OVERSIGHT HEARING
BEFORE THE
SUBCOMMITTEE ON
ENERGY AND MINERAL RESOURCES
OF THE
COMMITTEE ON
NATURAL RESOURCES
HOUSE OF REPRESENTATIVES
ONE HUNDRED THIRD CONGRESS
FIRST SESSION
ON
THE NET RECEIPTS SHARING PROGRAM
HEARING HELD IN WASHINGTON, DC
JULY 29, 1993
Serial No. 103-40
Printed for the use of the Committee on Natural Resources
### COMMITTEE ON NATURAL RESOURCES

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<table>
<thead>
<tr>
<th>State</th>
<th>Member</th>
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<tbody>
<tr>
<td>Indiana</td>
<td>Philip R. Sharp</td>
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<td>South Dakota</td>
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<td>James V. Hansen</td>
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<td>Barbara F. Vucanovich</td>
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<td>Elton Gallegly</td>
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<td>Oregon</td>
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<td>Wyoming</td>
<td>Craig Thomas</td>
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<td>Tennessee</td>
<td>John J. Duncan, Jr.</td>
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<td>Colorado</td>
<td>Joel Hefley</td>
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<td>John T. Doolittle</td>
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<tr>
<th>State</th>
<th>Member</th>
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<table>
<thead>
<tr>
<th>CONTENTS</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hearing held: July 29, 1993</td>
<td>1</td>
</tr>
<tr>
<td>Member statements:</td>
<td></td>
</tr>
<tr>
<td>Hon. Richard H. Lehman</td>
<td>1</td>
</tr>
<tr>
<td>Hon. Craig Thomas</td>
<td>2</td>
</tr>
<tr>
<td>Witness statements:</td>
<td></td>
</tr>
<tr>
<td>Panel consisting of:</td>
<td></td>
</tr>
<tr>
<td>Tom Fry, Director, Minerals Management Service, Department of the Interior, accompanied by James Shaw, Associate Director, Collection Program, Denver, Colorado, and Roger Hildebeidel, Bureau of Land Management</td>
<td>13</td>
</tr>
<tr>
<td>Roger Dewey, Director, Department of Audit, State of Wyoming, accompanied by Earl Kabeiseman, Director, Department of Revenue, State of Wyoming</td>
<td>29</td>
</tr>
<tr>
<td>Additional material submitted for the record from:</td>
<td></td>
</tr>
<tr>
<td>Hon. Craig Thomas:</td>
<td></td>
</tr>
<tr>
<td>1. Prepared statement of Hon. Barbara F. Vucanovich</td>
<td>4</td>
</tr>
<tr>
<td>Roger Dewey, Wyoming Department of Audit:</td>
<td></td>
</tr>
<tr>
<td>1. Prepared statement of Hon. Mike Sullivan, Governor, State of Wyoming</td>
<td>32</td>
</tr>
<tr>
<td>2. “Proposal to Implement Federal Royalty Collections Program for the State of Wyoming”</td>
<td>50</td>
</tr>
</tbody>
</table>
THE NET RECEIPTS SHARING PROGRAM

THURSDAY, JULY 29, 1993

HOUSE OF REPRESENTATIVES,
COMMITTEE ON NATURAL RESOURCES,
SUBCOMMITTEE ON ENERGY AND MINERAL RESOURCES,
Washington, DC.

The subcommittee met at 1:35 p.m. in Room 1310A of the Longworth House Office Building, the Honorable Richard Lehman (chairman of the subcommittee) presiding.

STATEMENT OF HON. RICHARD LEHMAN

Mr. LEHMAN [presiding]. The hearing will come to order. The subcommittee is meeting today to conduct an oversight hearing on the collection of federal mineral receipts by the Minerals Management Service.

This hearing was scheduled in response to concerns raised by our colleague, Congressman Craig Thomas, during Committee debate on the Omnibus Budget Reconciliation provision regarding mineral receipts.

The Mineral Leasing Act of 1920 originally provided that States would receive 37.5 percent of revenues generated from the leasing of petroleum and other significant minerals removed from the 1872 Mining Law and placed under the 1920 Act.

In 1982, Congress amended the 1920 Act with the Federal Oil and Gas Reform Act which, among other things, increased the State share to 50 percent of the gross receipts.

Beginning in 1984, the Administration has sought, from Congress, the means to recover all or part of its administrative costs from the gross receipts collected under the Mineral Leasing Act.

Since Fiscal Year 1991, Congress has included "net receipts sharing" language in the Department of the Interior's appropriation bills to recover approximately half the Federal administrative costs of onshore mineral leasing.

The provision accomplishes cost recovery by reducing the gross receipts prior to disbursing the States' shares.

The Budget Reconciliation bill would make permanent the recovery of 50 percent of federal administrative costs associated with the onshore mineral leasing program. In that way states would be paying approximately 25 percent of the 50 percent which would be deducted from the gross receipts.

This provision, although an understandable option from the budgetary standpoint, has not, also understandably, been popular with the States. In particular, Wyoming, which generates 40 per-
2

cent of onshore mineral leasing receipts, has been vocal in fighting this approach.

The purpose of this hearing, however, is not to question the approach embodied in the Reconciliation package. Instead, we need to look at the manner in which administrative costs are spent, the cost-effectiveness of administrative expenditures, and the actual amount spent on collections of on-shore revenues distributed to States, counties, and tribes.

I would note that the Western Governors' Association has recently passed a resolution asking the Congress to initiate a GAO study into the manner in which MMS and BLM calculate and spend their administrative costs. They believe they can do the job more efficiently and more cost-effectively.

The Administration has thus far maintained that certain functions, such as the royalty collection and disbursement, cannot be delegated to the states.

The witnesses this afternoon are Mr. Tom Fry, the newly appointed Director of MMS.

It's good to have you here today.

And Mr. Roger Dewey, Director of the Wyoming Division of Audit.

Gentlemen, I welcome you to the Committee, and I certainly look forward to your testimony.

At this time, I'd like to recognize the gentleman from Wyoming for his statement, Mr. Thomas.

STATEMENT OF HON. CRAIG THOMAS

Mr. THOMAS. Thank you very much, Mr. Chairman.

First let me thank you for holding this meeting. I appreciate that very much.

This topic is obviously of great importance to me and to those of us from Wyoming, and we've followed it very closely over the years, not only in Wyoming, of course, but in other Western States as well.

I particularly want to welcome Mr. Roger Dewey, who's the Director of Wyoming's Department of Audit, and Mr. Earl Kabeiseman, both of whom are old friends. Earl is the Director of Wyoming's Department of Revenue.

Let me just say that there are a number of things, of course, that a person can debate and discuss in this issue, but I think there are two that are outstanding.

One is the question of fairness, fairness from where we've been in terms of the royalty collection. The other, of course, is efficiency.

In the area of fairness, clearly the division of royalties based on 50 percent of the gross receipts was the agreement; that was the deal. And that's what we've been doing.

And then of course I understand, particularly in the area of the Appropriations Committee, there becomes this frenzy for money.

And so instead of looking at how we might do it more efficiently, the tendency is to say where can we get some more by changing the formula.

I think that's not fair.
Also, I think involved in the fairness issue, to go back further in history, is the question of ownership. Wyoming is 50-percent owned by the Federal Government.

Other States, including Nevada, are as much as 85-percent owned.

So, you know, in the original thirteen states, the other states, these lands were put up for disposal in various means and they became private. They are the source of funding.

So I think you could make a strong argument that, as a tradeoff for the notion of the Feds retaining that kind of ownership in the State, the State is indeed entitled to some consideration in terms of those royalties.

So it seems to me that those constitute the fairness argument.

The other one of course is efficiency. Regardless of the beneficiaries, the question of collecting these taxes as efficiently and quickly and simply in the least costly manner is what we're really seeking to do, and should do in all of government certainly.

I understand that the States' collection and the responsibilities of the Federal Government sometimes differ, and you have to understand that in comparing the costs.

But the fact is that the cost of collection in Wyoming has been substantially less. As a matter of fact, we've talked about this some before, and the cost for the collection by Minerals Management is nearly $60 per $1,000, as I understand it, and Wyoming collects theirs for about $5 per $1,000—substantially, substantially less money.

The other of course is that we're talking about the very same production. We're not talking about something else. We're talking about the same barrel of oil that is already handled for taxes. It's almost as if you had a sales tax shared by the State and the municipality, and each of them collects it separately.

Well, that isn't the way it's done. You collect it and then you disburse it, and that's the efficient way to do it.

I've visited with Mr. Fry, and I'm pleased with his openness and willingness to talk about this.

The Assistant Secretary has also indicated some interest in a fairness effort there.

So I won't go into great details about it. I'm anxious to hear the testimony from both of you.

Mr. Chairman, if I might submit Mrs. Vucanovich's statement for the record, please, sir.

Mr. LEHMANN. Certainly, without objection.

