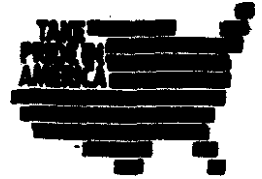




United States Department of the Interior



IN REPLY
REFER TO:

MMS-RVS-SM

MINERALS MANAGEMENT SERVICE
ROYALTY MANAGEMENT PROGRAM
P.O. BOX 25165
DENVER, COLORADO 80225
Mail Stop 653

3/23/89
MAR 23 1989

Dear Payor:

New valuation and related regulations for coal became effective March 1, 1989, and will apply to production occurring on or after that date. These regulations are at 30 CFR 202, 203, 206, 210, and 212. They were published in the Federal Register on Friday, January 13, 1989, at 54 F.R. 1492-1532. As a result of the issuance of these regulations, certain new instructions to royalty payors on Federal and Indian leases are required. These instructions relate specifically to product valuation and allowances, including a new requirement that the payor submit separate forms documenting transportation and washing allowances claimed on Form MMS-4014. These instructions, together with copies of the new allowance forms and details on how to complete them, are enclosed. Listed below are the various enclosures and the subjects covered:

Enclosure

1. General Instructions, Including Changes Required by New Regulations

A. Allowances

1. Due Dates for Allowance Reports
2. Mailing Address for Allowance Reports
3. Interest Charges/Losses of Previously Claimed Allowances
4. Calculating Allowances
5. Reporting for Transportation and Washing Allowance Adjustments
6. MMS Contact Point--Allowance Issues and Reporting Forms

B. Valuation

1. Change to Ad Valorem Lease Valuation Standards and Reporting

2. Potential Future Change in Royalty Reporting, Form MMS-4014
3. MMS Contact Point--Valuation Issues
2. Coal Transportation Allowance Report (Form-4293) and Instructions
3. Coal Washing Allowance Report (Form MMS-4292) and Instructions

Questions related to valuation or allowance issues should be directed to the Minerals Management Service contacts provided in Enclosure I. Questions related to Form MMS-4014 reporting should be directed to your Lessee Contact Branch representative. If your representative is unavailable or unknown, you may contact the Lessee Contact Branch at (303) 231-3288.

Sincerely,

Jerry D. Hill
Associate Director for
Royalty Management

3 Enclosures

A. Allowances1. Due Dates for Allowance Reports

Before a transportation or washing allowance may be claimed on Form MMS-4014, the appropriate allowance report, including schedules as required, must be submitted to the Minerals Management Service (MMS). (See Enclosures 2 and 3 for copies of the reports and detailed completion instructions.) Allowances may be claimed retroactively for a period not more than 3 months prior to the first day of the month in which the allowance report is filed with MMS, unless MMS approves a longer period upon a showing of good cause by the lessee. Where the lessee wishes to apply for an extension of the 3-month limit, it should submit its application, with supporting documentation, to MMS at the address shown in item A.6. of this enclosure. Thus, without special dispensation by MMS, in order for a lessee to claim allowances for March 1989, it must submit the applicable allowance reports to MMS by July 31, 1989. The allowance would continue in effect until the end of the calendar year or when the contract or rate ends or is modified, whichever is earlier.

After the initial reporting period, the allowance report must be submitted within 3 months after the end of each calendar year, or after the applicable contract or rate terminates or is modified, whichever is earlier, unless MMS approves a longer period. During the period between the end of the previous allowance reporting period and the submittal of the new allowance report (assuming it is filed timely), the lessee shall continue to report, on Form MMS-4014, the allowance from the previous reporting period.

Those transportation and washing allowances in effect as of March 1, 1989, will be allowed to continue until they terminate. (Allowances are "in effect" if written MMS approval has been given for an allowance for a time period that has not yet expired.) For allowances that are in effect as of March 1, 1989, and until the existing approval terminates, the lessee need do nothing to validate the allowance claimed on Form MMS-4014.

However, the lessee may, at any time in advance of the termination date and after the effective date of the regulations, submit the new allowance forms and begin reporting accordingly on Form MMS-4014.

For those lessees whose allowances are on a calendar-year basis and who elect to come under the new regulations effective March 1, 1989, the lessee would be required to submit, under the old regulations, actual cost data for the period January 1, 1988, through December 31, 1988, and for the period January 1, 1989, through February 28, 1989 (two separate submittals).

In order to avoid the requirement for two separate submittals of actual cost data, MMS hereby authorizes lessees whose approved allowances are on a calendar-year basis and who elect to come under the new regulations effective March 1, 1989, to include January and February 1989 actual cost data with the Calendar Year 1988 cost data and to submit only one allowance request covering the period January 1988 through February 1989. The allowance request covering the 14-month period would be due no later than June 1, 1989.

The MMS may establish different reporting dates for individual lessees where such changes would result in more effective administration. Lessees will be consulted if MMS wishes a different reporting date.

2. Mailing Address for Allowance Reports

Completed transportation and washing allowance reports are to be submitted to the following address:

Minerals Management Service
 Royalty Management Program/Allowances
 P.O. Box 5200
 Denver, Colorado 80217

3. Interest Charges/Losses of Previously Claimed Allowances

If MMS finds that a lessee has improperly determined a transportation or washing allowance, the lessee shall be liable for additional royalties, plus interest, or shall be entitled to a credit without interest. The lessee is liable for interest on those deductions taken in noncompliance with the regulations and on underpayments resulting from erroneous reporting. Likewise, the lessee must repay the full amount of any allowance claimed, plus interest, when such deduction is disallowed by the regulations.

