

(1) *Settlement agreement* means a settlement agreement that is between the United States and a lessee, or between an individual Indian mineral owner and a lessee and is approved by the United States, resulting from administrative or judicial litigation; and

(2) *Written agreement* means a written agreement between the lessee and the MMS Director (and approved by the tribal lessor for tribal leases) establishing a method to determine the value of production from any lease that MMS expects at least would approximate the value established under this subpart.

(c) The MMS or Indian tribes may audit, or perform other compliance reviews, and require a lessee to adjust royalty payments and reports.

[72 FR 71241, Dec. 17, 2007]

**§ 206.51 What definitions apply to this subpart?**

For purposes of this subpart:

*Affiliate* means a person who controls, is controlled by, or is under common control with another person.

(1) Ownership or common ownership of more than 50 percent of the voting securities, or instruments of ownership, or other forms of ownership, of another person constitutes control. Ownership of less than 10 percent constitutes a presumption of noncontrol that MMS may rebut.

(2) If there is ownership or common ownership of 10 through 50 percent of the voting securities or instruments of ownership, or other forms of ownership, of another person, MMS will consider the following factors in determining whether there is control in a particular case:

(i) The extent to which there are common officers or directors;

(ii) With respect to the voting securities, or instruments of ownership, or other forms of ownership:

(A) The percentage of ownership or common ownership;

(B) The relative percentage of ownership or common ownership compared to the percentage(s) of ownership by other persons;

(C) Whether a person is the greatest single owner; and

(D) Whether there is an opposing voting bloc of greater ownership;

(iii) Operation of a lease, plant, or other facility;

(iv) The extent of participation by other owners in operations and day-to-day management of a lease, plant, or other facility; and

(v) Other evidence of power to exercise control over or common control with another person.

(3) Regardless of any percentage of ownership or common ownership, relatives, either by blood or marriage, are affiliates.

*Area* means a geographic region at least as large as the defined limits of an oil and/or gas field in which oil and/or gas lease products have similar quality, economic, and legal characteristics.

*Arm's-length contract* means a contract or agreement between independent persons who are not affiliates and who have opposing economic interests regarding that contract. To be considered arm's length for any production month, a contract must satisfy this definition for that month, as well as when the contract was executed.

*Audit* means a review, conducted in accordance with generally accepted accounting and auditing standards, of royalty payment compliance activities of lessees or other interest holders who pay royalties, rents, or bonuses on Indian leases.

*BLM* means the Bureau of Land Management of the Department of the Interior.

*Condensate* means liquid hydrocarbons (generally exceeding 40 degrees of API gravity) recovered at the surface without resorting to processing. Condensate is the mixture of liquid hydrocarbons that results from condensation of petroleum hydrocarbons existing initially in a gaseous phase in an underground reservoir.

*Contract* means any oral or written agreement, including amendments or revisions thereto, between two or more persons and enforceable by law that with due consideration creates an obligation.

*Exchange agreement* means an agreement where one person agrees to deliver oil to another person at a specified location in exchange for oil deliveries at another location, and other consideration. Exchange agreements:

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(1) May or may not specify prices for the oil involved;

(2) Frequently specify dollar amounts reflecting location, quality, or other differentials;

(3) Include buy/sell agreements, which specify prices to be paid at each exchange point and may appear to be two separate sales within the same agreement, or in separate agreements; and

(4) May include, but are not limited to, exchanges of produced oil for specific types of oil (e.g., WTI); exchanges of produced oil for other oil at other locations (location trades); exchanges of produced oil for other grades of oil (grade trades); and multi-party exchanges.

*Field* means a geographic region situated over one or more subsurface oil and gas reservoirs encompassing at least the outermost boundaries of all oil and gas accumulations known to be within those reservoirs vertically projected to the land surface. Onshore fields usually are given names, and their official boundaries are often designated by oil and gas regulatory agencies in the respective states in which the fields are located.

*Gathering* means the movement of lease production to a central accumulation or treatment point on the lease, unit, or communitized area, or to a central accumulation or treatment point off the lease, unit, or communitized area as approved by BLM operations personnel.