[Prepared statement of Mrs. Vucanovich follows:]
Mr. Chairman, thank you for calling this oversight hearing on an issue of importance to many western states that have shared mineral leasing royalty monies with the federal government for many years. Of course, until very recently those receipts were split with the states in which the leases are producing the funds on a 50-50 basis without reduction for administrative costs. I have not agreed with the appropriators decisions for the last three fiscal years to factor in a portion of those costs before distributing the "net receipts." The Mineral Leasing Act does not contemplate such a reduction but the Rules Committee protected the appropriations bills from challenge, and the rest is history.

Now, to be certain, Nevada is not a heavy hitter under the Mineral Leasing Act, like my colleague's state of Wyoming for example. My state has some oil production in Railroad Valley which comes from federal leases, but we lack coal resources, sodium or potash deposits, phosphate, and oil shale so very little revenue is returned to Nevada under gross receipts or net receipts sharing. However, Mr. Chairman, I think we all see the day coming when minerals locatable under the Mining Law of 1872 become royalty-bearing, and then Nevada will become the Wyoming of gold. The administrative costs issue will be important in the debate on receipts distribution for public lands hardrock mines.

But beyond the parochial issue of fighting for revenue for our states, Mr. Chairman, is the basic question of fairness. In my view, if the feds tell the states they must contribute to the burden of administering the mineral leasing laws, then we ought to at least examine the ability of the states to opt to do some of the functions themselves. At least some states could likely achieve this at a cost savings to the federal Treasury, and thereby benefit taxpayers not just in Wyoming, but in Nevada, California, West Virginia and everywhere. I believe this idea deserves a serious investigation, perhaps in a pilot study ordered by Congress.

With that, Mr. Chairman, let me finish by welcoming today's witnesses, the newly appointed Director of the Minerals Management Service, Mr. Tom Fry, and Mr. Roger Dewey of the State of Wyoming.
Mr. THOMAS. And if I may submit my own statement for the record, and thank you again for holding this hearing.

[Prepared statement of Mr. Thomas follows:]
Thank you Mr. Chairman for holding this hearing today. This is a topic which is of great importance to the State of Wyoming and something I have closely followed over the last few years. I would also like to welcome Mr. Roger Dewey who is the Director of the Wyoming Department of Audit and Mr. Earl Kabeiseman who is the Director of Wyoming's Department of Revenue.

Collection of mineral royalties on federal lands is vital to the economy of Wyoming. As you know, 50 percent of my state is owned by the federal government. This has some serious consequences for Wyoming's residents and requires the state and the federal government to work closely together on numerous issues. Resources collected from the mineral royalty program are used to support various programs including education, road construction and payments to towns and counties.

For a number of years, I have been interested in the way the Minerals Management Service collects royalties on federal lands. Wyoming is by far the largest producer of royalties and has an important stake in ensuring that these funds are collected in an efficient manner. Unfortunately, this is not the case.
Currently, it costs the Minerals Management Service nearly $60 per thousand dollars collected to administer the net receipts program. This is extremely high. Wyoming administers a similar program at the state level for roughly five dollars per thousand dollars collected. Although there are some differences between these two programs, it seems incomprehensible that the discrepancy should be this large.

Recently, some members of the Administration and House Natural Resources Committee Chairman George Miller have indicated that changes may be necessary in the net receipt program. I strongly agree and am pleased that progress is being made in our efforts to correct these problems.

There are a number of proposals currently being considered regarding changes to the net receipt program. One of the most promising ideas is a plan which would allow the states to collect the royalties instead of MMS. The State of Wyoming has authorized a study of the collection process and the results seem promising. I support these efforts and believe state collection of these receipts is the most practical solution to this entire situation.

Mr. Chairman, clearly the current net receipts program is not working. It is inefficient and costs enormous amounts of money. I believe it is important for this Subcommittee and the Committee on Natural Resources to pursue this issue and find a solution
which will benefit the citizens of Wyoming and all of the people who live in the public lands states. Thank you again, Mr. Chairman, I look forward to hearing the testimony of our witnesses.
Mr. LEHMAN. Thank you very much.
Mr. THOMAS. I forgot. May I also put in, and you already men­tioned that, the Western Governors' statement with respect to this.
[Policy statement of the Western Governors' Association, Resolu­tion 93–019, follows:]
Western Governors' Association
Resolution 93-019
June 22, 1993
Tucson, Arizona

SPONSOR: Governor Sullivan
SUBJECT: Administrative and Operating Costs Under Federal-State Shared Receipt Programs

A. BACKGROUND

1. State and local government shares of federal mineral, timber, grazing, recreation and other public land resource related receipts were designed to compensate public land states for the continued federal ownership of land and mineral resources and the concurrent tax base diminishment and development restraints created by that ownership.

2. State shared receipt programs were basic to the congressional compromise which led to the retention of significant federal land and mineral interests in the western states.

3. State and county shared receipts are an important revenue source for impact assistance, such as education, roads and highways, sewer and water and other public facilities and programs needed to support the industries and work forces engaged in development activities on federal lands.

4. Western state and local governments expend significant amounts of their own-source revenues for the planning, accommodation and regulation of federal land and mineral resource development and management activities.

5. Congressional authorizations for state and local shares of federal receipts have historically and consistently been interpreted to mean gross receipts and not net receipts, nor receipts less administrative costs.

6. Each year since 1991, Congress has inserted language into its Interior Appropriations bill that deducts 25 percent of the Interior and Agriculture Departments' cost of administering their mineral and geothermal steam leasing programs from the states' share of the mineral receipts.

7. The Concurrent Budget Resolution for Fiscal Year 1994 directs the House and Senate Natural Resource Committee to make the deduction permanent by amending the Mineral Leasing Act of 1920 and all other statutes which share federal revenues derived from royalties and leasing of on-shore minerals and geothermal steam. The Fiscal Year 1994 Reconciliation bill directs the Minerals Management Service to deduct each year 25 percent of the
B. GOVERNORS' POLICY STATEMENT

1. We oppose any proposal to deduct administrative and operating costs from gross receipts for federal minerals, national forests and other congressionally-authorized state and county shared receipts.

2. We support efforts to assure full collection and proper accounting of federal mineral and other resource related receipts in order to improve returns to the federal government as well as affected states and counties.

3. We support efforts to reduce unreasonable and unnecessary administrative burdens and costs and to make more productive, efficient and accountable federal mineral, timber and other resource related programs.

4. We support efforts of the federal government to contain its "administrative costs" by streamlining its expensive and often cumbersome auditing and accounting procedures and to delegate those functions to the states, as appropriate.

5. Congress should limit any administrative costs that are deducted from the federal receipts to those costs directly related to audit and collection functions. Congress should place these limits in the Reconciliation bill or the bill's report. While those deductions should relate to the amount of receipts
each state received, the deduction should be no more than the actual cost incurred in executing audit and collection functions within each state.

6. We support a larger role for the states in determining how to administer the leasing and collection programs. If those policy functions that relate to what lands should be leased and their supervision are included in deductible administrative cost, states should have a corresponding role in those decisions.

7. We support full funding for state audits of federal mineral leases, including those for oil, gas, coal, geothermal, potash and sodium.

C. GOVERNORS' MANAGEMENT DIRECTIVE

1. A copy of this resolution shall be transmitted to the President, the Director of the Office of Management and Budget, the Secretaries of Interior and Agriculture, the chairman and ranking minority members of both the authorizing and appropriations committees and members of the western congressional delegations.

2. The WGA staff shall continue to monitor and report to the governors on any legislative or budget proposals which could adversely affect current federal-state shared receipt program formulas.

3. The WGA staff shall continue to survey the affected states to determine how mineral and national forest revenues are spent, listing specific projects where such information is available.

4. A request shall be made to key members of the congressional delegations to obtain a report from the General Accounting Office, or some other independent entity, on: (1) how administrative costs for mineral revenues are spent; (2) the cost effectiveness of administrative expenditures; and (3) the actual amount spent on collecting onshore revenues distributed to the states, counties and tribes.

5. The WGA staff shall work with the states to ensure a pilot project is ready for implementation if states are authorized to assume the collection and auditing functions of the shared receipt programs.
Mr. LEHMAN. Certainly we'll put those in the record without objection.

And I would be pleased to recognize Mr. Fry for his statement, and anything you have to include in the record will be done without objection.

You may proceed.

PANEL CONSISTING OF TOM FRY, DIRECTOR, MINERALS MANAGEMENT SERVICE, DEPARTMENT OF THE INTERIOR, ACCOMPANYED BY JAMES SHAW, ASSOCIATE DIRECTOR, COLLECTION PROGRAM, DENVER, CO, AND ROGER HILDEBEIDEL, BUREAU OF LAND MANAGEMENT; AND ROGER DEWEY, DIRECTOR, DEPARTMENT OF AUDIT, STATE OF WYOMING, ACCOMPANYED BY EARL KABEISEMAN, DIRECTOR, DEPARTMENT OF REVENUE, STATE OF WYOMING

STATEMENT OF TOM FRY

Mr. Fry. Thank you very much, Mr. Chairman.

