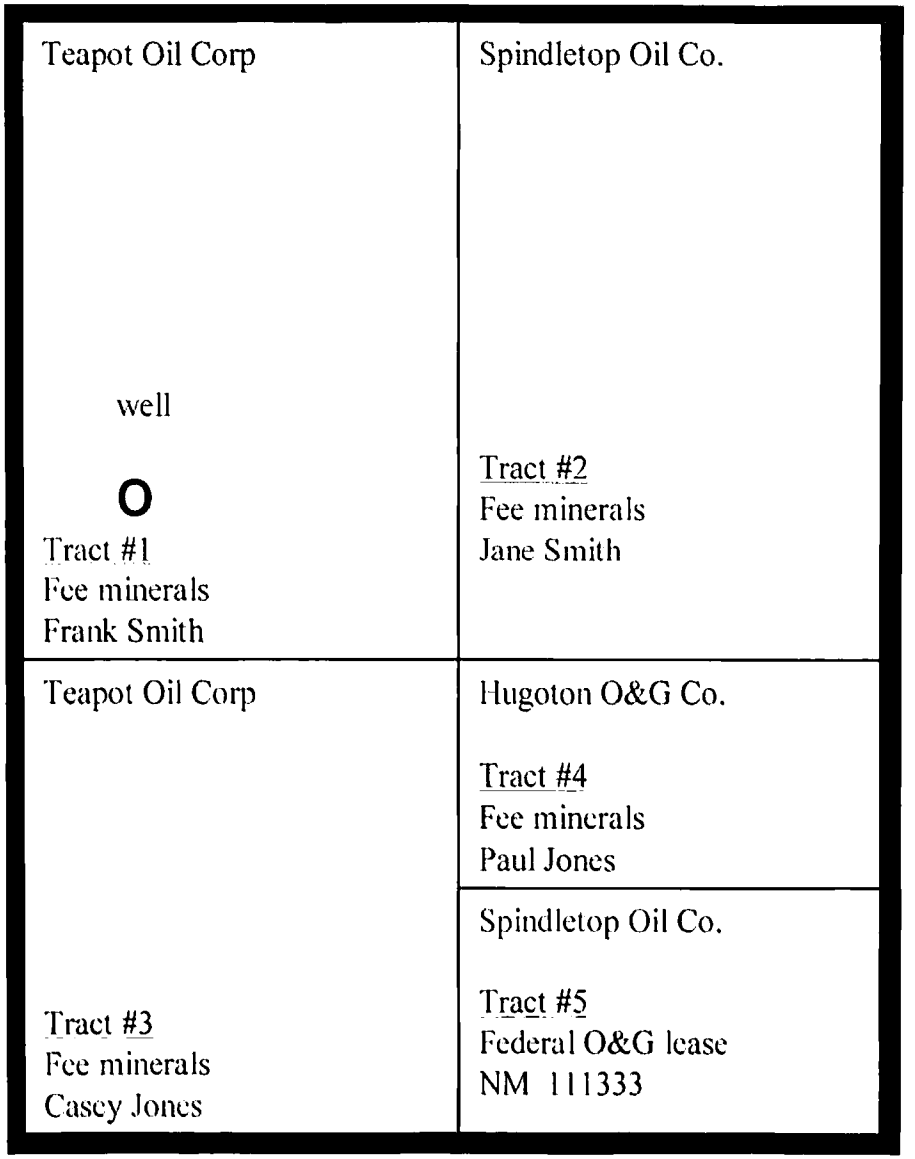
Example of a CA Plat



Lists Tract Ownership, including lessor, lease no., lessee, and any overriding royalty interest owners

Exhibit "B"

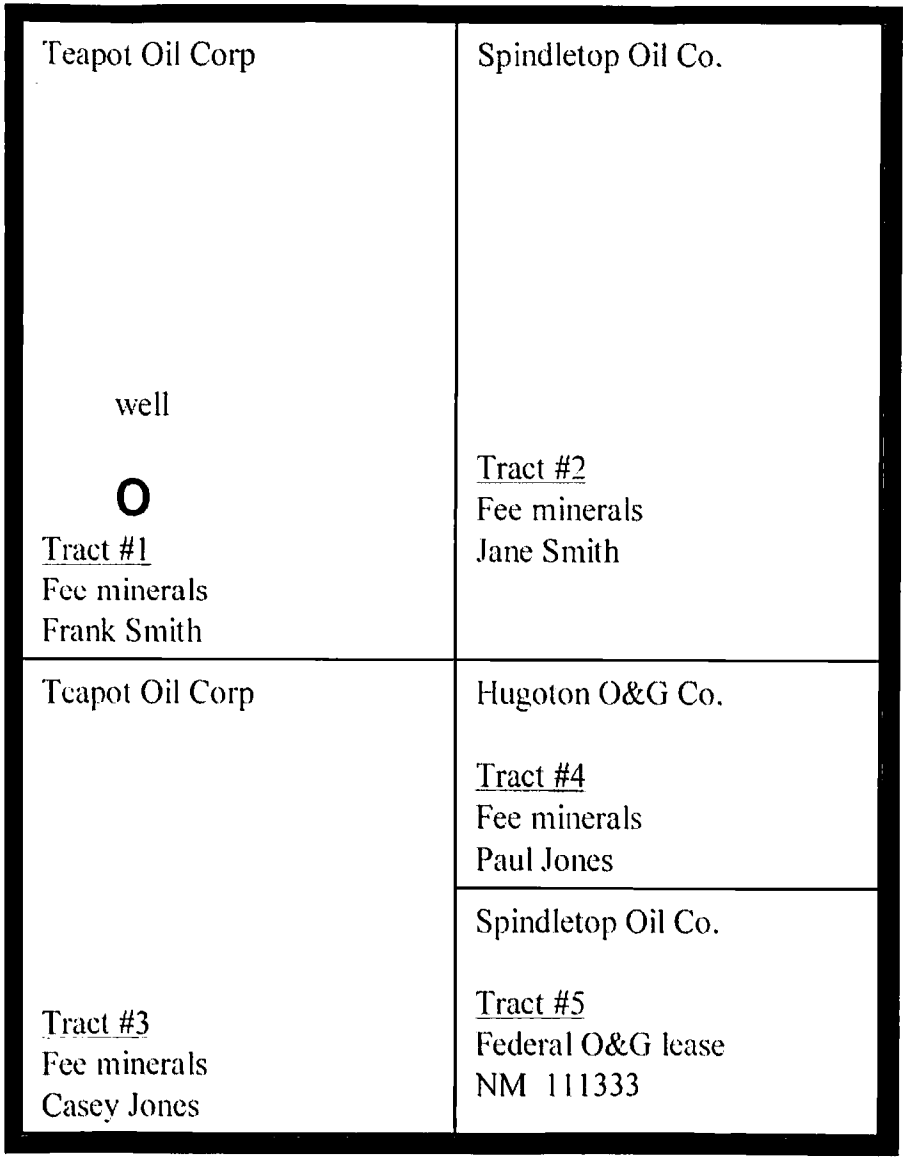
Tract No.	Legal Description	Lessor	Lease No., royalty rate	Lessee
1	T 10 N., R 10 W., sec. 14: NW¼, 160 acres	Frank Smith	F. S. 1 12.5%	Teapot Oil Corp
2	T 10 N., R 10 W., sec. 14: NE¼, 160 acres	Jane Smith	JS 23 15%	Spindletop Oil Co.
3	T 10 N., R 10 W., sec. 14: SW¼, 160 acres	Casey Jones	CJ 421 16.667%	Teapot Oil Corp
4	T 10 N., R 10 W., sec. 14: N½SE¼, 80 acres	J. Paul Jones	JPJ 17 12.5%	Hugoton O&G Co.
5	T 10 N., R 10 W., sec. 14: S½SE¼, 80 acres	USA	NM 111333 12.5%	Spindletop Oil Co.