*Gross proceeds* means the total monies and other consideration accruing for the disposition of oil produced. Gross proceeds also include, but are not limited to, the following examples:

(1) Payments for services, such as dehydration, marketing, measurement, or gathering that the lessee must perform at no cost to the lessor in order to put the production into marketable condition;

(2) The value of services to put the production into marketable condition, such as salt water disposal, that the lessee normally performs but that the buyer performs on the lessee's behalf;

(3) Reimbursements for harboring or terminaling fees;

(4) Tax reimbursements, even though the Indian royalty interest may be exempt from taxation;

(5) Payments made to reduce or buy down the purchase price of oil to be produced in later periods, by allocating those payments over the production whose price the payment reduces and including the allocated amounts as proceeds for the production as it occurs; and

(6) Monies and all other consideration to which a seller is contractually or legally entitled, but does not seek to collect through reasonable efforts.

*Indian tribe* means any Indian tribe, band, nation, pueblo, community, rancheria, colony, or other group of Indians for which any minerals or interest in minerals is held in trust by the United States or that is subject to Federal restriction against alienation.

*Individual Indian mineral owner* means any Indian for whom minerals or an interest in minerals is held in trust by the United States or who holds title subject to Federal restriction against alienation.

*Lease* means any contract, profit-share arrangement, joint venture, or other agreement issued or approved by the United States under an Indian mineral leasing law that authorizes exploration for, development or extraction of, or removal of lease products. Depending on the context, lease may also refer to the land area covered by that authorization.

*Lease products* means any leased minerals attributable to, originating from, or allocated to Indian leases.

*Lessee* means any person to whom the United States, a tribe, or individual Indian mineral owner issues a lease, and any person who has been assigned an obligation to make royalty or other payments required by the lease. Lessee includes:

(1) Any person who has an interest in a lease (including operating rights owners); and

(2) An operator, purchaser, or other person with no lease interest who makes royalty payments to MMS or the lessor on the lessee's behalf

*Lessor* means an Indian tribe or individual Indian mineral owner who has entered into a lease.

*Like-quality oil* means oil that has similar chemical and physical characteristics.

*Location differential* means an amount paid or received (whether in money or in barrels of oil) under an exchange agreement that results from differences in location between oil delivered in exchange and oil received in the exchange. A location differential may represent all or part of the difference between the price received for oil delivered and the price paid for oil received under a buy/sell exchange agreement.

*Marketable condition* means lease products that are sufficiently free from impurities and otherwise in a condition that they will be accepted by a purchaser under a sales contract typical for the field or area.

*MMS* means the Minerals Management Service of the Department of the Interior.

*Net* means to reduce the reported sales value to account for transportation instead of reporting a transportation allowance as a separate entry on Form MMS-2014.

*NYMEX price* means the average of the New York Mercantile Exchange (NYMEX) settlement prices for light sweet oil delivered at Cushing, Oklahoma, calculated as follows:

(1) Sum the prices published for each day during the calendar month of production (excluding weekends and holidays) for oil to be delivered in the nearest month of delivery for which NYMEX futures prices are published corresponding to each such day; and

(2) Divide the sum by the number of days on which those prices are published (excluding weekends and holidays).

*Oil* means a mixture of hydrocarbons that existed in the liquid phase in natural underground reservoirs and remains liquid at atmospheric pressure after passing through surface separating facilities and is marketed or used as such. Condensate recovered in lease separators or field facilities is considered to be oil.

*Operating rights owner*, also known as a working interest owner, means any person who owns operating rights in a lease subject to this subpart. A record title owner is the owner of operating rights under a lease until the operating

rights have been transferred from record title (see Bureau of Land Management regulations at 43 CFR 3100.0-5(d)).

*Person* means any individual, firm, corporation, association, partnership, consortium, or joint venture (when established as a separate entity).

*Processing* means any process designed to remove elements or compounds (hydrocarbon and nonhydrocarbon) from gas, including absorption, adsorption, or refrigeration. Field processes that normally take place on or near the lease, such as natural pressure reduction, mechanical separation, heating, cooling, dehydration, and compression, are not considered processing. The changing of pressures and/or temperatures in a reservoir is not considered processing.

*Quality differential* means an amount paid or received under an exchange agreement (whether in money or in barrels of oil) that results from differences in API gravity, sulfur content, viscosity, metals content, and other quality factors between oil delivered and oil received in the exchange. A quality differential may represent all or part of the difference between the price received for oil delivered and the price paid for oil received under a buy/sell agreement.