I'd like to introduce Mr. Jim Shaw, who is sitting here with me at the table. He's our Associate Director for our Royalty Collection Program, stationed in Denver, and he's come in to try to help us answer any of the technical questions that may come up today that are way over my head. So I appreciate Mr. Shaw being here today.

We have submitted written testimony, and we do appreciate the fact that you will put that in the record for us.

Maybe I should give you a bit of history on how this program got started.

It's my understanding that in 1991 the appropriation was begun to create this net receipts sharing. The total costs on which it is based are really divided among three agencies of the Federal Government: the MMS, the BLM, and the Forest Service. Last year, this totalled about $140 million worth of costs.

About 39 percent of that was attributable to the MMS; about 51 percent were costs generated by the BLM; approximately 11 percent were costs generated by the Forest Service.

Obviously, each of these areas are different. The BLM and the Forest Service are in the leasing business. They do work where they test wells and test for production, so that's the kind of work they're in.

From the MMS standpoint, we're talking about the collection effort itself. Collection, verification and distribution of revenues that are received from Federal and tribal lands.

The system, as it was created and as it works today, is based on pro rata distribution of revenues.

The MMS has looked at other ways that that might be handled. Mr. Thomas mentioned the fact that other ways have been looked at.

Every time we look at a different way of handling this, some State is probably going to be able to object that it doesn't appear to be fair.

We would be the first to agree that it's certainly the case in Wyoming. While the formula is a fair formula, Wyoming probably pays a heavier burden than any other State, not just in terms of dollars
but also in the amount that the State of Wyoming has to pay based on the effort that we use to collect those dollars.

So we would encourage looking at any formula that might be fairer to the State of Wyoming because we recognize the situation the State is in.

Some have suggested, as Mr. Thomas has, that our costs may be too high. I welcome that discussion. I have no preconceived notions as to whether or not the MMS is charging or spending too much money in order to administer this program.

We're more than willing to listen to anyone who has a suggestion as to how we can better accomplish our job of collecting data.

It's also been suggested that the MMS has been unwilling to share data. I can represent to the Chairman of this Committee that during my stewardship of MMS, there will never be a question of sharing data. We view ourselves as partners with the States and the Indian tribes, and whatever data we have about our collection and distribution process will be made available to any of those partners we have.

There are certain Federal functions that I think we should be reminded of that the MMS is specifically involved in, which I don't think are matters that States desire to become involved in, or probably are prohibited from being involved in.

Those are the collection and obligation of Federal funds, conducting of administrative hearings and appeals, issuing regulations, reports to Congress and the President, and also the enforcement effort.

Those, at least from studies that have been done to date, are matters that are within the exclusive province of the Federal Government, and they're probably not matters the States would be involved in.

I would point out, from our survey of the dollars that are involved here, about 22 percent—I'm not sure exactly, but in that neighborhood—of the dollars that go towards this collection effort come from those categories.

So the 22 percent are things that the Federal Government will continue to have to do, even if the States become involved in this program.

There's also been discussion of pilot projects and the States becoming involved in the collection effort.

We would welcome the opportunity to look at any pilot project. Our only concern would be, and I think the concern of everyone would be, that the taxpayer pays less dollars to have this job done.

Any program that anybody can come up with which makes sense and saves the taxpayers dollars, we would like to look at and would endorse.

We've encouraged in the past, I understand, the States to make presentations like that. I understand the State of Wyoming may have a presentation they would like to make.

We look forward to looking at that and working with them on their proposal.

Lastly, I would just like to say that this whole issue of charging States to collect their dollars is not one that the Department of the Interior is particularly—I started to use the word "concerned"—our interest is not in keeping these dollars for the Department of the
Interior. We would like someday for this to be a function that, if the Federal Government is going to do, then the Federal Government does not charge the States for it.

However, we view this as a budget question, not as a policy question for the Department of the Interior. And whatever plan Congress comes up with for distribution of funds and charging of fees for collection of these dollars, we would be happy to administer and we would endorse.

We look forward to working with this subcommittee, the States, and all our other constituents in trying to resolve these very difficult matters, and hope that this hearing will provide us with the opportunity to further open the dialogue between ourselves and our other constituents.

Thank you very much, Mr. Chairman. We look forward to taking any of your questions.

[Prepared statement of Mr. Fry follows:]
I would like to thank the Chairman and Members of the Subcommittee for the opportunity to testify today. My testimony will focus on the many issues surrounding net receipts sharing and more specifically, on mineral leasing program costs and how the Department allocates those costs to States.

As you know, net receipts sharing is the method through which States share in the cost of administering the onshore Federal mineral leasing program. A portion of Bureau of Land Management (BLM), Minerals Management Service (MMS), and U.S. Forest Service (USFS) costs to administer the mineral leasing program is deducted from the leasing revenues before they are shared with States. MMS assembles the cost data from all three bureaus, allocates shares to States, and makes the deductions from the revenues disbursed monthly to States.

Since FY 1991, a net receipts sharing provision has been included annually in the Department of the Interior Appropriations Act. It has been proposed in the President's FY 1994 Budget and included in the budget reconciliation legislation passed by the House and Senate. The Administration proposal displays total mineral leasing program costs of about $140 million. Approximately $54 million of that amount (about 39 percent) is attributable to MMS. BLM costs total $71 million (about 51 percent), and USFS costs are approximately $16 million (about 11 percent). Attached to my statement are discussions regarding how BLM, MMS and USFS calculate their costs.

We understand States are concerned about reductions from their revenues. They have expressed concerns about program costs and the methods used to allocate those costs to States. Some have suggested they could perform the functions cheaper and more efficiently themselves.

In 1992, at the request of the Senate Appropriations Committee, MMS was the lead agency in the conduct of a study that analyzed which royalty-related functions might be performed by States more efficiently and at lower cost. The study concluded that only a few functions are reserved to the Executive Branch of the Federal Government, most notably, allocating and obligating Federal funds, conducting administrative hearings and appeals, issuing final regulations and
policies, authorizing reports to Congress and the President, and taking enforcement actions. Most other functions could be delegated if additional statutory authority were available. (The delegation authority found in the Federal Oil and Gas Royalty Management Act (FOGRMA) of 1982 is limited to inspections, audits and investigations.) However, the report concluded that the functions most amenable to partition and delegation to States were MMS' royalty audit work and BLM's production verification functions (inspections).

When the report was released, States were invited to submit cost proposals for the Federal functions they wished to assume, but to date none has been received by MMS.

Significant additional Federal costs could be incurred if functions which are not as readily separable as audit or inspections are delegated. Some States have felt that their lower overhead, familiarity with leases within their own borders, and experience collecting other revenues on Federal, State and private land leases would give them a cost advantage in carrying out most mineral revenue functions. However, if States duplicate portions of MMS accounting systems and functions, while MMS continues to perform non-delegable functions as well as all revenue management services for Indian and offshore leases and onshore leases in States which do not desire to assume Federal functions, the total cost of the mineral leasing program will likely increase rather than decrease.

In addition, State mineral lease accounting systems and practices may not be compatible with requirements for accounting for Federal funds. Bringing State systems into compliance with statutorily-mandated Federal standards may raise costs as well.

To take the responsibilities required to manage Federal mineral revenues, we assume a State must be able to fulfill the same statutory and regulatory standards and obligations as the Federal government. Some States simply do not receive enough revenues from Federal leasing to make the effort worthwhile; in tight budgetary times, other States may not choose to dedicate the resources required.

MMS supports the delegation of functions to States when it can be done in an efficient and cost-effective manner. For example, we are very pleased with the results of the delegated audit program, which began almost 10 years ago with an agreement with the State of Wyoming. Nine States (Wyoming, California, Utah, Colorado, Montana, Oklahoma, North Dakota, Louisiana, and Texas) and four Indian Tribes (Navajo, Southern Ute, Ute, and Ute Mountain Ute) are participating, with New Mexico soon to be added. We have developed a very beneficial working relationship, and have steadily increased the funding for the program to the current level of $5.1 million ($4.1 million of this total is for State cooperative audits). Our
policy is to treat the State and Indian auditors as full partners in the audit process, and it is working very successfully.

In addition, the Bureau of Land Management has cooperative agreements with four Tribes (Navajo, Jicarilla Apache, Southern Ute, and Ute Mountain Ute) to perform field inspections of oil and gas leases. To date no State has asked for a delegation to perform field inspections.

Some States have questioned why the Government spends as much as it does for mineral lease management. Although I cannot speak for USFS, I know that MMS and BLM believe they are responding to Congressional directives to manage Federal mineral revenues aggressively and to carry out its wishes with respect to FOGRMA inspection and enforcement activities. MMS performs several compliance functions which we understand most States do not perform for State leases; they include automated verification of reported data, intensive database maintenance, identification and resolution of reporting errors, and debt collection followup and enforcement.

