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July 30, 1997

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Mr. David S. Guzy
Chief, Rules & Procedures Staff
Minerals Management Service
Royalty Management Program
P.O. Box 25165, Mail Stop 3101
Denver, CO 80225-0165

Re: Notice of Proposed Changes to MMS' recently issued proposed rule regarding valuation of crude oil produced from federal leases, published July 3, 1997

Dear Mr. Guzy:

The Rocky Mountain Oil & Gas Association (RMOGA) is pleased to have the opportunity to comment on the Minerals Management Service's proposed changes to its recently issued proposed rule regarding valuation of crude oil produced from federal leases. Unfortunately, the timing of these comments and the length of the comment period were not sufficient to be able to bring a large association, such as RMOGA, together for a comprehensive review and analysis. However, in the spirit of participation, RMOGA offers the following comments on the proposed changes.

RMOGA is a regional trade association representing hundreds of members, large and small, who account for more than 90% of the oil and gas exploration, production, refining, transportation and marketing activities in the Rocky Mountain region. Following are the Association's comments on the above-referenced proposed changes.

The Minerals Management Service received a large number of comments on the initial proposed oil valuation rule in public hearings in Denver and Houston. MMS has indicated the proposed changes came from discussions at these meetings. Unfortunately, the changes proposed were only a small fraction of the suggestions made to improve a proposal that, in our view, is seriously flawed.

THE SIMPLE SOLUTION:
In all of our discussions with individual companies and the following associations: American Petroleum Institute; Domestic Petroleum Council; Independent Petroleum Association of America; Independent Petroleum Association of Mountain States; and the

Mid-Continent Oil & Gas Association, one central theme continues to bubble to the top of everyone's list .... a Royalty-In-Kind program for the federal government's share of oil production. This solution to the problem of oil valuation would give the federal government assurances that it is receiving full value for its oil by taking possession of it at or near the lease, and selling it to buyers with differing economic interests. Such a program should have a set of principles that must be adhered to in order to ensure fairness and full participation within the private sector.

A RIK Program should:

1. Reduce administrative and compliance burdens while providing the opportunity for federal and state governments to maximize their revenues.
2. Require transactions at or near the lease that fulfills the lease obligations.
3. Provide that when the government elects to take "in kind" it must take all royalty production for a certain time.
4. Require the use of private marketing expertise to streamline government operations.
5. Provide the states with the opportunity to be involved in designing and implementing the program.
6. Make production taken "in kind" broadly available for public purchase.

PROPOSED CHANGES BY MMS:

It is true that the MMS has made some minor changes to their proposed rule to value oil, but the underlying principle of substituting an index used for "hedging and speculation" continues to be the centerpiece of the proposal. The proposed changes continue the fiction that there is <u>only one price for a barrel of oil throughout the United States</u>, rather than a basket of prices that are determined by location, quality, transportation, supply and demand, plus other factors. MMS continues to believe that very little oil is actually sold at arm's-length at or near the lease. RMOGA continues to strongly disagree with this statement. Our members, both large and small, majors and independents, tell us there is an active market at the lease, and that most of these transactions are documentable and legitimate.

RMOGA believes that the purchase of crude oil is not a suspicious transaction because willing buyers and sellers with differing economic interests are involved. RMOGA also believes there are additional methods of determining market value, including the use of comparable sales reports from the same geographic area.

The issue of crude oil calls was altered in the proposed changes to the oil valuation rule. RMOGA believes the original proposal was based on an "irrational suspicion of legitimate arm's-length transactions." If an arm's-length transaction needs to be examined, MMS currently can require that sale to be examined under the benchmarks if the lessee's proceeds do not reflect the reasonable value of the production because of misconduct by or between two contracting parties. RMOGA believes the solution is already at hand without the imposition of a convoluted index-based system.

RMOGA also believes that additional regulation of crude oil subject to calls is both unnecessary and unfounded. If MMS wants to examine a particular call with an apparently low sale price, it can, under current procedures, require the lessee to show cause why this sale should not be valued under the current benchmarks.

RMOGA also believes the restrictions dealing with exchange agreements are unnecessary. We believe the option of valuing oil under arm's-length buy/sell contracts solve this problem. The lessee then may either use a price acceptable under the benchmark system, or the lessee may use the price from a subsequent arm's-length resale of the oil minus the differential, if any, between the two separate transactions.

CONCLUSION:

RMOGA believes very strongly that the MMS needs to withdraw the proposed oil valuation rule with subsequent proposed changes and put together a task force, including representatives from the affected states as well as the petroleum industry, to develop a Royalty-In-Kind program. We believe that the current system has served the United States very well. We also believe that the solutions to problems identified by MMS are already contained in the current system. We believe that MMS has more than enough data to value oil through the use of the arm's-length transaction and by using comparable sales. It is with these thoughts in mind that RMOGA urges MMS to withdraw the proposed rule and to develop an RIK program that will solve virtually all of the valuation questions by allowing both the federal government and the states to market their share of the production.

Sincerely,

Clifford F. Dodge

Clifford F. Dodge
RMOGA Executive Vice President

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