Payors should be aware that MMS is planning to implement an automated system to monitor allowances reported on both the allowance reporting forms and Form MMS-4014. For example, differences between data reported on the allowance forms and Form MMS-4014, or nonsubmission of allowance reporting forms where allowances are deducted on Form MMS-4014, will dictate closer review of individual allowances. Further analysis of case details may result in partial or total disallowance of deductions already claimed or in assessment of interest, or both. Thus, it is in the best interest of the lessee to file its allowance reporting form timely and accurately.

4. Calculating Allowances

For a lessee to recoup its full expense of washing the royalty fraction of lease coal, the per-ton allowance rate must be calculated by dividing the total expense of washing all coal entering the wash plant by the number of clean tons of output exiting the wash plant. Similarly, the per-ton transportation allowance rate for transporting

lease production, including waste, to a wash plant must be calculated by dividing the total transportation expense by the tons of production transported, expressed in terms of clean coal tonnage. Complete descriptions of these calculations are contained in Enclosures 2 and 3.

5. Reporting for Transportation and Washing Allowance Adjustments

The new regulations at 30 CFR 206 (published at 54 F.R. 1522-1531, January 13, 1989) have no provisions requiring change to procedures for adjusting transportation and washing allowances claimed on Form MMS-4014. The existing adjustment procedures are still applicable. For further information on adjustments, chapter 5 of the MMS Solid Minerals Payor Handbook should be consulted. The handbook will be revised in the near future to reflect changes in allowance reporting.

6. MMS Contact Point--Allowance Issues and Reporting Forms

Questions related to allowance issues or procedures, and requests for additional copies of Forms MMS-4292 and MMS-4293, should be directed to:

Chief, Solid Minerals Valuation Branch
 Royalty Valuation and Standards Division
 Minerals Management Service
 P.O. Box 25165, Mail Stop 653
 Denver, Colorado 80225
 (303) 231-3550

B. Valuation

1. Change to Ad Valorem Lease Valuation Standards and Reporting

The new regulations at 30 CFR § 206.257 (published at 54 F.R. 1525, January 13, 1989) exclude the cost of the Federal Black Lung Excise Tax, the abandoned mine land (AML) reclamation fee, and severance taxes from gross proceeds to arrive at the value for Federal royalty purposes. These specific exclusions apply only to Federal leases and do not apply to Indian tribal or allottee leases.

The lessee/payor will be required to show the gross amount of each of these exclusions on Form MMS-4014. For each line recording sales quantity, sales value, and royalty value on Form MMS-4014, three additional lines will enumerate the exclusions from gross proceeds.

The royalty payable line and the three exclusion lines will not necessarily appear on the same royalty report; an exclusion may be taken only after the tax or fee has actually been paid, but not earlier than the royalty on the applicable tonnage is paid. For example, AML fees are paid quarterly, 30 days after the end of the quarter. The royalty on coal sold in January is reported and paid in February, but the exclusion for January AML fees (paid in April) may

not be taken until the April reporting month. The February royalty report would include royalty exclusions for January severance taxes and Black Lung Excise Tax that were paid in January or February. The April royalty report would include a royalty line for March coal sales and separate royalty exclusions for January, February, and March AML fees and for March severance taxes and Black Lung Excise Tax.

For each exclusion:

- Column 5 will show the specific exclusion.
- Column 6 will show the Accounting Identification (AID) Number.
- Column 7 will show the Product Code.
- Column 8 will show the Selling Arrangement Code.
- Column 9 will show the Sales Month and Year.
- Column 10 will show the Transaction Code. Codes 80, 81, and 82 will be used for the Black Lung Excise Tax, AML fee, and severance tax exclusions, respectively.
- Column 11 will show the Adjustment Reason Code (only if the previously reported exclusion is being revised). Note: When revising sales value and royalty value owing to a change in an exclusion, the reporting line for the exclusion causing the value and royalty changes must also be revised.
- Column 12 will be left blank.
- Column 16 will show the dollar amount by which the specific exclusion reduces the sales value of the coal product. This figure will be a negative value.
- Column 17 will show the net reduction of royalty caused by each exclusion. The dollar amount will be entered as a negative number.

Thus, while the initial royalty line shows a royalty based on gross proceeds, the net royalty due for the particular AID number, product, selling arrangement code, and sales month will show the effect of the three royalty exclusions.

2. Potential Future Change in Royalty Reporting, Form MMS-4014

In light of the revised allowance reporting requirements, which specify detailed reporting by selling arrangement, MMS is considering changing reporting on Form MMS-4014 to mirror the allowance reporting changes. (Selling arrangement, as defined at 30 CFR § 206.251 (published at 54 F.R. 1523, January 13, 1989) means the individual contractual arrangements under which sales or dispositions of coal are made to a purchaser.) By requiring a lessee to report its royalties on a selling arrangement basis, MMS will be able to conduct meaningful comparisons of Form MMS-4014 and corresponding allowance reports to confirm the accuracy of allowances reported on Form MMS-4014. If MMS decides to make such reporting changes, MMS will provide lessees with revised reporting instructions.

3. MMS Contact Point--Valuation Issues

Questions related to valuation issues or procedures, including general valuation standards, should be directed to:

Chief, Solid Minerals Valuation Branch
Royalty Valuation and Standards Division
Minerals Management Service
P.O. Box 25165, Mail Stop 653
Denver, Colorado 80225
(303) 231-3550