In addition to the specific requirements of FOGRMA, this Committee, in its periodic reviews of our Royalty Management operations, has called for increased effort by MMS in several areas, such as:

- Intensive monitoring of transportation and processing allowances to detect those that do not qualify under MMS regulations.
- Additional enhancements to computer routines which identify out-of-compliance conditions (exception processing), and resources to assure that newly identified exceptions will be resolved.
- Verification of production reports by collecting and comparing data on monthly purchaser summary statements.
- Assessments against companies for all erroneous reports.

We have to assume such recommendations mean this Committee wants us to do more, rather than less. Our customers within State and tribal governments, and among other Federal agencies, also express continued interest in increased information and more assurance that royalties are fully collected. We would assume that, if State delegation occurred, this Committee would expect States to manage those programs with an equally aggressive effort—an effort that would likely result in comparable budgetary outlays.

In considering the advantages and disadvantages of delegating functions to States, we are also sensitive to the intention expressed in FOGRMA that royalties be
collected in a manner that does not create an unreasonable burden on lessees, and that a "uniform and effective royalty management system prevail" for Federal leases in all States. Several industry groups commented to the Mineral Royalty Transfer Study team that they objected to transfer of additional functions to States, believing that it would be inefficient for all parties.

This concludes my prepared testimony. I would be happy to answer any questions the Members of the Subcommittee might have.
MMS COSTS

The Minerals Management Service costs that are used to calculate the net receipts sharing cost base include that portion of its Royalty Management Program (RMP) and General Administration budgets associated with Federal onshore lease activities.

Most royalty accounting functions are performed for all Federal and Indian leases in MMS' national accounting center, using systems and processes that serve all types of leases nationwide. Consequently, MMS has needed to identify workload indicators to allocate its appropriated budget among onshore Federal, offshore Federal, and Indian leases. In contrast, BLM and USFS can attribute a large portion of their onshore mineral leasing budgets to operations in regional, State and local field offices. In other words, they can point to a direct link to costs in specific States. For MMS, that link is not so readily identifiable.

The workload indicator that the Royalty Management Program uses in its current approach is producing leases. This is because the program's revenue collection functions are concentrated on producing leases. Costs are allocated for Federal onshore leases based on the number of onshore producing leases compared to the total of all producing leases (onshore, offshore, Indian). Since onshore producing leases comprise about 77% of the total, the amount of RMP's budget allocated to Federal onshore activities is about 77% of the total budget.

The General Administration appropriated budget is used to calculate overhead for the onshore mineral leasing program. General Administration pays the rent, telephone, and utility bills for the bureau. It provides such things as personnel and procurement support, and policy and executive management and oversight for all of MMS. For net receipts sharing purposes, its appropriated budget is reduced to reflect only the support provided to that portion of RMP resources associated with Federal onshore activities. First an adjustment is made to separate resources supporting RMP from those supporting the OCS Program based on the number of RMP staff to the total of OCS and RMP staff. This net amount is adjusted to differentiate only RMP onshore activities using the 77% ratio of Federal onshore producing leases to the total of all producing leases.

Finally, the cost base subject to net receipts sharing is reduced by costs from four specific activities: royalty-in-kind program and late/erroneous reporting assessments (energy and minerals companies already reimburse the Federal Treasury for costs associated with these activities); late disbursement interest (compensation to States for loss of the time value of disbursements); and cooperative audit agreement funding for States.
The following table details the derivation of MMS’ budget for Federal onshore activities:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Royalty Management Program</td>
<td>66,544</td>
</tr>
<tr>
<td>-3,306 FY 1991 &amp; 92 Indian Initiatives</td>
<td></td>
</tr>
<tr>
<td>63,238 RMP Budget net of special initiatives</td>
<td></td>
</tr>
<tr>
<td>X 77.1% Percent of Federal onshore to total producing leases</td>
<td></td>
</tr>
<tr>
<td>48,750 RMP budget for onshore activities</td>
<td></td>
</tr>
<tr>
<td>General Administration</td>
<td>32,427</td>
</tr>
<tr>
<td>X 41% Percent of RMP to total RMP &amp; OCS FTE</td>
<td></td>
</tr>
<tr>
<td>13,429</td>
<td></td>
</tr>
<tr>
<td>X 77.1%</td>
<td></td>
</tr>
<tr>
<td>10,353</td>
<td></td>
</tr>
<tr>
<td>MMS Budget for Onshore Activities</td>
<td>59,103*</td>
</tr>
<tr>
<td>-400 Royalty-in Kind Program</td>
<td></td>
</tr>
<tr>
<td>-500 Late/Erroneous Reporting Assessments</td>
<td></td>
</tr>
<tr>
<td>-4,100 State Cooperative Audit Agreements</td>
<td></td>
</tr>
<tr>
<td>-150 Late Disbursement Interest</td>
<td></td>
</tr>
<tr>
<td>MMS Budget applicable to NRS</td>
<td>53,953</td>
</tr>
</tbody>
</table>

* The $59.10 million total is reduced to account for the estimated reimbursements Treasury will receive from industry for RIK Program and late and erroneous reporting assessments. Also taken out is the estimated funding the States receive from RMP for their cooperative audit agreement work and the late disbursement interest paid to them when RMP does not meet the FOGRMA disbursement time schedule.

After these adjustments, the MMS budget applicable to the NRS cost base totals $53,953 million. Please note, based on the Administration’s proposal, the prior year’s enacted budget (FY 1993) has been used to determine the FY 1994 NRS cost base.
BLM COSTS

To assist the Minerals Management Service in calculating the amount to be deducted from gross mineral leasing receipts for net payments to the States, the Bureau of Land Management must calculate the amount it spends to administer mineral leasing programs on Federal lands.

General Methodology Used

First, all amounts related to the management of Indian-owned minerals are excluded. Likewise program costs for conducting mineral commodities programs such as sand and gravel which are sold directly rather than leased are deducted. Finally, program costs for minerals subject to location under the mining laws are excluded from any calculations related to net receipt sharing.

BLM derives its actual obligations for the most recent completed fiscal year from the data included in BLM's official financial management system reports from the data reported by program subactivity. BLM applies the deductions listed above to exclude costs for Indian minerals programs and non-leasable minerals programs. BLM estimates the amounts of total program cost for the current fiscal year from the amounts enacted to date in the current appropriations act, and estimates the amounts for the next budget year from the amounts planned for these programs in the President's Budget request. BLM applies the same deductions for Indian minerals program, and non-leasable minerals programs as stated above. To the direct leasable minerals program costs (costs associated with leasing actions, NEPA compliance, etc.), BLM adds the factor for the program share of general administration program costs as explained below.

BLM then provides MMS with bureauwide Federal mineral leasing total program obligations for the previous (completed) fiscal year, and an estimate of these expenditures for the current and upcoming budget fiscal year.

Specific methodology to calculate BLM Federal Mineral Leasing Total Program Costs

To determine the amount of program cost, BLM starts with funds obligated in the BLM’s oil and gas, and other minerals management program budget subactivities. (The other minerals management program includes geothermal resources, mineral materials, solid leasable minerals, uranium, and oil shale.)

From the data in the BLM financial management records for the last completed fiscal year, for the oil and gas, coal, and non-energy leasable minerals program, BLM subtracts (1) any obligations identified as being in support of Indian minerals are subtracted from the total, and the amounts obligated for (2) mineral materials
and (3) uranium programs. (Uranium expenditures are solely to manage Indian lease.) These arithmetic operations produce the calculation of total direct BLM mineral leasing program costs on Federal lands.

To the above total, BLM adds a factor of 19 percent to account for the program’s allocable share of general administration program expenses such as, but not limited to; personnel management, contracting and property management services, financial management, budgeting, space rental, Federal telecommunications system costs, unemployment compensation, etc., as defined in BLM’s general administration and IRM operations and management budget activity justification.