Within each tract, allocated further down to lessor, based upon lease royalty rate, and any overriding royalty interest owners

Exhibit "C"

Tract No.	Allocation (fractional)	Lessee	Lessor
1	0.250000	Teapot Oil Corp 0.21875	Frank Smith (12.5% X .25) 0.031250
2	0.250000	Spindletop Oil Co. 0.212500	Jane Smith 0.037500
3	0.250000	Teapot Oil Corp .208334	Casey Jones 0.041660
4	0.125000	Hugoton O&G Co. 0.109375	J. Paul Jones 0.015625
5	0.125000	Spindletop Oil Co. 0.109375	USA 0.015625



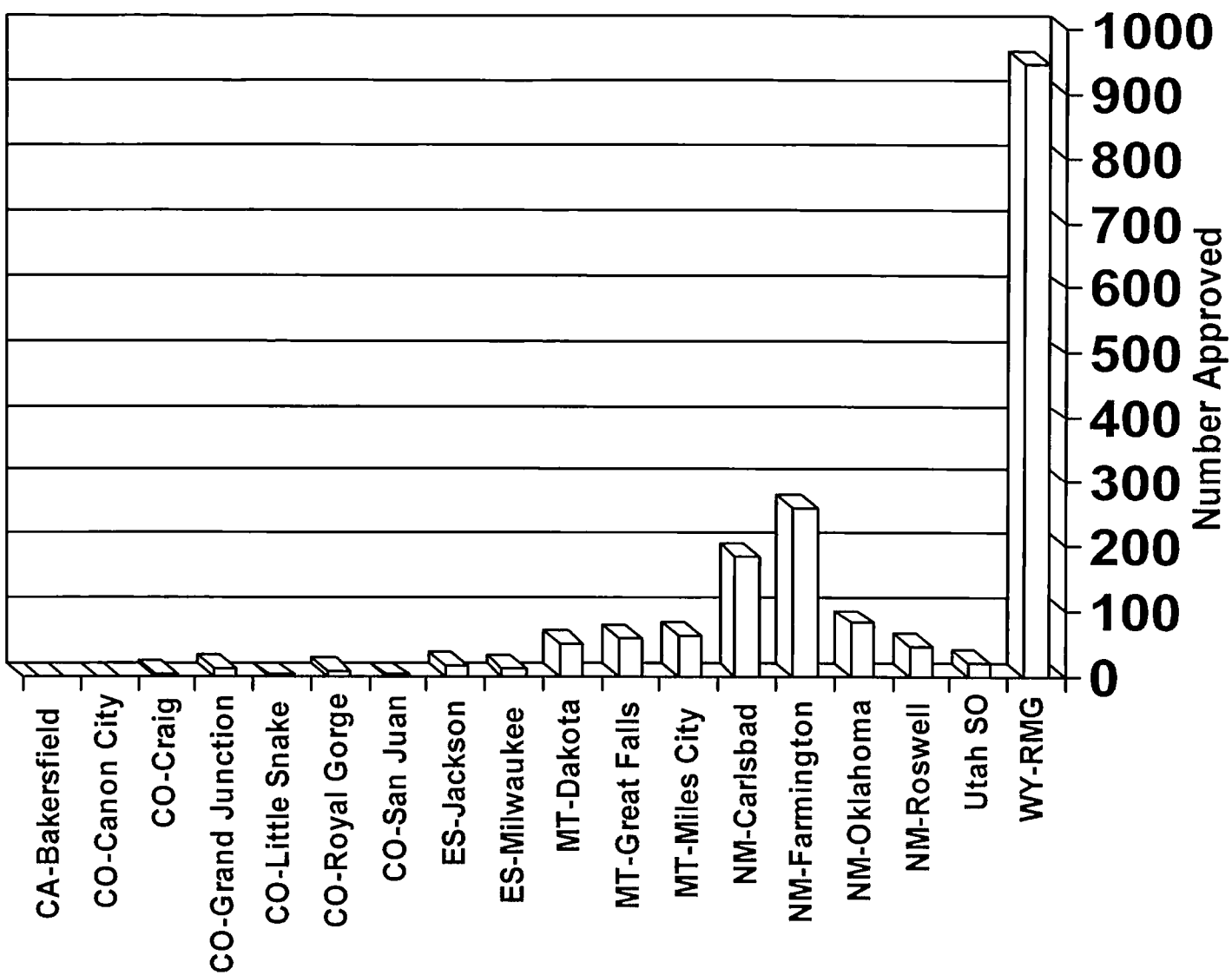
Specific Project on CAs

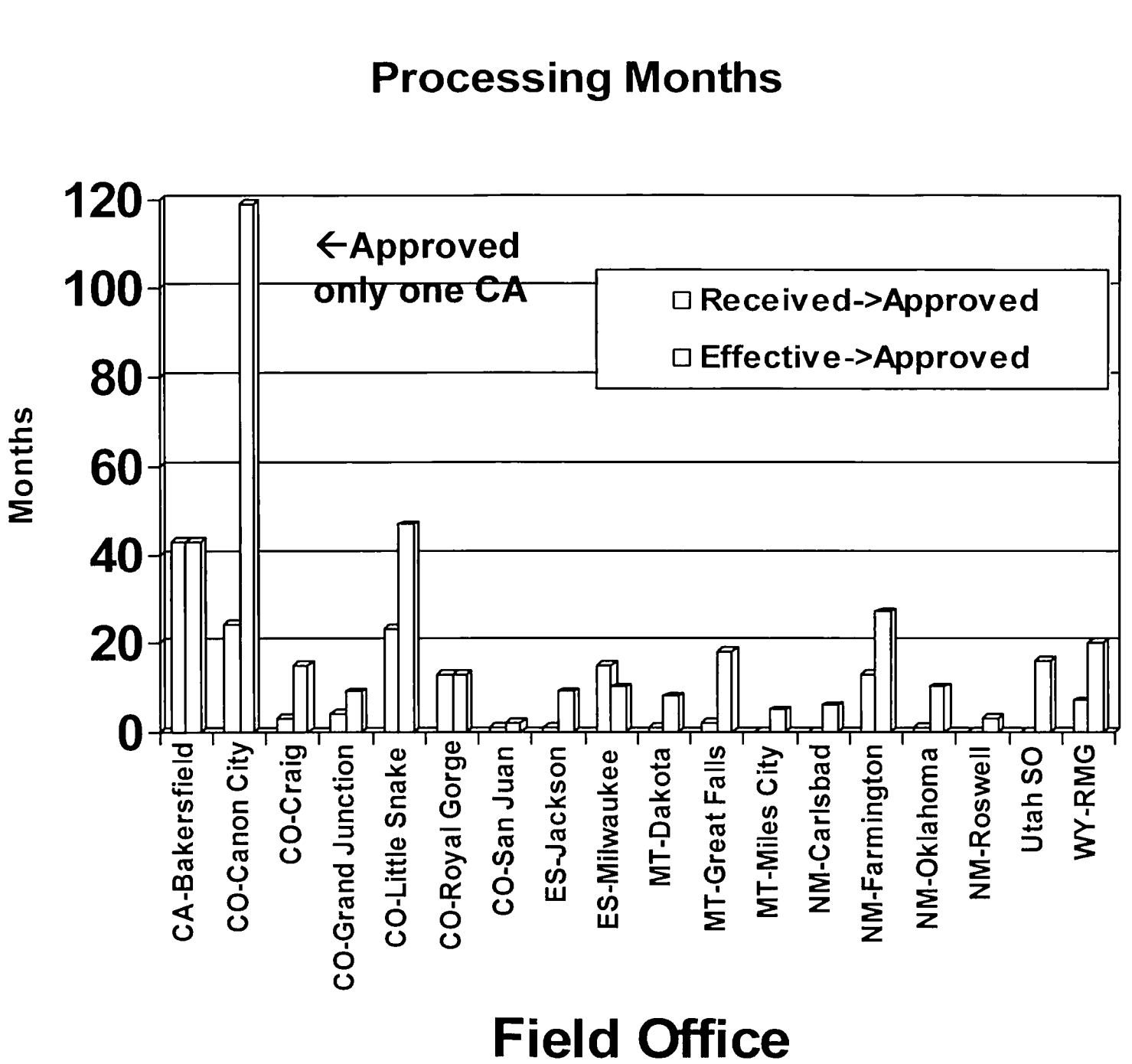
- Looked at period January, 2003 through March, 2006. Findings:
  - 1,778 Federal CAs approved throughout BLM
  - Nationwide, about 14% of CAs were submitted prior to the well being drilled
  - Over one-third of the CAs were approved within one month of receipt
  - Nearly 90% were approved with one year

