Minerals Management Service, Interior

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 arm’s-length sales contract after the exchange(s) occur(s), 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.

(3) You must adjust your gross proceeds for any location or quality differential, or other adjustments, you received or paid under the arm’s-length exchange agreement(s). If MMS determines that any exchange agreement does not reflect reasonable location or quality differentials, MMS may adjust the differentials you used based on relevant information. You may not otherwise use the price or differential specified in an arm’s-length exchange agreement to value your production.

(4) If you value oil under this paragraph, MMS will allow a deduction, under §§206.56 and 206.57, for the reasonable, actual costs to transport the oil:

(i) From the lease to a point where oil is given in exchange; and

(ii) If oil is not exchanged to Cushing, Oklahoma, from the point where oil is received in exchange to the point where the oil received in exchange is sold.

(5) If you or your affiliate exchange(s) your oil at arm’s length, and neither paragraph (e)(1) nor (e)(2) of this section applies, MMS will establish a value for the oil based on relevant matters. After MMS establishes the value, you must report and pay royalties and any late payment interest owed based on that value.

(f) You may not deduct any costs of gathering as part of a transportation deduction or allowance.

(g) You must also comply with §206.54.

§206.53 How do I determine value for oil that I or my affiliate does not sell under an arm’s-length contract?

(a) The unit value of your oil not sold under an arm’s-length contract is the volume-weighted average of the gross proceeds paid or received by you or your affiliate, including your refining affiliate, for purchases or sales under arm’s-length contracts.

(1) When calculating that unit value, use only purchases or sales of other like-quality oil produced from the field (or the same area if you do not have sufficient arm’s-length purchases or sales of oil produced from the field) during the production month.

(2) You may adjust the gross proceeds determined under paragraph (a) of this section for transportation costs under paragraph (c) of this section and §§206.56 and 206.57 before including those proceeds in the volume-weighted average calculation.

(3) If you have purchases away from the field(s) and cannot calculate a price in the field because you cannot determine the seller’s cost of transportation that would be allowed under paragraph (c) of this section and §§206.56 and 206.57, you must not include those purchases in your weighted-average calculation.

(b) Before calculating the volume-weighted average, you must normalize the quality of the oil in your or your affiliate’s arm’s-length purchases or sales to the same gravity as that of the oil produced from the lease. Use applicable gravity adjustment tables for the field (or the same general area for like-quality oil if you do not have gravity adjustment tables for the specific field) to normalize for gravity.

Example to paragraph (b): 1. Assume that a lessee, who owns a refinery and refines the oil produced from the lease at that refinery, purchases like-quality oil from other producers in the same field at arm’s length for use as feedstock in its refinery. Further assume that the oil produced from the lease...
that is being valued under this section is Wyoming general sour with an API gravity of 23.5°. Assume that the refinery purchases at arm’s length oil (all of which must be Wyoming general sour) in the following volumes of the API gravities stated at the prices and locations indicated:

<table>
<thead>
<tr>
<th>Volume (bbl)</th>
<th>API Gravity</th>
<th>Price per bbl</th>
<th>Location</th>
</tr>
</thead>
<tbody>
<tr>
<td>10,000</td>
<td>24.5°</td>
<td>$34.70</td>
<td>Purchased in the field.</td>
</tr>
<tr>
<td>8,000</td>
<td>24.0°</td>
<td>$34.00</td>
<td>Purchased at the refinery after the third-party producer transported it to the refinery, and the lessee does not know the transportation costs.</td>
</tr>
<tr>
<td>9,000</td>
<td>23.0°</td>
<td>$33.25</td>
<td>Purchased in the field.</td>
</tr>
<tr>
<td>4,000</td>
<td>22.0°</td>
<td>$33.00</td>
<td>Purchased in the field.</td>
</tr>
</tbody>
</table>

2. Because the lessee does not know the costs that the seller of the 8,000 bbl incurred to transport that volume to the refinery, that volume will not be included in the volume-weighted average price calculation. Further assume that the gravity adjustment scale provides for a deduction of $0.02 per 1/10 degree API gravity below 34°. Normalized to 23.5° (the gravity of the oil being valued under this section), the prices of each of the volumes that the refiner purchased that are included in the volume-weighted average calculation are as follows:

<table>
<thead>
<tr>
<th>Volume (bbl)</th>
<th>API Gravity</th>
<th>Normalized Price per bbl</th>
<th>Additional Deduction</th>
</tr>
</thead>
<tbody>
<tr>
<td>10,000</td>
<td>24.5°</td>
<td>$34.50</td>
<td>($0.20 deducted)</td>
</tr>
<tr>
<td>9,000</td>
<td>23.0°</td>
<td>$33.35</td>
<td>($0.10 added)</td>
</tr>
<tr>
<td>4,000</td>
<td>22.0°</td>
<td>$33.30</td>
<td>($0.30 added)</td>
</tr>
</tbody>
</table>

3. The volume-weighted average price is \((10,000 \times 34.50/100) + (9,000 \times 33.35/100) + (4,000 \times 33.30/100) / 23,000 = 33.84/100\). That price will be the value of the oil produced from the lease and refined prior to an arm’s-length sale, under this section.

(c) If you value oil under this section, MMS will allow a deduction, under §206.56 and 206.57, for the reasonable, actual costs:
(1) That you incur to transport oil that you or your affiliate sell(s), which is included in the weighted-average price calculation, from the lease to the point where the oil is sold; and
(2) That the seller incurs to transport oil that you or your affiliate purchase(s), which is included in the weighted-average cost calculation, from the property where it is produced to the point where you or your affiliate purchase(s) it. You may not deduct any costs of gathering as part of a transportation deduction or allowance.

(e) You must also comply with §206.54.

§206.54 How do I fulfill the lease provision regarding valuing production on the basis of the major portion of like-quality oil?

(a) For any Indian leases that provide that the Secretary may consider the highest price paid or offered for a major portion of production (major portion) in determining value for royalty purposes, if data are available to compute a major portion, MMS will, where practicable, compare the value determined in accordance with this section with the major portion. The value to be used in determining the value of production, for royalty purposes, will be the higher of those two values.

(b) For purposes of this paragraph, major portion means the highest price paid or offered at the time of production for the major portion of oil production from the same field. The major portion will be calculated using like-quality oil sold under arm’s-length contracts from the same field (or, if