The attached table shows the details of the BLM program calculations for FY 1992 actual obligations, FY 1993 enacted to date estimated costs and FY 1994 President’s Budget estimates.
<table>
<thead>
<tr>
<th>FUNDING CALCULATIONS</th>
<th>OIL AND GAS</th>
<th>COAL</th>
<th>OTHER MINERAL RESOURCES</th>
<th>COMMODITY</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>GEOTHERMAL</td>
<td>MINERAL MATERIALS</td>
</tr>
<tr>
<td>1992 ACTUAL</td>
<td>49,931</td>
<td>8,597</td>
<td>2,373</td>
<td>3,025</td>
</tr>
<tr>
<td>INDIAN MINERALS DEDUCTION ( )</td>
<td>4,497</td>
<td></td>
<td>0</td>
<td>211</td>
</tr>
<tr>
<td>COMMODITY NOT SUBJECT TO NRS ( )</td>
<td>3,025</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>SUBTOTAL</td>
<td>45,434</td>
<td>8,493</td>
<td>2,373</td>
<td>2,833</td>
</tr>
<tr>
<td>OVERHEAD @ 19%</td>
<td>8,637</td>
<td>1,613</td>
<td>453</td>
<td>542</td>
</tr>
<tr>
<td>1992 ACTUAL NRS COSTS TOTAL</td>
<td>54,066</td>
<td>10,100</td>
<td>2,824</td>
<td>3,431</td>
</tr>
<tr>
<td>1993 ENACTED TO DATE</td>
<td>51,702</td>
<td>8,453</td>
<td>2,395</td>
<td>3,737</td>
</tr>
<tr>
<td>INDIAN MINERALS DEDUCTION ( )</td>
<td>4,453</td>
<td></td>
<td>0</td>
<td>215</td>
</tr>
<tr>
<td>COMMODITY NOT SUBJECT TO NRS ( )</td>
<td>3,737</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>SUBTOTAL</td>
<td>47,249</td>
<td>8,151</td>
<td>2,395</td>
<td>2,852</td>
</tr>
<tr>
<td>OVERHEAD @ 19%</td>
<td>8,729</td>
<td>1,566</td>
<td>455</td>
<td>542</td>
</tr>
<tr>
<td>1993 ENACTED NRS COSTS TOTAL</td>
<td>55,988</td>
<td>9,938</td>
<td>2,850</td>
<td>3,393</td>
</tr>
<tr>
<td>1994 UNCONTROLLABLE CHANS &quot;S&quot;</td>
<td>.544</td>
<td>-22</td>
<td>-11</td>
<td>-14</td>
</tr>
<tr>
<td>1994 PROGRAM CHANGES</td>
<td>2,800</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1994 PRESIDENTS BUDGET REQUEST</td>
<td>53,158</td>
<td>8,431</td>
<td>2,384</td>
<td>3,720</td>
</tr>
<tr>
<td>INDIAN MINERALS DEDUCTION ( )</td>
<td>4,784</td>
<td>101.2</td>
<td></td>
<td>214</td>
</tr>
<tr>
<td>COMMODITY NOT SUBJECT TO NRS ( )</td>
<td>3,720</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>SUBTOTAL</td>
<td>45,274</td>
<td>8,320</td>
<td>2,384</td>
<td>2,038</td>
</tr>
<tr>
<td>OVERHEAD @ 19%</td>
<td>9,891</td>
<td>1,582</td>
<td>453</td>
<td>539</td>
</tr>
<tr>
<td>1994 PRESIDENTS BUDGET REQUEST</td>
<td>57,565</td>
<td>9,912</td>
<td>2,387</td>
<td>3,377</td>
</tr>
</tbody>
</table>

Bureau of Land Management

May 3, 1993

Net Receipt Sharing (NRS)
Mineral Leasing Administrative Total Program Costs ($000)
FOREST SERVICE COSTS

The Forest Service portion of the net receipts base totals $15.8 million which is comprised of $13.6 million for the Leasable Minerals Program and $2.2 million in associated overhead costs.

The Leasable Minerals Program provides coordination with BLM on the issuance of leases on Forest Service lands and jointly administers postlease operations and reclamation with BLM or other agencies within the Department of the Interior. Oil and gas leasing remains the largest commodity administered by this Program; however, coal, geothermal, phosphate, and other mineral leases are also administered.
Net Receipts Sharing

NRS Based on Administration & House Proposed Language

NRS Cost Calculation

The proposed language requires that the costs applicable to net receipts sharing be based on the prior year’s enacted budget authority for the applicable mineral administration and enforcement programs. For the MMS which performs royalty collection activities for Federal onshore, Federal offshore and Indian leases, its costs related to Federal onshore work versus offshore and Indian is based on the number of Federal onshore producing leases to total producing leases.

Based on the proposed language which permanently requires the recovery of 50% of the total mineral leasing program costs (States’ share is 25% of total costs), States’ payments are reduced by $34.578 million.

The following table and attachments detail the derivation of the NRS cost based on the proposed language.

<table>
<thead>
<tr>
<th>FY 1993 Enacted Costs</th>
<th>($millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bureau of Land Management</td>
<td>72.169</td>
</tr>
<tr>
<td>Minerals Management Service</td>
<td>59.103</td>
</tr>
<tr>
<td>USDA-Forest Service</td>
<td>15.786</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>147.058</td>
</tr>
<tr>
<td>Less certain costs *:</td>
<td></td>
</tr>
<tr>
<td>BLM lease administrative filing fees</td>
<td>1.500</td>
</tr>
<tr>
<td>Royalty-in-Kind fees</td>
<td>.400</td>
</tr>
<tr>
<td>State audit agreements</td>
<td>4.100</td>
</tr>
<tr>
<td>RMP reporting assessments</td>
<td>.500</td>
</tr>
<tr>
<td>Late Disbursement Interest</td>
<td>.150</td>
</tr>
<tr>
<td><strong>NRS COST BASE</strong></td>
<td>140.408</td>
</tr>
<tr>
<td>Proposed Amount to be Recovered (50%)</td>
<td>70.204</td>
</tr>
<tr>
<td>States’ share</td>
<td>34.578</td>
</tr>
</tbody>
</table>

* These items are estimated amounts because they are either not appropriated line items or are fees determined by industry actions.
Distribution of NRS Deductions

The proposed language requires the distribution of the NRS deductions to be based on the prior year's payment distribution. For example, if State X receives 10% of the total distributions to Treasury and States in FY 1993, its FY 1994 NRS deduction would be 10% of the amount required to be recovered.

Please note, the figures in all tables are based on FY 1992 distributions and thus subject to revision. Per proposed language, the FY 1994 distribution of NRS deductions will be based FY 1993 distributions.
## Mineral Leasing Receipts Distributed by Interior
### (Dollars in thousands)

<table>
<thead>
<tr>
<th>State</th>
<th>Gross Payments</th>
<th>Less NRS</th>
<th>Net to States</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alabama</td>
<td>1,248</td>
<td>93</td>
<td>1,155</td>
</tr>
<tr>
<td>Alaska</td>
<td>8,463</td>
<td>597</td>
<td>7,866</td>
</tr>
<tr>
<td>Arizona</td>
<td>144</td>
<td>10</td>
<td>134</td>
</tr>
<tr>
<td>Arkansas</td>
<td>4,373</td>
<td>379</td>
<td>3,994</td>
</tr>
<tr>
<td>California</td>
<td>27,045</td>
<td>1,907</td>
<td>25,138</td>
</tr>
<tr>
<td>Colorado</td>
<td>49,354</td>
<td>3,494</td>
<td>46,060</td>
</tr>
<tr>
<td>Florida</td>
<td>89</td>
<td>6</td>
<td>82</td>
</tr>
<tr>
<td>Georgia</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Idaho</td>
<td>1,818</td>
<td>128</td>
<td>1,690</td>
</tr>
<tr>
<td>Illinois</td>
<td>79</td>
<td>7</td>
<td>72</td>
</tr>
<tr>
<td>Indiana</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Kansas</td>
<td>1,236</td>
<td>87</td>
<td>1,149</td>
</tr>
<tr>
<td>Kentucky</td>
<td>138</td>
<td>13</td>
<td>125</td>
</tr>
<tr>
<td>Louisiana</td>
<td>803</td>
<td>74</td>
<td>729</td>
</tr>
<tr>
<td>Michigan</td>
<td>1,144</td>
<td>95</td>
<td>1,049</td>
</tr>
<tr>
<td>Minnesota</td>
<td>22</td>
<td>3</td>
<td>19</td>
</tr>
<tr>
<td>Mississippi</td>
<td>772</td>
<td>87</td>
<td>685</td>
</tr>
<tr>
<td>Missouri</td>
<td>866</td>
<td>101</td>
<td>765</td>
</tr>
<tr>
<td>Montana</td>
<td>21,116</td>
<td>1,489</td>
<td>19,627</td>
</tr>
<tr>
<td>Nebraska</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Nevada</td>
<td>8,832</td>
<td>623</td>
<td>8,209</td>
</tr>
<tr>
<td>New Mexico</td>
<td>114,149</td>
<td>8,049</td>
<td>106,100</td>
</tr>
<tr>
<td>North Carolina</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>North Dakota</td>
<td>5,786</td>
<td>408</td>
<td>5,378</td>
</tr>
<tr>
<td>Ohio</td>
<td>355</td>
<td>31</td>
<td>323</td>
</tr>
<tr>
<td>Oklahoma</td>
<td>1,641</td>
<td>122</td>
<td>1,519</td>
</tr>
<tr>
<td>Oregon</td>
<td>148</td>
<td>10</td>
<td>138</td>
</tr>
<tr>
<td>Pennsylvania</td>
<td>18</td>
<td>2</td>
<td>17</td>
</tr>
<tr>
<td>South Carolina</td>
<td>3</td>
<td>0</td>
<td>3</td>
</tr>
<tr>
<td>South Dakota</td>
<td>565</td>
<td>40</td>
<td>526</td>
</tr>
<tr>
<td>Tennessee</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Texas</td>
<td>853</td>
<td>93</td>
<td>759</td>
</tr>
<tr>
<td>Utah</td>
<td>35,666</td>
<td>2,515</td>
<td>33,151</td>
</tr>
<tr>
<td>Virginia</td>
<td>129</td>
<td>12</td>
<td>117</td>
</tr>
<tr>
<td>Washington</td>
<td>994</td>
<td>70</td>
<td>924</td>
</tr>
<tr>
<td>West Virginia</td>
<td>279</td>
<td>28</td>
<td>251</td>
</tr>
<tr>
<td>Wisconsin</td>
<td>7</td>
<td>1</td>
<td>6</td>
</tr>
<tr>
<td>Wyoming</td>
<td>235,836</td>
<td>13,999</td>
<td>221,838</td>
</tr>
</tbody>
</table>

### Total
- Gross: 524,173
- Less NRS: 34,574
- Net to States: 489,599

### NPR-Alaska (BLM)
- 60
- 4
- 46

1/ Includes Wyoming's share ($33.3M) of large coal valuation case estimated to be resolved and paid out by the end of FY 1994.