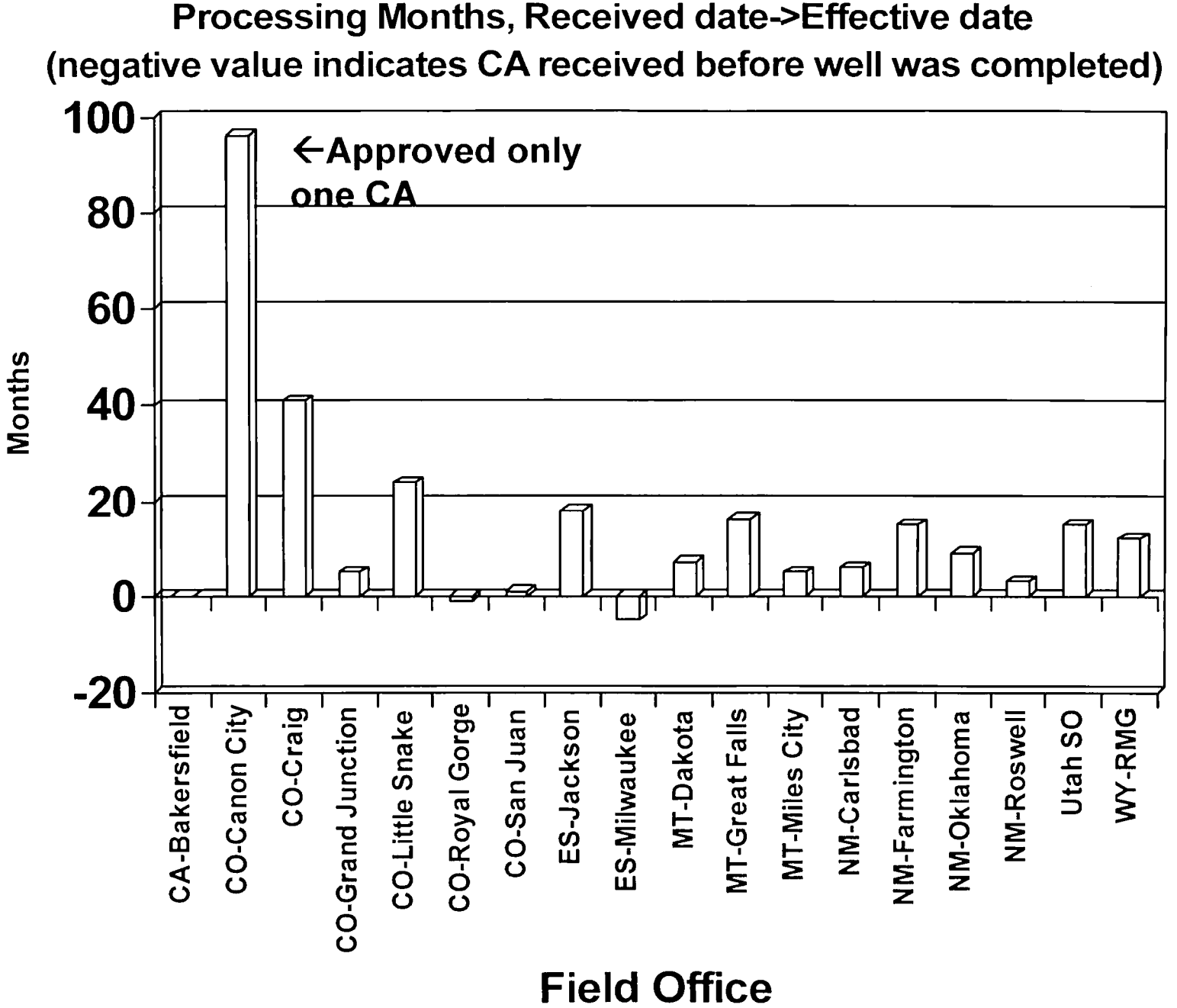
Wyoming Statistics

- CA submittal rate in Wyoming at peak was 27 per month
- CA approval rate was 26 per month
- backlog in January, 2003 was 157; reached a high of 274 in November 2004
- Present backlog is 180 applications
- Processing Unit Agreements and PAs, and preparing RFDs for RMPs higher priority than CAs
- Wyoming RMG has identified more than 1,100 potential CAs
  - CBNG is being developed on 80-acre spacing
  - Conventional gas wells are being developed on an 80-acre, lease-line basis in southwest Wyoming)

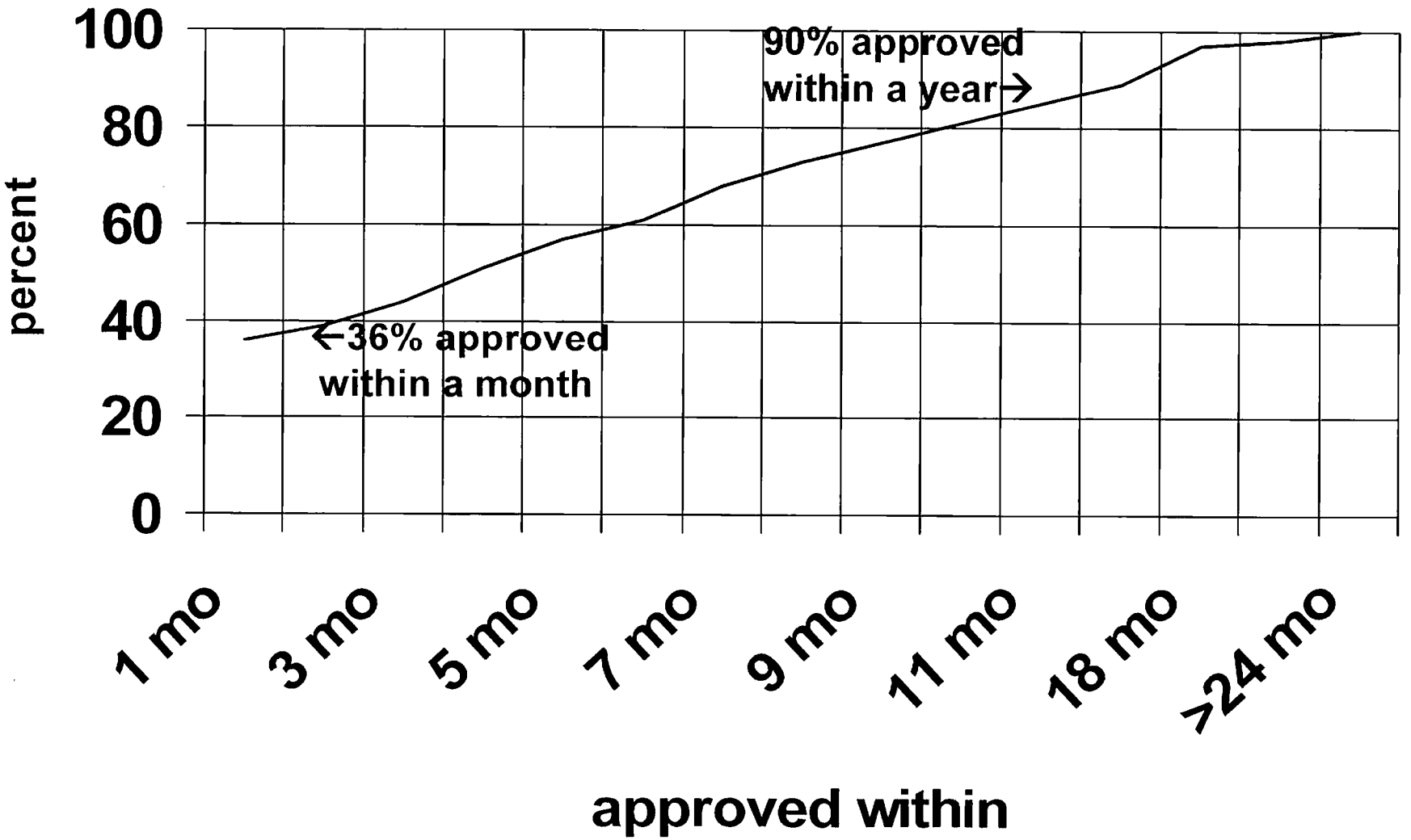
Number of CAs Approved, 2003-2006



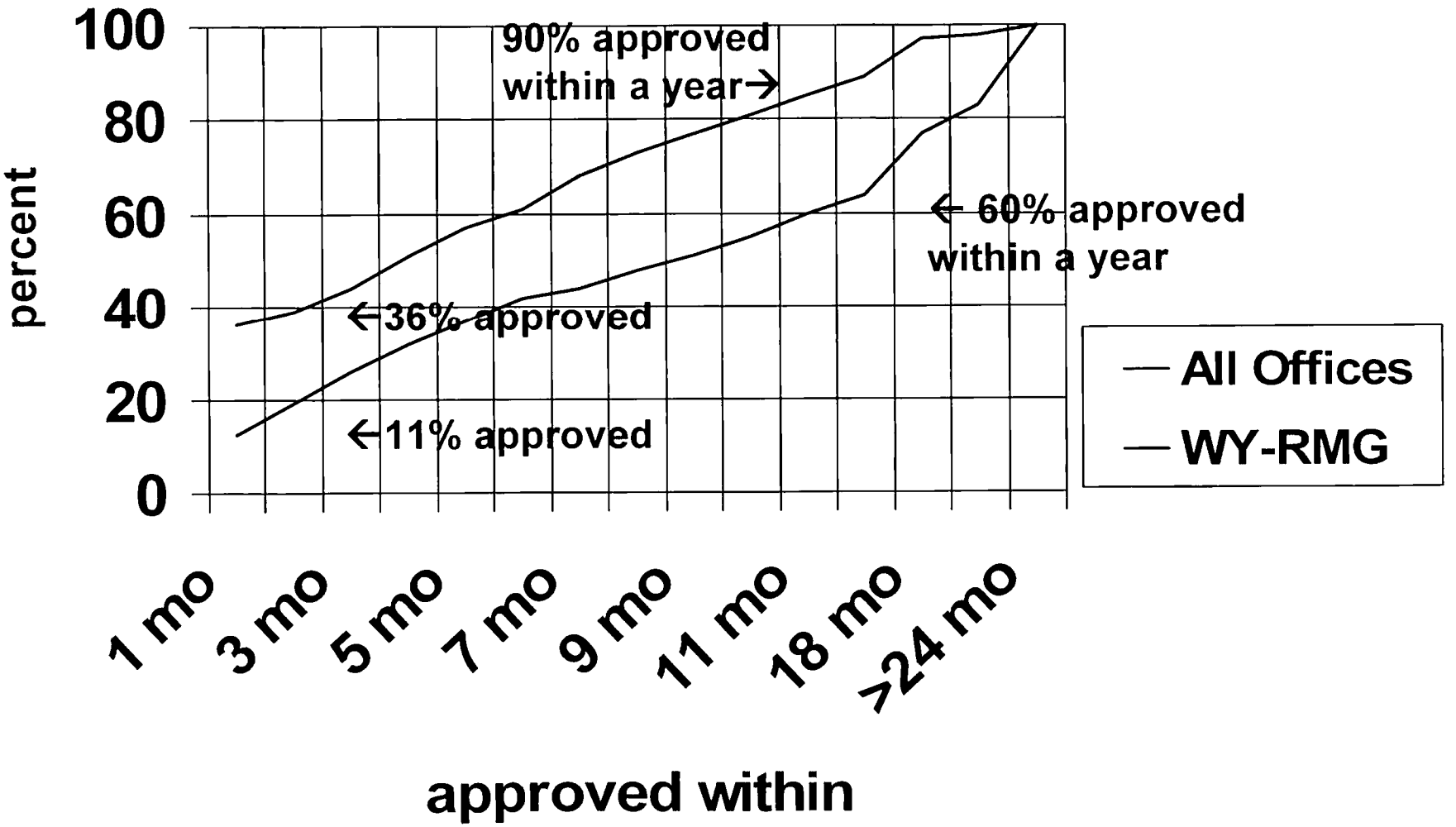

Processing Months
120
100
80
60
40
20
0
Months
←Approved
only one CA
Received->Approved
Effective->Approved
CA-Bakersfield
CO-Canon City
CO-Craig
CO-Grand Junction
CO-Little Snake
CO-Royal Gorge
CO-San Juan
ES-Jackson
ES-Milwaukee
MT-Dakota
MT-Great Falls
MT-Miles City
NM-Carlsbad
NM-Farmington
NM-Oklahoma
NM-Roswell
Utah SO
WY-RMG
Field Office