*Sale* means a contract between two persons where:

(1) The seller unconditionally transfers title to the oil to the buyer and does not retain any related rights such as the right to buy back similar quantities of oil from the buyer elsewhere;

(2) The buyer pays money or other consideration for the oil; and

(3) The parties' intent is for a sale of the oil to occur.

*Sales type code* means the contract type or general disposition (e.g., arm's-length or non-arm's-length) of production from the lease. The sales type code applies to the sales contract, or other disposition, and not to the arm's-length or non-arm's-length nature of a transportation allowance.

*Transportation allowance* means a deduction in determining royalty value for the reasonable, actual costs of moving oil to a point of sale or delivery off the lease, unit area, or communitized

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area. The transportation allowance does not include gathering costs.

*WTI* means West Texas Intermediate.

*You* means a lessee, operator, or other person who pays royalties under this subpart.

[72 FR 71241, Dec. 17, 2007, as amended at 73 FR 15890, Mar. 26, 2008]

### **§ 206.52 How do I calculate royalty value for oil that I or my affiliate sell(s) or exchange(s) under an arm's-length contract?**

(a) The value of oil under this section is the gross proceeds accruing to the seller under the arm's-length contract, less applicable allowances determined under §§ 206.56 and 206.57. If the arm's-length sales contract does not reflect the total consideration actually transferred either directly or indirectly from the buyer to the seller, you must value the oil sold as the total consideration accruing to the seller. Use this section to value oil that:

(1) You sell under an arm's-length sales contract; or

(2) You sell or transfer to your affiliate or another person under a non-arm's-length contract and that affiliate or person, or another affiliate of either of them, then sells the oil under an arm's-length contract.

(b) If you have multiple arm's-length contracts to sell oil produced from a lease that is valued under paragraph (a) of this section, the value of the oil is the volume-weighted average of the total consideration established under this section for all contracts for the sale of oil produced from that lease.

(c) If MMS determines that the value under paragraph (a) of this section does not reflect the reasonable value of the production due to either:

(1) Misconduct by or between the parties to the arm's-length contract; or

(2) Breach of your duty to market the oil for the mutual benefit of yourself and the lessor, MMS will establish a value based on other relevant matters.

(i) The MMS will not use this provision to simply substitute its judgment of the market value of the oil for the proceeds received by the seller under an arm's-length sales contract.

(ii) The fact that the price received by the seller under an arm's-length contract is less than other measures of

market price is insufficient to establish breach of the duty to market unless MMS finds additional evidence that the seller acted unreasonably or in bad faith in the sale of oil produced from the lease.

(d) You must base value on the highest price that the seller can receive through legally enforceable claims under the oil sales contract. If the seller fails to take proper or timely action to receive prices or benefits to which it is entitled, you must base value on that obtainable price or benefit.

(1) In some cases the seller may apply timely for a price increase or benefit allowed under the oil sales contract, but the purchaser refuses the seller's request. If this occurs, and the seller takes reasonable documented measures to force purchaser compliance, you will owe no additional royalties unless or until the seller receives monies or consideration resulting from the price increase or additional benefits. This paragraph (d)(1) does not permit you to avoid your royalty payment obligation if a purchaser fails to pay, pays only in part, or pays late.

(2) Any contract revisions or amendments that reduce prices or benefits to which the seller is entitled must be in writing and signed by all parties to the arm's-length contract.

(e) If you or your affiliate enter(s) into an arm's-length exchange agreement, or multiple sequential arm's-length exchange agreements, then you must value your oil under this paragraph.

(1) If you or your affiliate exchange(s) oil at arm's length for WTI or equivalent oil at Cushing, Oklahoma, you must value the oil using the NYMEX price, adjusted for applicable location and quality differentials under paragraph (e)(3) of this section and any transportation costs under paragraph (e)(4) of this section and §§ 206.56 and 206.57.

(2) If you do not exchange oil for WTI or equivalent oil at Cushing, but exchange it at arm's length for oil at another location and following the arm's-length exchange(s) you or your affiliate sell(s) the oil received in the exchange(s) under an arm's-length contract, then you must use the gross proceeds under your or your affiliate's