Reflects FY 1993 Enacted Budget Authority less estimated reductions for: State audit agreements, Royalty-in-Kind administration fees, late disbursement interest, BLM administrative filing fees, and assessments for payor late and erroneous reporting.

Note: Proposed language requires deductions be based on prior year actual payment distribution. Only FY 1992 actuals are currently available. If language is adopted, the deductions will be based on the actual FY 1993 payment distribution.
Mr. LEHMAN. Thank you very much.
We'd like to recognize Mr. Dewey for his statement as well.
You may proceed.

STATEMENT OF ROGER DEWEY

Mr. DEWEY. Thank you, Mr. Chairman.
I'm obviously not the Governor of Wyoming. The Governor thanks you very much for having this hearing and giving us this opportunity.
Due to problems in his schedule, he couldn't be with us. I sometimes suspect that those problems have more to do with the temperature in Washington in July than anything else.
I think the first thing that we need to say is, in a little different way than Congressman Thomas did, that our share of the royalties is not a dole. It is the price that this body was willing to pay for the Western States not to develop their tax base by the sale of the federal land.
I think all of us in the West would very quickly be willing to give up our share of the royalties if you'd just sell off the land. We're ready and we're not here to argue the cost-sharing issue any further. I guess it's here. We don't like it. We think it's illegal. We think it's the wrong thing to do, but it's here. So we won't further that debate any more.
But we are concerned about the costs, and we feel that the costs are just too great. It has been without accountability. We've been unable to get the numbers.
Congressman Thomas, a few years ago, spent the better part of the year trying to get the breakdown just between the MMS, the BLM and the Forest Service. It's been a program that's been absolutely cloaked in secrecy.
Mention has been made of the comparison of our costs in Wyoming to the costs of the MMS. We used their numbers. We are told their numbers have nothing in them except costs related to the direct collection of the royalties. And we still find them to be nearly $60.
We are doing the same things for $5. That kind of a difference really makes you nervous when you start thinking about getting before a committee like this and saying, hey, those numbers are twelve times as much.
You sit there and wait for somebody who's going to say, yes, but. But in fact, the IRS collects all of its revenues for a cost of $5 a $1,000. Their problems are a lot greater, a lot more complex, than either ours or the MMS'.
And that confirms for us, pretty well, that our numbers are correct. If we could move to our kind of a cost, we'd save $50 million a year. That's $25 million that would go to the States and $25 million that would go to reducing the deficit.
I think the first thing we'd like to ask of the committee today is that they recognize the cost-based distribution of these charges that have been included in the Senate bill. It is more fair. It is nearly half of the charge to Wyoming, based upon a share of the revenues.
We offer really two solutions to bringing the cost in line. Wyoming is ready, is eager, to undertake a pilot program.
We think we can develop a collection program and do the work by use of the pilot program and prove that this work can be done for significantly less money.

We’ve included with our testimony the proposal which has been prepared by our staff and Anderson Consulting, which would put us in that business.

The proposal provides for collection, and I need to reinforce that. As Mr. Fry said, we’re not looking to get into the appeals business or the rules and regulations creation business, or those kinds of things. Those are things that MMS should continue to do.

But it is our firm belief that these costs are not going to be brought under control. We won’t make any progress unless somebody backs off and takes a look at this program and says, can we reinvent how to collect royalties for the Federal Government.

We’ve tried the incremental approach of let’s fix this, let’s fix that, and it just isn’t going to work. And the pilot is one way to take a fresh look and develop a whole new program and prove that it can be done for considerably less.

We can put a program like that in place, as the proposal points out, for a little over $6 million. It would take somewhere between 18 and 24 months to develop.

We would, in that process, completely review how the royalties are to be collected. We would work with the industry.

It is certainly not our intent that we would do a collection program that would be more onerous to the industry. It’s our belief that we can considerably reduce their reporting requirements and be much more efficient and get the job done.

The operating costs, as estimated by the consultant, would be in the nature of $1.4 million per year to collect all of the Wyoming royalty leases.

If you extrapolate from that, that would mean that MMS would be able to do all of that collection procedure for $7 million. Even with 35 percent for the other activities and another 35 percent for audit, there are significant savings.

This committee asked that we address the issues of non-delegable functions, and we have in the written testimony.

Basically, most of the functions that were in the report last year as non-delegable are not related to collection. We agree with what Mr. Fry has said. Those functions, for the most part, are things that need to be done by MMS.

There are some of them that mechanically we can do and we’re doing now in the audit procedures. If you’re not willing to address the problem by instituting a pilot, then we would propose that there be some kind of a complete review of MMS and its procedures and how they do it.

And we would propose that that be done by somebody unrelated to MMS, that it be done by the States who care. And involve the industry, so that we make sure we don’t make things worse for them.

But it would be appropriate, in our view, to create—I don’t know, Congress comes up with the names, not us—a commission, board, or whatever you want to call it, but some kind of an outside body to take a look at it, completely changing it and making recommendations as to how it should be done.
I think part of that has to be a review of the requirements that are imposed upon the MMS by this body to see what, in that area, can be done to relieve costly operations.

I guess I would say simply that we hope you will authorize the pilot project. If not, we certainly ask that you establish the review. I want to say here, for the record, that I've had more conversation with the MMS this past week than I've had in the past three years.

And we're here to answer your questions.

[Prepared statement of Hon. Mike Sullivan, Governor, State of Wyoming, submitted by Mr. Dewey, follows:]
My name is Mike Sullivan and I am the governor of the State of Wyoming. With me are Roger Dewey and Earl Kabeiseman. Roger is the Director of our Department of Audit and Earl is the Director of our Department of Revenue. Earl collects Wyoming severance taxes. Roger audits severance taxes but he also audits federal royalties under a delegation of authority from the Mineral Management Service. Wyoming is the largest state in the production of minerals from federal lands.

I want to thank you for this opportunity to share with you our thoughts and concerns about the Mineral Management Service's costs and the state's sharing in those costs. I am here not only as Governor representing the citizens of Wyoming but also as a member of the Western Governor's Association representing the other western governors and their citizens.

I feel compelled to first risk being thought to be preachy in order to make two points quite clear. The sharing of mineral royalties with the states is not a dole or handout but is the price that this body, Congress, was willing to pay for the privilege of not selling the federal lands as they had in the east, the midwest and the south. By retaining the federal lands the nation denied to the affected states the ability to develop their tax base and their economy and to control major portions of their territory.

That decision by Congress may well have been the right one and certainly
the nation has accrued many benefits from it. The affected states have accrued precisely the result expected - limited development of their tax base and their economy. If the decision were to be made on strictly economic terms, I am sure that every western governor would happily give up the mineral royalty share in return for the sale of the federal holdings in his state.

Each state has committed its share of the royalties to public service expenditures deemed to be of priority in that state. In my State approximately half of those funds are earmarked to be distributed to educate the children in our schools. Another 30% are dedicated to maintain non federal roads and highways. We have many miles and very little tax base. The balance is provided to counties, towns and the University to provide citizen services. Beginning in 1991 our share of those funds was diminished by a charge to us for the administration and collection of those funds. This has either caused these entities to diminish their services or has made it necessary for them to seek alternative sources of revenues placing pressure on their ability to deliver other services. This sharing has reduced your costs, but it has been achieved by increasing costs to, or reducing service by, these local government entities. Last year's charge to Wyoming of $13 million dollars took $130 for each public school child from the support to our schools.

You will be relieved to hear that, having made these points, I am not here to further the debate on cost sharing. It is here. It has been here for several years. It has been cloaked in secrecy as to actual costs and an unwillingness to divulge budget and expense information. But it is here.

Our concern greater than sharing is cost. It is absurd! It is without accountability! It is draining funds from valuable programs at the federal, the state and the local levels. The MMS claims, in their Net Receipts Sharing Reductions Schedule a 1992 cost of $54,900,000. Their calendar year collections of onshore royalties were $937,499,852. This is a cost, using their own numbers, of $58.56 per thousand dollars of royalties collected. Wyoming performs a nearly identical process of collecting and
auditing severance taxes for a cost of $4.98 per thousand - one twelfth the cost. Such a tremendous difference raises questions about the numbers so I suggest you look at the IRS. They collect all taxes for $.50 per hundred or $5.00 per thousand. Their function is far more complicated than either Wyoming's or MMS's, but their number confirms ours.