Processing Months, Received date->Effective date
(negative value indicates CA received before well was completed)
100
80
60
40
20
0
-20
Months
←Approved only one CA
CA-Bakersfield
CO-Canon City
CO-Craig
CO-Grand Junction
CO-Little Snake
CO-Royal Gorge
CO-San Juan
ES-Jackson
ES-Milwaukee
MT-Dakota
MT-Great Falls
MT-Miles City
NM-Carlsbad
NM-Farmington
NM-Oklahoma
NM-Roswell
Utah SO
WY-RMG
Field Office

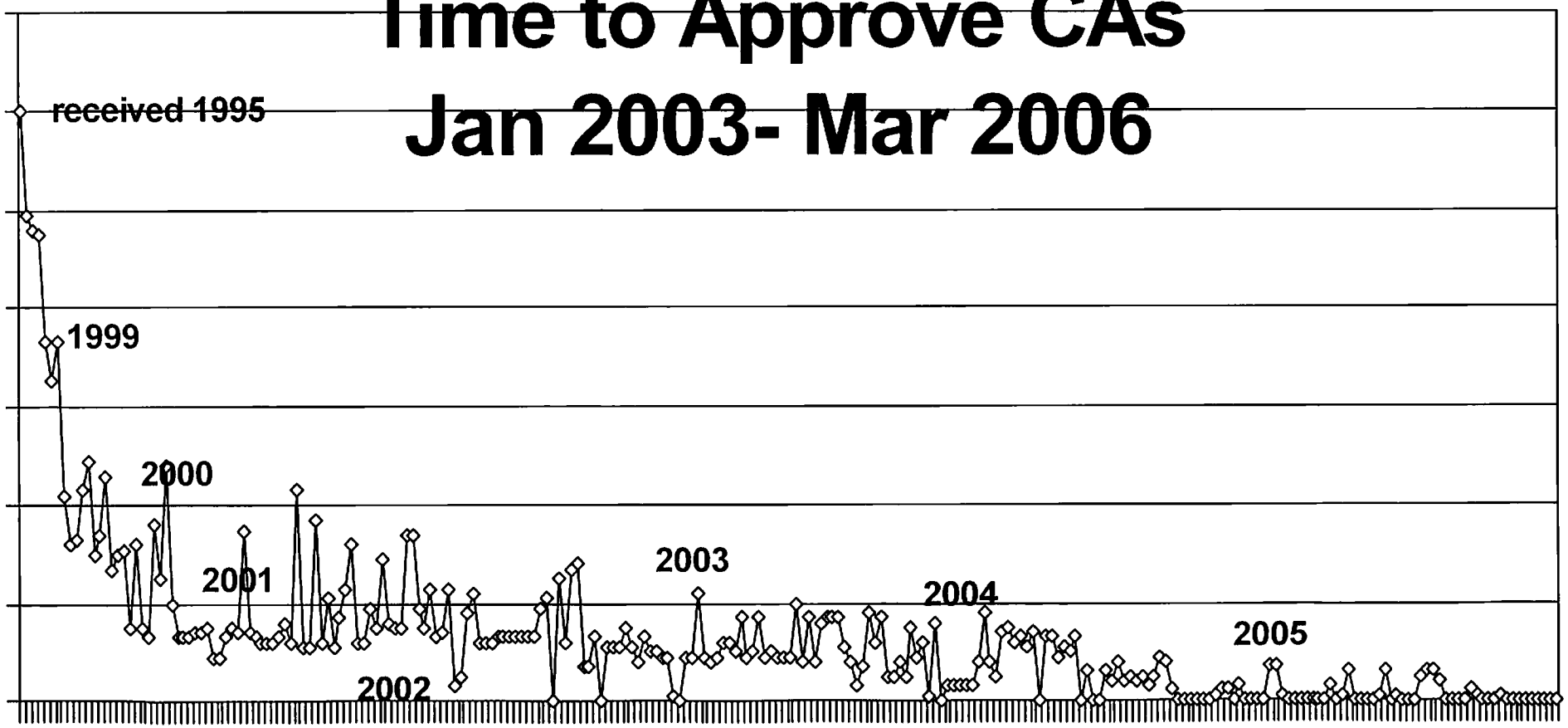
Time to Approve (all offices)



Time to Approve



Farmington
Time to Approve CAs
Jan 2003- Mar 2006



When CA application was Received

Some reasons for delay between effective date and approval date

- In some cases, the State or BLM must approve a spacing order before an application may be approved
- In most cases (>85%), the operator did not submit the CA until long after the well was completed; often, the submission is incomplete or has errors which must be corrected prior to approval
- If operator does not timely submit a CA, the field office will contact and require submission within 60 days
- In 2003-2004, RMG was swamped by CA applications for CBNG wells in Powder River Basin

Wyoming state Office –Reservoir Management Group (RMG)'s response to the Recommendations from the Oil and Gas Royalty Reporting Subcommittee of the Royalty Policy Committee (Committee)

In your **Communitization Agreements (CAs)** discussion in the **Reporting Royalties on Retroactively Approved PA and CA Agreements** section of the Committee's report, there are several errors, or at least wrong or misleading information in the first two sections. They include:

In your Background section. the last sentence in paragraph 2 does not reflect the CA process applied by the RMG in Wyoming. We do not require paying well determinations before approving CAs. Some of the CAs are approved prior to approval of an APD (seldom), the well completion (more often), for CBNG wells, prior to gas production, and most often, **after gas production**. The RMG indicates on their approval letter whether the CA well has been completed, is shut-in, is producing water, or is producing natural gas; copies of the approval letters are sent to MMS in Denver. CO.

In your BLM Research section, you state that most of the BLM offices approve fewer than 100 CAs a month and that the RMG had three offices that approved more than 100 CAs per month and that RMG averaged more than 900 per month. These numbers are in error. Table 1 shows the numbers and rates of CAs received and approved by the RMG from January 1, 2000 through August 31, 2006 shows average approval rates ranged from 3.5 to 37.2 CAs per month. Figure 1 graphically shows the number of CAs received, pending and approved by the RMG for the period January 1, 2001 through August 31, 2006. Please note the relatively abrupt increase in number of pending CAs in June 2002.

Table 1. Number of CAs received and approved by RMG in Wyomingfor selected periods from 1/1/2000 through 8/31/2006.

	Number			Average Number		
Dates	CAs Received	CAs Approved	Staff Working on CAs	CAs Received Per Month	CAs Approved per Month	Remarks
1/1/2000 – 3/31/2001	52	52	2	3.5	3.5	
4/1/2001 – 12/31/2001	81	96	2	10.1	12	
1/1/2002 – 6/30/2002	150	87	2	25	14.5	
7/1/2002 – 12/31/2002	153	101	2	25.5	16.8	
1/1/2003 – 6/30/2003	136	94	2	22.7	15.7	
7/1/2003 – 12/31/2003	175	214	4	29.2	35.7	
1/1/2004 – 6/30/2004	180	92	3	30	15.3	Did not work on new CAS for three months
7/1/2004 – 12/31/2004	121	109	4	20.2	18.2	Did not work on new CAS for one month
1/1/2005 – 6/30/2005	148	223	4	24.7	37.2	Initiated Self Certification of Signatures
7/1/2005 – 12/31/2005	142	199	4	23.7	33.2	
1/1/2006 – 8/31/2006	348	235	3	43.5	29.3	Initiated Self Certification of CA Language