Attached to our testimony is a schedule, using MMS figures, which details these costs. It also shows that Wyoming collects and audits its severance taxes with 30 employees. MMS performs the same functions for 3.7 times as many revenue dollars with 37 times as many employees - 1107. Actually since royalties are generally 12% and severance taxes generally 6%, we process more than half as many subject dollars with 3% of the people.

If MMS collected at the same cost as Wyoming, or the IRS, it would cost $4,687,500, a savings of $50,212,500. That is $25 million dollars a year to reduce the federal deficit and $25 million that you would not charge the states. That is our concern!

The MMS cost numbers used in the calculations are not really cost numbers but are from something called the "Derivation of Net Receipts Sharing Reductions Schedule". That is Interiorspeak for saying, "we don't want to talk about cost sharing because we don't want to talk about costs." Actual expenses are cloaked in secrecy. Representative Thomas waged a lengthy battle several years ago to get MMS to even provide the split of the numbers between MMS, BLM and Forest Service. Sharing in a schedule or an appropriation denies any accountability to the states of what they are being charged. This certainly seems a strange way for an agency to act when their only charge is collection and accounting.

By persistence the Wyoming delegation managed to drag out of Interior the actual costs related to managing Wyoming leases and collecting the related royalties. It turns out that the charge to the State of Wyoming would be $6 million less if the cost sharing charge were based upon actual cost rather than the "schedule" charges generated by a proportion of revenues formula. This is because the costs of management and collection are more a function of number of leases or units than they are of dollars collected. The Senate
has adopted an approach in their appropriation which caps the costs to be shared at an amount based on those costs actually expended. We would hope that this body would join in that plan. Even more fair would be to limit the costs to be recovered to the rate of costs incurred by the IRS.

We offer two solutions to bringing the costs into line. First, we propose that you delegate the collection process to the states. I am prepared today to discuss the time and dollars involved to develop a pilot program and prove that it can be done for significantly less cost.

Wyoming is eager to undertake a pilot program of royalty collections from leases located in our State under a delegation of authority similar to that under which we now conduct the MMS audits. Other states may also be ready. We are prepared to perform all of the collection related functions up to, but not including, the appeals process. We would collect the royalties, make necessary adjustments with payors, account for them, deposit them to MMS and report to the MMS.

I authorized a study of the collection process and its potential delegation to us. I did so because of our interest in reducing these costs and our belief that a delegation of the collection process to the states would achieve such a reduction. It was performed by State personnel and by the consultant that is currently designing and installing our new mineral tax system. That study resulted in a Proposal to Implement Federal Royalty Collections Program for the State of Wyoming. A copy of that proposal is attached to my testimony. We have expended considerable staff time and nearly $50,000 of scarce State funds to have this proposal prepared and we hope you will give it full consideration.

The Proposal is attached to this testimony. The Proposal provides for collection of royalties due from leases in Wyoming. While it assumes that Wyoming would collect those royalties in accordance with all of the present royalty related rules, regulations, lease terms and policies it does not assume that collections will be done in accordance with the rules related to the present collection system or procedures. It is our firm belief that the
problem is the present system and procedures - that we will not make any progress on cost containment unless we replace it. That belief has been confirmed by the consultant that participated in the preparation of the plan. During the period of the pilot we assume that Wyoming would not be subject to changes other than those applied to all states and that we would be accorded the cooperation necessary to make the project work.

Our planned system will be designed to minimize impact on the industry payors. We will ask them for less information. We will either ask for the information in the same format that they now supply it or in their own accounting format. Our system will make it easier for the payor.

As you can see it will take 3 to 6 months to re-engineer the approach to collections. It will take another 6 months to design a system. Putting it in place and testing it will take 12 to 15 months more. There is overlap in these schedules. The bottom line is that we can have a system in place in as little as 18 months if all goes well and if we have the full cooperation of MMS. In any case, we should have a system in place in no more than 24 months. We estimate the cost to develop and implement the system to be $5.6 million. Putting an organization in place to operate the system will cost another $900,000. If you examine the program closely you will see that we have been extremely conservative in our estimates. We have included in the estimates funds to address potential contingencies which may occur.

If you can authorize the project by 10/1/93 we can have the system in place to begin collection 10/1/95, possibly much earlier. That is the beginning of your fiscal year. While it would make some things smoother to make the start coincident with your fiscal year, that is not especially important. We can start whenever the system is ready and coordinate our collections with those of the MMS.

Also attached is a description of the costs of operating the system. These costs are understandably higher in the start up years, but still substantially under ongoing costs of the MMS. These costs do not assume any increase in the level of audit activity under our delegation contract. If it should be desired that we do all of the Wyoming audits we can provide cost estimates
for your consideration. They will be less than current costs.

The State of Wyoming and Anderson Consultants estimate the operating costs of the system to be $1.4 million dollars per year - including the contingency funds for unexpected costs. We would be doing the lion's share of MMS's work for one tenth of what they now want to charge us as our share of their cost. If you extrapolate from the numbers - Wyoming is 20% of MMS's costs - the cost to run a re-engineered system for all states would be $7 million plus the cost of the administrative functions such as appeals, rule making, etc. A far cry from $55 million!

Last year the MMS study group addressed the delegation issue. The original group included a representative of Wyoming and one other state. After the group had finished most of its work and had prepared a draft report, the MMS rewrote the report without the involvement, or even the review, of the state participants. The MMS report cited nondelegable functions as a major barrier. You have asked that we address the functions as they are reported on pages 5-1, 5-2 and 5-3 of their report.

**Allocating and obligating Federal Funds.** I hardly think that calculating overpayments can properly be called obligating Federal monies. If checks are to be issued they could be issued by MMS. Mechanically we can prepare and account for them - or not as you choose.

**Conducting administrative hearings and appeals.** Whether we could, or not, is unimportant. We should not. MMS should.

**Issuing final regulations and policies.** Delegation of collection functions does not include in any way making of rules or policy.

**Authorizing reports to the Congress and the President.** This is not a part of the collection process and has no bearing on whether the functions could be delegated.

**Enforcement.** Collections are done on a voluntary basis.
Enforcement is not a collection function and would not be delegated.

The report further references a 12/16/91 OMB policy letter which they say precludes the delegation. Congress certainly has the final say. It would not seem that there should be any significant policy reason to deter delegation to another party of equal interest.

**Lease terms.** There is no reason to consider leasing authority in the delegation of a collection process. The authority would not be delegated in any way, and in point of fact is not MMS authority, but BLM authority.

**Royalty in kind** is not a significant issue. If MMS should want to take royalties in kind they should certainly handle them.

As you can see most of the issues raised are unrelated to a delegation of the collection process. Those that are related can be dealt with.

Some will ask why do a pilot with the largest state program? We would suggest that the state with the largest program is likely to be the state with the most expertise to apply to the project. A new system is clearly required!. The cost of designing a system will be the same whether the state's collections are small or large. Wyoming is currently designing a new system for collection of severance taxes, so we not only are familiar with mineral related collections we also have current expertise and experience in managing the development of a minerals system. But if it is not Wyoming, we are supportive of the pilot and will work with the designated state. We have confidence that any of our sister states can develop and implement a program less costly than the current one.

If you are not willing to address the problem of excessive cost by instituting a pilot we would propose a complete review of the MMS current program. We have asked them why their costs are so high. The response has always been that they are required to do many things that we are not. They have
been unwilling, or unable, to tell us what those things are. There isn't much you have to do to determine royalties. You have to know the value of the mineral severed. You have to know what the mineral is, so you can apply the correct royalty rate. You have to multiply. Certainly there are issues related to value such as deductions for post severance cost, etc., but we have those, too. If they are doing other things, they are not related to collecting royalties and the states should not be called upon to bear their cost.

Each and every function of the MMS must be subjected to a series of challenges - Why do you do this? What would happen if you didn't? Why do you do it this way? Couldn't it be done in a less expensive way? Can you do this with less burden on the industry? etc. etc. etc.

Our experience with the management of the agency has been that they do not want to find manpower or dollar reductions. The agency is very small - by federal standards. Reductions would make it smaller and lead to it losing agency status and becoming a part of BLM.

We fear that the desire to reduce MMS's costs does not exist within the agency. It has been described as an agency made up of dozens of little cultures which have been developed over a long time with little or no change in their makeup. Any reorganization or reduction will be strongly resisted.

The industry's major concern is that any change would cause disruptions in how they report and pay. Such disruptions often require them to redesign their accounting and electronic systems. Based upon past experience that concern is legitimate. In the past changes have not considered impact upon payors. So the desire does not exist in the industry. The states who pay half of the exorbitant costs seem to be the only entities motivated to reduce them.