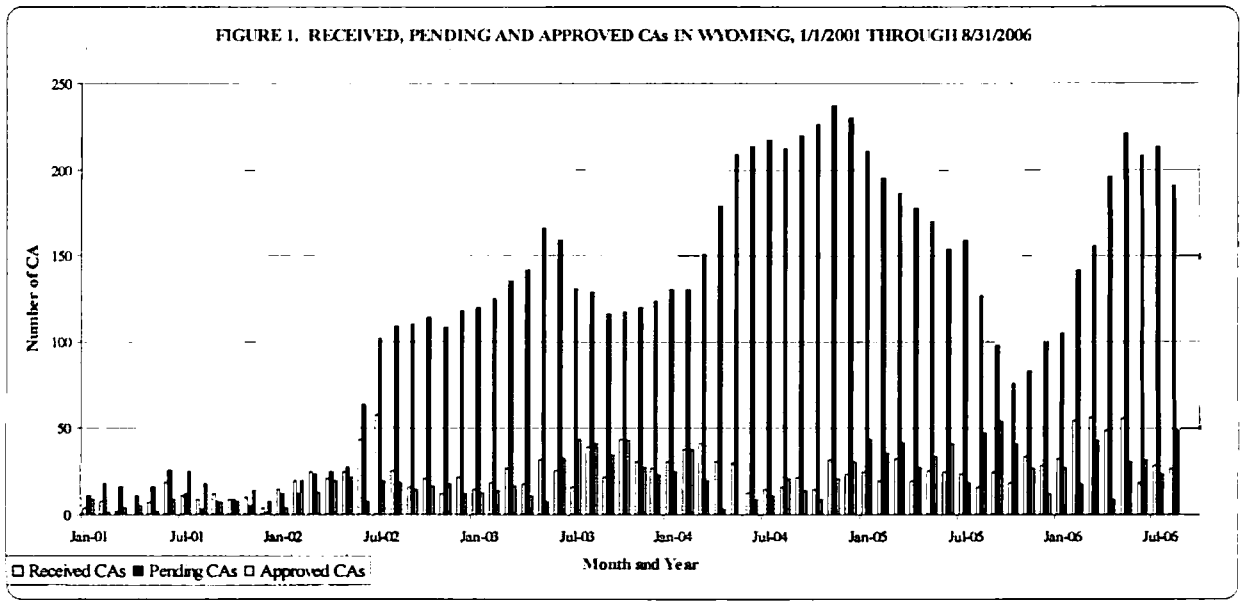


Figure 2 shows the number of CAs received and approved by the RMG for all of Wyoming's field offices from October 1, 2005 through August 31, 2006.

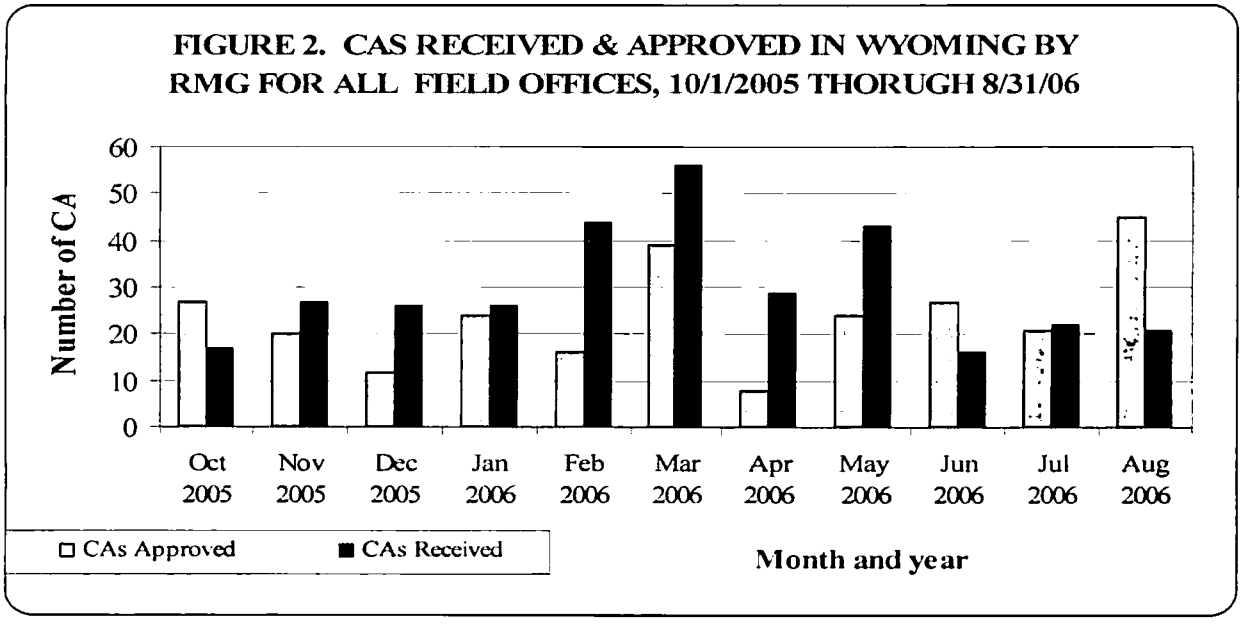
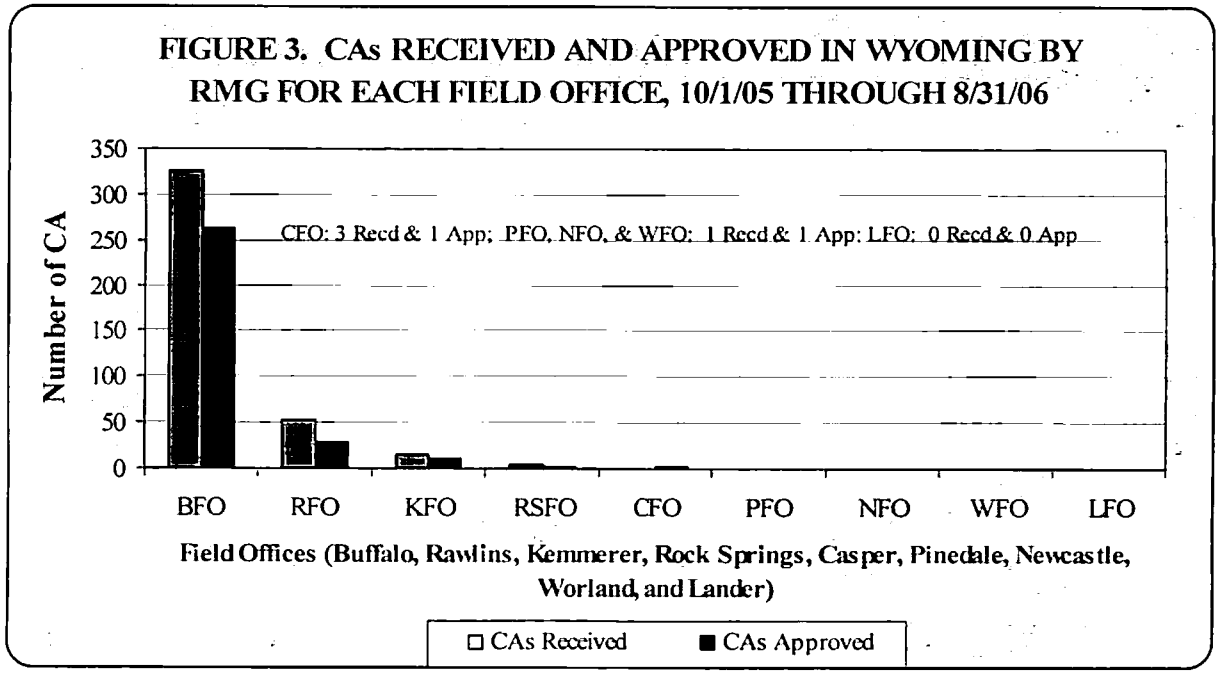


Figure 3 shows the number of CAs received and approved graphically for each of Wyoming's field offices. Please note that the Buffalo Field Office is by far the leader in number of CAs received and approved.



In response to the Subcommittee Recommendations section of the Committee's report, we have the following comments:

1. MRM to accept and process all royalty lines received for approved CAs regardless of whether a 1st production notice has been issued.. This may require a temporary workaround and potentially a future system change to allow these lines to clear automatically. BLM needs to issue an Instruction Memorandum (IM) on when 1st production notices should be sent especially on CBM wells when they know gas is involved.
   Response: In Wyoming, RMG's CBNG (CBM) CA approval letter indicates whether the CA well has been completed, is shut-in, is producing water, or **is producing natural gas**; copies of the approval letters are sent to MMS in Denver, CO. It is RMG's intention that the CA approval letter be used as an additional notification to MMS that gas is being produced.

2. BLM to develop procedure to monitor the timely submission of Communitization Agreements, and actively follow-up with operators.
   Response: In Wyoming, RMG actively monitors the submission of CAs and has aggressively contacted industry regarding CAs, hence the large backlog of unapproved CAs. These contacts are initiated by the RMG's Drainage and CA programs. RMG also has identified more than 1,000 additional potential CAs, and is contacting industry by phone and e-mail regarding these potential CAs.

3. BLM to review annually the status of field office approvals for backlog of CAs still needing approval, and for CA approval timelines to identify any prioritization and/or resource allocation issues.

Response: RMG reviews each communitization agreement as it arrives in our office and attempts to identify wells that already have long periods of production before the CA was received and process them first. RMG also has streamlined the CA approval process by allowing the operators to "Self Certify" that the requisite signatures required for approval have been obtained and to also "Self Certify" that the CA language of the submitted CA is identical to the Standard Communitizaton Form except for Sections 1, 5, 6, and 10, where applicable. This self-certification process has decreased the processing time for CAs by as much as 50 percent. RMG has identified and contacted management about the need for additional resources and several options are being considered. RMG continues to search for methods to streamline the process even more. As of September 21, 2006, RMG's CA backlog was 211.

4. BLM to identify opportunities where the importance of timely submission of CAs can be communicated to appropriate industry representatives (industry meetings such as RMMLF). This was not previously discussed during the Subcommittee meetings.
   Response : BLM is partnering with RMMLF in a Special Institute on Federal Onshore Pooling and Unitization in November 2006 where CAs will be addressed.

In the Committee's report on retroactively approved PA & CA Agreements of September 6, 2006, the Committee had concerns about the timeliness of CA approvals and the difference between the effective and approval dates. Part of these concerns can be attributed to the differences between the received and approved dates. There are several reasons and are addressed as follows.

1. The operators seldom initiate a CA until after the wells are spudded.
2. Obtaining the requisite signatures from all of the parties can take from two to six months. Sometimes the operator has to go before the Wyoming Oil and Gas Conservation Commission and "force-pool" some or all of the working-interest owners or sometimes the Bureau of Land Management has to force pool the interested parties with federal leases; these force pooling operations may take as many as three months.
3. When processing CAs, RMG frequently finds that the CA applications are incomplete (all requisite signatures were not included, the agreement language was incorrect, and land and title information are incorrect). When this occur, the operators are contacted by phone or e-mail for corrected information.
4. RMG has had a backlog of pending CAs since 2001; the backlog has ranged from one or two to as many as 240. .
5. Other RMG activities did not allow for full staffing for CA processing.

The following summarizes the Wyoming State Office Reservoir Management Group's CA program. Our CA program started to accelerate in January 2002 in response to the Wyoming Oil and Gas Commission establishing 80-acre spacing for coalbed natural gas (CBNG) development in the Powder River Basin in March 2001 (See Table 1, above). Please note the changes in the number of CAs received and approved increased after March 2001. RMG is presently processing CAs submitted in the last five months. Our CA backlog as of September 21, 2006 was 211; this number is a "moving target" owing to the rates that CAs are received and approved. Figures 4 and 5 show the projected rates that we anticipate CAs will be received and will be approved. Please note the differences between the projected rates for CAs that are received and approved, as many as 60 CAs per month may be receive by October 2008 whereas only 42 CAs per month are predicted to be approved by October 2008, assuming current staffing levels.

FIGURE 4. CAs RECEIVED JULY 04 THROUGY AUGUST 06

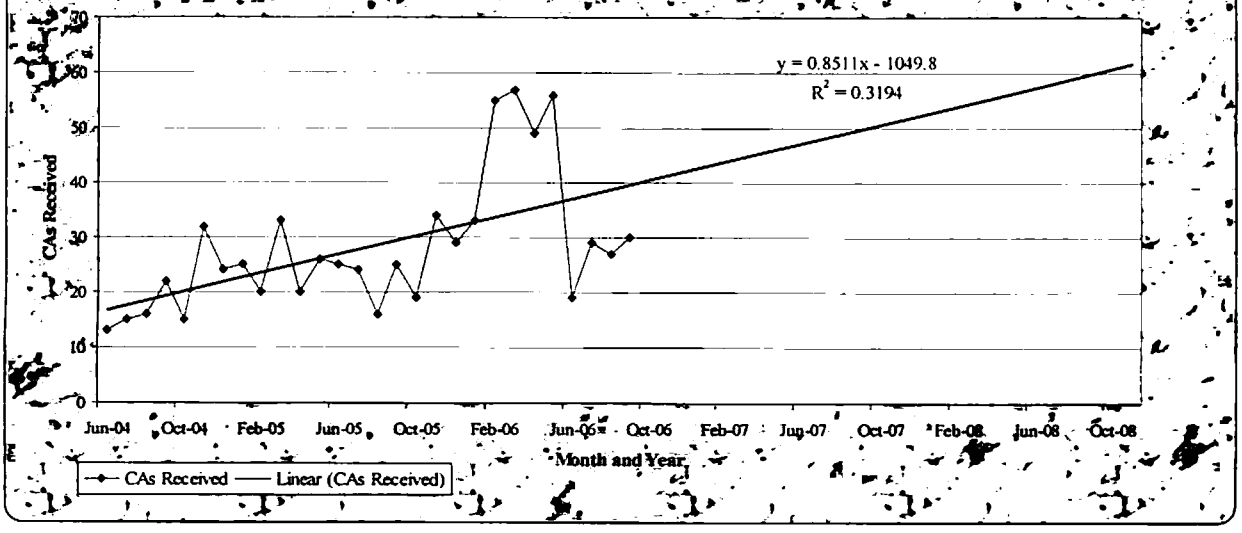


FIGURE 5. WYOMING CAs APPROVED JULY 04 THROUGH AUGUST 06

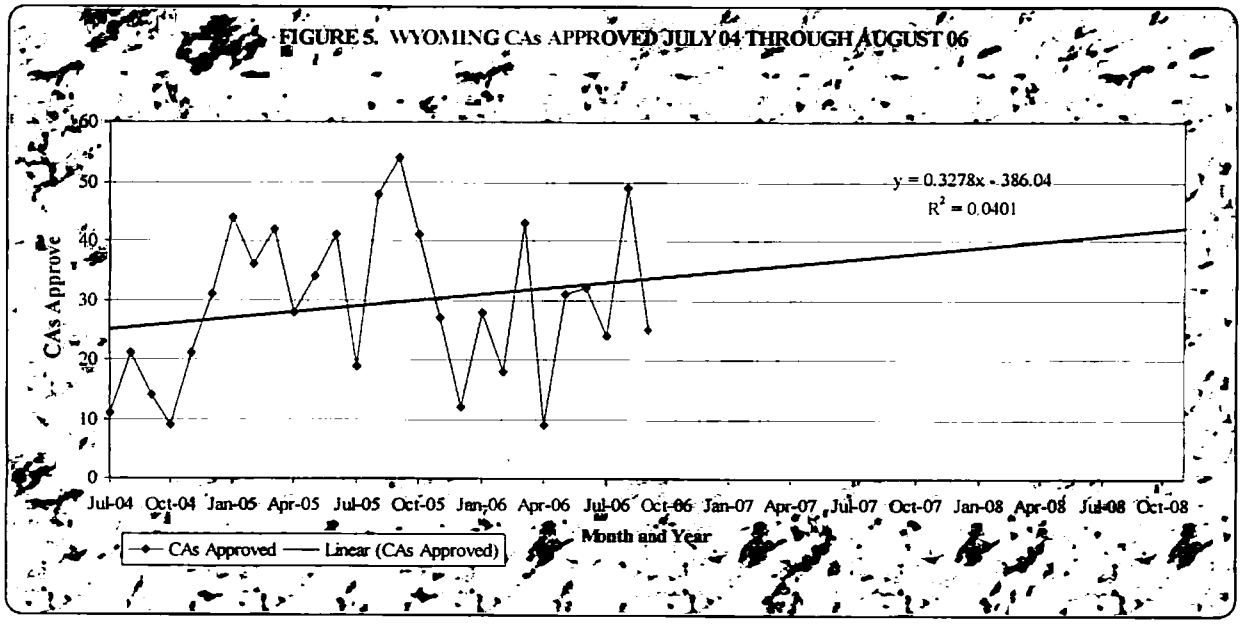
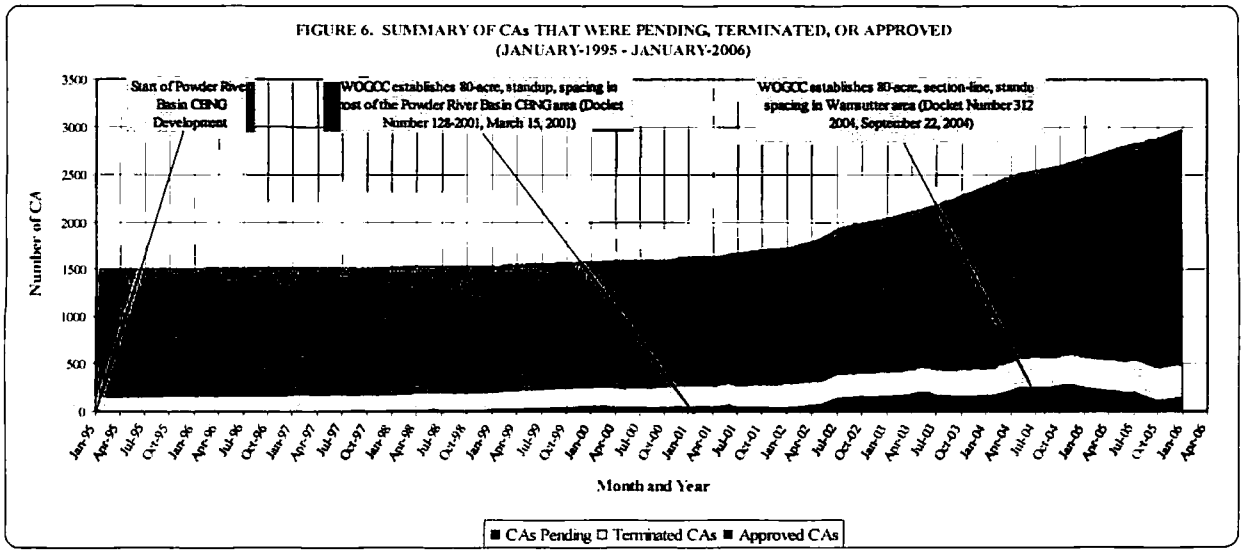


Figure 6 summarizes the terminated, pending, and approved CAs from January 1995 through January 2006.



In your **Unit Participating Areas (PAs)** discussion in the **Subcommittee Recommendations** section of the Committee's report, we have the following comments:

1. BLM to develop procedure to monitor the timely submission of Unit Participating Areas, and actively follow-up with operators.
   Response: In Wyoming, RMG has a system in place that utilizes an Access database as a tracker for unit activity including the initial obligation well(s) and subsequent wells drilled after the initial PA(s) have been established. RMG updates this data base on a daily basis and notifies the operators of the need for a paying-well determinations and/or for PA applications.

2. BLM to review annually the status of field office approvals for backlog of PAs needing approval and PA approval timelines to identify any prioritization and/or resource allocation issues.
   Response: In Wyoming, RMG actively monitors the status of PAs and contacts the operators in a timely manner. We continually reprioritize pending PWD and PA applications as they are processed. RMG continues to search for methods to streamline the process even more. At the present time, RMG does not have a significant backlog of unapproved PWDs or PAs.

3. BLM to talk to the Reservoir Management Group in Wyoming to determine if PWD requirements can be changed in the Powder River Basin. This may require an amendment to the Unit agreements. Instead of PWD on a well basis, perhaps they could be done on a group of wells.
   Response: In Wyoming, RMG has designed a coal bed natural gas specific Exploratory Unit Agreement. In Section 9, Initial Drilling Obligation, we use multiple well requirement because a single well will not efficiently develop a coal bed natural gas deposit. Portions of the language are given below:

A. **CBNG Productivity Requirement**: The CBNG unit language provides that one well or a combination of wells must meet a productivity requirement in order to qualify to be placed into a PA. To meet the productivity requirement, the operator must show, in the initial PA application, that a single well produces or a combination of wells cumulatively produce specified amounts of gas for a period of fifteen consecutive days. In most CBNG units. the gas volume required for a single well to meet the productivity requirement is seventy five (75) thousand cubic feet per day. In most CBNG units. the cumulative gas volume required for a combination of wells to meet the productivity requirement is three hundred (300) thousand cubic feet per day. In certain circumstances. these CBNG volume requirements may change.

Determination of the productivity requirement for multiple wells developed on 40- to 80-acre spacing requires that an individual well capable of producing unitized substances have no more than two thousand (2,000) feet between it and adjacent wells capable of producing unitized production or dewatering that enhances production of unitized substances from another well.

Determination of the productivity requirement for multiple wells developed on one hundred sixty (160) acres requires the wells must be located in proximity to each other so that no more than four thousand (4.000) feet distance exists between the wells.

B. **CBNG Participating Area Methodology**: Because of the large number of CBNG wells that are projected to be drilled in Wyoming, the RMG determined a methodology for defining the participating boundary. This reduces the administrative workload of both the unit operator and the BLM by: 1) providing a simple mechanical method of defining initial and revised PA boundaries, and 2) reducing the number of PA applications for both initial and revised PAs. This methodology is summarized below:

The language for the CBNG unit agreement requires that a mechanical circle approach be used for the PA boundary definition. The lands included in the initial PA and subsequent revisions are regarded as reasonably proved to be productive. The methodology for CBNG wells drilled on 40- or 80-acre spacing is different for CBNG wells drilled on 160-acre spacing. For 40- or 80- acre spacing, the productive lands will be all 40-acre subdivisions, or aliquot equivalents, that are cut by ¼ mile (1,320') radius circle drawn around any well completed as a well capable of producing unitized substances or as a dewatering well necessary for the production of unitized substances in the participating area. The effective date of the initial PA is the date of first sales.

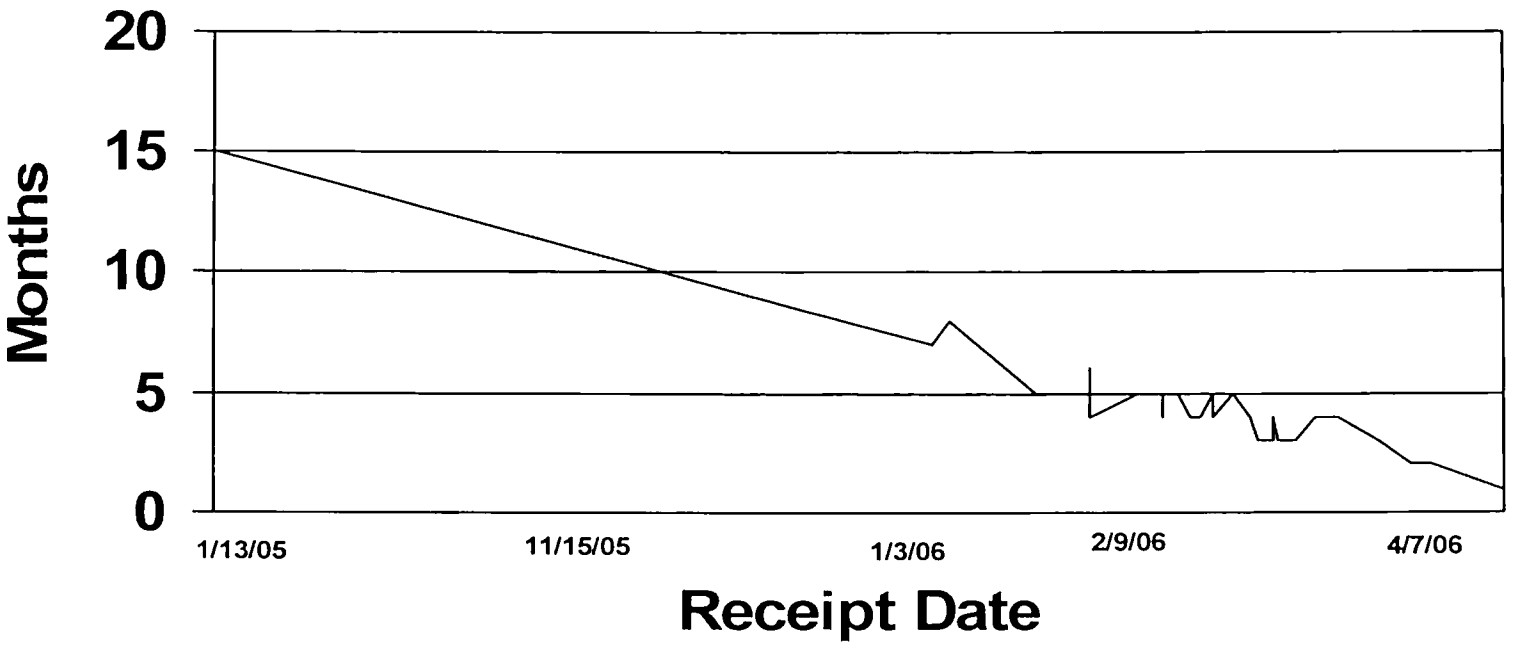
For 160-acre CBNG well spacing, the CBNG unit agreement language still provides for the use of the mechanical circle method. However, to meet the productivity requirement for multiple wells within a participation area, the unit agreement terms were amended to provide that the distance between wells shall be no more than four thousand (4,000) feet, instead of two thousand (2,000) feet. In addition, the circle radius measurement around the location of any well used to define the lands included within a participating area shall be amended to two thousand (2,000) feet instead of the one-quarter mile (1,320'). Revisions of participating area boundaries may be requested when additional wells are completed outside existing participating area boundaries when they are within

four thousand (4.000) feet of existing participating area boundaries, or of any other well to be included in a revised participating area boundary.

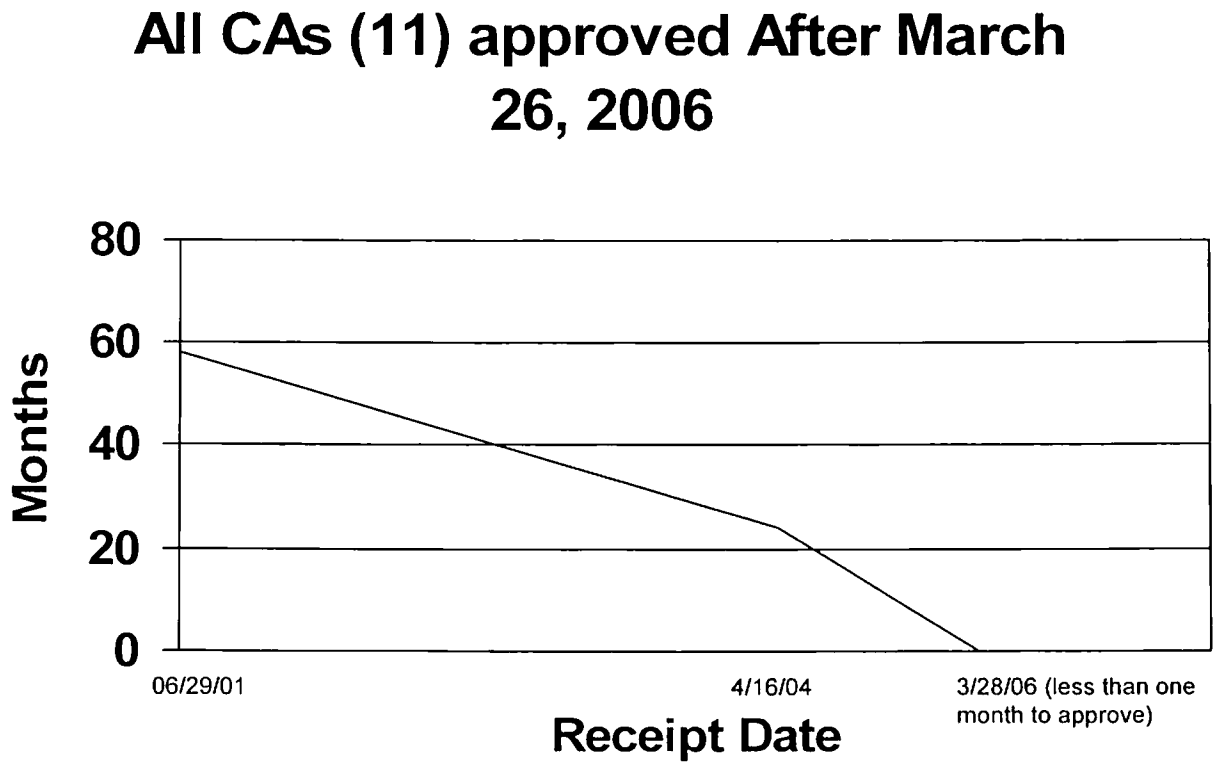
4. BLM to identify opportunities where the importance of timely submission of PAs and PWDs can be communicated to appropriate industry representatives (industry meetings such as RMMLF). This was not previously discussed at the Subcommittee meetings.
   Response : BLM is partnering with RMMLF in a Special Institute on Federal Onshore Pooling and Unitization in November 2006 where PAs will be addressed.

Updated Chart of Reservoir Management Group Processing Time

All CAs (47) approved after March 26, 2006



Updated Chart of Farmington Field Office CA Processing Times



January 13, 1995

3160 (922.PL)

LAN Transmission
Instruction Memorandum No. MT-95-023
Expires: 9/30/96

To: District Managers

From: State Director

Subject: Policy on Coalbed Methane Wells

The Miles City District Office has received several applications for permits to drill coalbed methane wells. Some of these leases are approaching lease expiration dates. Due to the nature of coalbed methane gas wells, the current policy on lease extension may not apply.

The production characteristics of coalbed methane gas wells are radically different from gas wells completed in conventional reservoirs. A coalbed methane well is defined as any well completed in one or more coal seams. In many cases the gas within these coal seams cannot be produced without first reducing the hydrostatic pressure by removing some of the water from the coal seam. As the hydrostatic pressure is reduced in the coal seam, the desorption of methane gas from the internal coal surfaces frees the gas to be produced. Despite the fact that the water is never completely removed from the coal seam, this production of water is commonly referred to as "dewatering."

Coalbed methane wells are typically characterized by relatively high initial water production rates and relatively low initial methane production rates. Over a period of time, the water production rate decreases and the methane production rate increases. Eventually, the methane rate peaks and then begins to decrease as depletion of the sorbed methane becomes the controlling factor. The peak methane gas production rate may occur within a few days or may take as long as 2 years after water production begins. The net effect is that, unlike a conventional gas well, the paying production capability of a coalbed methane well, as demonstrated by actual methane production, can only be determined much later in the life of the well.

However, the current policy states that if a lease does not contain a well capable of producing in paying quantities during the period that the lease is beyond its primary term, the lease may expire. If this policy is applied to coalbed methane wells, most leases with coalbed methane wells will expire during the initial high water and low gas production period. The following is the Montana lease extension policy that will apply only to coalbed methane wells.

A lease containing a well completed in a coal seam that is continuously producing water but has not yet begun to produce methane in paying quantities, will be determined to be a lease capable of production in paying quantities and considered held-by-production (HBP). Additionally, if the authorized officer (AO) determines, based on the relevant data, that a well would produce methane in paying quantities upon the reduction of hydrostatic pressure by the production of water from the well, the lease can be considered HBP. Upon the determination that a lease is capable of production in paying quantities, a first production memorandum would be prepared and forwarded to Fluids Adjudication and the Minerals Management Service.

When a well that is holding a lease by continuously producing water ceases water production operations without prior approval from the AO, a 60-day letter must be sent to the operator. The operator would be allowed 60 days within which to commence operations and provide evidence that the well is capable of producing gas in paying quantities, or the lease would be terminated in accordance with 43 CFR 3107. The wording in the standard 60-day letter must be amended to include appropriate language for situations involving coalbed methane wells (see Attachment 1).

Any venting of gas or disposal of produced waters associated with continuous water production from the coal seam must be approved in accordance with NTL-4A and Onshore Oil and Gas Order No. 7. Also, if a well is drilled over the lease expiration date, the field office must make a determination whether the activities of the operator constitute actual drilling operations on the lease in accordance with BLM Manual Handbook H-3107-1, Continuation, Extension, or Renewal of Leases.

Nothing in this IM is intended to change or circumvent appropriate reviews for potential impacts to the surface or subsurface resources such as surface or ground water. Also, this policy does not apply to Indian leases.

If you have any questions, please contact Pascual Laborda at (406) 255-2862

Signed by:
Thomas P. Lonnie
Acting

Authenticated by:
Marianne Schappek

1 Attachment
1-Sample Coalbed Methane 60-day letter (1 pp)

Distribution
WO-610, LS, Rm. 510 - 1
SC-325 - 1
RAHS - 1
SOMT - 1
Durango DO, Attn: Jim Lavato - 1
MT-931, Attn: Tim Bozorth

United States Department of the Interior

BUREAU OF LAND MANAGEMENT
Montana State Office
222 North 32nd Street
P.O. Box 36800
Billings, Montana 59107-6800

3100 (922.W)

June 6, 1996

Instruction Memorandum No. MT-96-056
Expires: 09/30/97

To: District Managers
Area Manager, Great Falls

From: State Director

Subject: First Production Memoranda for Leases, Unit/Communitization Agreements

This memorandum does not apply to the Butte District

The purpose of a First Production Memorandum (FPM) is to inform the MSO when a lease enters producing status. It also prompts the MSO to notify the Minerals Management Service (MMS) that the lease account should be transferred from rental status to royalty/minimum royalty status. Since all of the recent directives from the Bureau emphasize the importance of re-designing any process, if possible, to improve efficiency, we believe the process of preparation of the FPM for lease, unit and communitization agreements (CA) may be streamlined.

According to our original instructions on an FPM, IM MT-90-197 (Attachment 1), an FPM must be prepared by the field office after a CA/unit becomes productive. Most of the information needed to prepare a unit/CA FPM is obtained from the unit/CA approval letter. The only additional information that would have to be provided is a list of leases receiving actual or allocated production.

Therefore, in order to streamline the process of preparation of the unit/CA FPM, we decided that the unit and CA approval letter may also be utilized as a FPM. This will eliminate the need for the field offices to prepare a separate FPM, and will allow the MMS to more quickly learn which leases will be affected by the unit/CA approval.

The following are detailed instructions for each situation:

1. <u>FPM for a lease, or non-producing CA</u>

When a lease or non-producing CA becomes productive, a FPM is required. The instructions in IM MT-90-197 remain appropriate, except that the following information no longer needs to be provided:

- well's total depth and surface elevation;
- producing formation and intervals;
- reported formation tops;
- initial daily production;
- well capability and status.

2. Approval of secondary unit, unit expansion or unit participating area (PA).

The field offices will no longer be required to prepare an FPM. The unit approval letter prepared by the Reservoir Management and Operations Section will serve as the FPM. The information concerning which federal and/or Indian leases will be held by allocated/actual production will be added to the unit approval letter. The unit effective date will be used as the first production date for the unit.

Attached is a general form letter we propose to use that will provide both unit approval information, and serve as the FPM (Attachment 2). As you can see, the approval letter will be modified to include a list of leases that will be held by allocated production, and those for which FPMs for actual/ allocated production have already been prepared.

3. Producing communitization agreement

For a producing CA, the field offices will no longer be required to prepare an FPM. The CA approval letter will serve as the FPM through inclusion of the following additional information:

a. Well completion date;
b. Well name/number and location; and
c. Identification of leases that will be held by actual or allocated production.

This memorandum supersedes IM MT-90-197 (Attachment 1). If you have any questions, please contact Chun Wong, at (406) 255-2857.

Signed by:
Francis R. Cherry, Jr.
Acting

Authenticated by:
Aleta Zahorodny (MT922)

2 Attachments
1-IM MT-90-197 (12 pp)
2-Sample Unit Approval/FPM for Secondary Unit (2 pp)

cc:
WO(300), MIB., Rm. 5627
All State Office (920)
MMS, Royalty Management Program, P.O. Box 25165, Denver, Colorado 80225

922:CWong:jk:6/3/96:x2805:922/UNIT_FPM.CHN