If you should decide not to authorize a pilot program of delegated collection, then it is incumbent on you to challenge the costs. Our experience is that MMS won't do it. We ask that you set up a review body to ask the challenging questions. The challengers clearly need to be representatives of the states. The industry needs to be represented. MMS should not be represented!
Such a review has been discussed with our delegation and with other members of Congress. The idea has been received favorably. It would seem to be an appropriate response if the review body is made up of members who have an interest in changing the system for the better.

I hope you will authorize the pilot project! If not I ask that you establish the review. I can't imagine that you would do neither. If not, simple fairness would dictate that the states who will pay half of the agencies' costs be given an equal voice in the management of those agencies. We are not interested in being involved in the day to day management, but certainly we have much to contribute. We both have much to gain by involving the expertise and knowledge of the states in the making of policy and in the management oversight - and especially in the establishment of processing systems. This is not only true of MMS but also of the other agencies whose costs we share - BLM and Forest Service. We will ultimately come to that. The pilot or the review would be a simpler solution to implement and I am confident would bring us both significant dollar savings in a shorter period of time.

We are prepared to answer questions. My associate, Mr. Kabeiseman, was involved in the development of the Proposal and estimate of the operating costs. He is prepared to answer specific questions about the Proposal and the costs. It is our desire to work with you to solve this problem which is so costly to both our governments.
### Wyoming Department of Audit

#### Mineral Revenues and Expenditures

**Federal vs State of Wyoming 1992**

**FileName:** COSTCOMP.WR1  
**Date:** June 18, 1992

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FOOTNOTE LEGEND

A - PER PHONE CALL FROM MICHAEL BAUGHER, PUBLIC AFFAIRS OFFICE - MMS, CALENDAR YEAR 1992 TOTAL STATES SHARE $472,286,727; WYO SHARE 184,872,805; ALASKA SHARE $7,957,802. ((472,286,727-7,957,802)/50)+(7,957,802/50)=937,499,852

B - WYOMING FY92 ANNUAL REPORT DEPT OF REVENUE

C - WYOMING'S SHARE DIVIDED BY 50%

D - STATE FY 92 DEPTS OF AUDIT AND REVENUE SEVERANCE BUDGETS

E - PER HOLLY TOMLINSON, ROYALTY LIAISON OFFICE, DOI MMS - DERIVATION OF NET RECEIPTS SHARING REDUCTIONS SCHEDULE

F - (WYOMING TOTAL ROYALTY DOLLARS/TOTAL ON-SHORE ROYALTY DOLLARS) * MMS TOTAL COST

G - PER HOLLY TOMLINSON, ROYALTY LIAISON OFFICE, DOI MMS - STAFFING LEVELS

H - PER HOLLY TOMLINSON, ROYALTY LIAISON OFFICE, DOI MMS - STAFFING LEVELS

I - PER HOLLY TOMLINSON, ROYALTY LIAISON OFFICE, DOI MMS - DERIVATION OF NET RECEIPTS SHARING REDUCTIONS SCHEDULE

J - (WYOMING TOTAL ROYALTY DOLLARS/TOTAL ON-SHORE ROYALTY DOLLARS) * TOTAL FEDERAL ADMIN COST

K - (FEDERAL ADMIN COST/TOTAL ON-SHORE DOLLARS)*1000

PREPARED BY
Wyo Dept of Audit
## Wyoming Department of Audit

**Mineral Revenues and Expenditures**

**Lease Administration Costs**

**Federal vs State of Wyoming**

1992

**File Name:** ADMINCMP.WR1  
**Date:** June 18, 1992

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**Lease Administration**

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**Cost as a Percentage of Collections**

- Wyoming: 1.19%
- Federal: 8.69%

**Cost per $1000 Collected**

- Wyoming: $11.85
- Federal: $86.93

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**Footnote Legend**

A - Wyoming State Land Office Schedule - 1992  
B - Total On-Shore Dollars, Mineral Revenue Schedule, Fed vs State of Wyo  
C - Per Holly Tomlinson, Royalty Liaison Office, DOI MMS - Derivation of Net Receipts Sharing Reductions Schedule

Prepared by  
Wyoming Dept of Audit
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INFORMATION OBTAINED FROM
Gerald Hutchinson
Wyo State Land Office
Mr. LEHMAN. Thank you. I appreciate your testimony.

Let me just say, at the outset, we wouldn't be having this hearing today if we didn't believe this was a serious matter and something that we're concerned about.

I certainly appreciate Mr. Fry not only being here today, but coming by my office to see me, and having discussions there as well. I understand he's new in this role.

The first thing we do is haul him up before the Congress to listen to our complaints about the way the operation's been run for the last eight years, during a time in which he was doing something entirely different from what he's doing now. So I understand your situation. I know you have brought some staff with you that can help us out here as well.

Let me just start by just asking the basic question, I guess.

Mr. Dewey, in his testimony, basically says that it costs the IRS $5 a $1,000 to collect tax money. What they do in the State of Wyoming is roughly equivalent to that. Yet it costs the Minerals Management Service just under $60 per thousand in this area.

Why?

Mr. FRY. I'll give it my best shot at trying to answer that. I'm not sure I can completely answer that.

I think some of the time, we're talking about apples and oranges. In MMS, when we do this costing, we're making a determination of what it costs for the purpose of making a deduction. We go through a process that has been somewhat imposed upon us to determine what those costs are. From the MMS perspective, we only spend about 1 percent of the dollars that we spend on total program costs in this process for royalty collection specifically. The rest of it is for other efforts that relate to royalty collection.

Now we end up in document processing, database maintenance, report correction. Some of these things are things the States are involved in, the things that we are involved heavily in, we have to keep the database of all the leases because we end up having to make payments, not just to the Treasury, but we have to make payments to Indian tribes and to BIA for specific Indian allotees. The Indians are taking up about 8 percent of these dollars that are expended.

We do a great deal of verification. This is a little different than the IRS. It's something that the Congress has asked us to do where we look at each and every line of every report to determine whether or not the data that have been submitted are correct on the front end. This is obviously an increased cost.

We end up involving about about 33 percent of our money in the audit. I cannot explain the difference between our apples and apples at the IRS, because I don't know what their dollars are made up of.

Our dollars are based on these kinds of figures. I did mention earlier the non-delegable functions. I think about 22 percent of those dollars that we spend relate to those kinds of functions.

I'm not trying to suggest that I know how the State of Wyoming calculates their $5. But I wonder, and would be more than happy to sit down with them and determine whether our $60 and their $5 are the same dollars.
I think there are a number of things that we do that we're required to do that they do not have to do with their collection effort. That means that we're talking about apples and oranges.

If we get down and say the MMS, on just royalty collection, spends \( x \) dollars, and maybe that's $3, and the State of Wyoming has learned how to do that for $2. We'd want to learn how to do that for $2. We would like to have the opportunity to learn from Wyoming as to how better to do that.

So we look forward to meeting with them and working with all the States on how better to do this.

I'll make one other statement along this line. MMS has volunteered itself for the Vice President's Reinventing Government Task Force. They're going to have a number of laboratories. We have asked to participate in one of the laboratories which is to take a clean look at the collection process of the MMS.

This involves not only the MMS, but States, Indian tribes, and our constituents in the oil business. This is just beginning. We think this gives us an opportunity to take a fresh look at how the process works, and take the recommendations of that group, which is all the people involved in the program, and see if we can improve not only what it costs us to collect, but the efficiency of our collection.

Mr. LEHMAN. Can you elaborate a little more on how that's going to work?

Mr. FRY. Yes.

The way it has started is the initial group within MMS has been put together. They met in Columbus for the last 2 weeks with a clean slate. They didn't send any managers; they were sent in to develop some general ideas of how this might occur.

Now that that has taken place, we've reconstituted a committee of industry, States, and tribes, which will become a part of the greater committee, which will come up with an overall plan. It's not taking a look at how MMS does it; it's taking a fresh look at how this should be done.

That's what we're asking this group to do. They're supposed to have a report to the Vice President by the end of September, I believe.

And what I foresee is, once that report is generated, we'll keep that group together to the extent that there are recommendations they feel should be implemented. We'll keep that group together in order to come up with implementation plans.

I think what will happen by the end of September will be a broad overview and not an implementation plan. I think we'll have to have an implementation plan after September.

Mr. LEHMAN. So when do you see that?

Mr. FRY. I'm not exactly sure how long that will take. I would hope that the implementation plan, to the extent one is needed, will be done by the end of the year. That's, again, that group's mission and task; it's not being run by the MMS.

In turn, our people listen to the people who are coming in from industry and the States and the tribes, who have their own decisions as to how best this should be done.

Mr. LEHMAN. And your department was selected by the White House for this?
Mr. FRY. We have been selected. We volunteered and we were selected. I'm not sure which came first.

Mr. LEHMAN. Hopefully there, we can address some of the concerns that are being raised here.

Also, can you explain, for me, how you come to the conclusion that 19 percent is a reasonable figure to charge for overhead at BLM?

Mr. FRY. I'm going to defer the answer to that question, if I might.

Jim, do you know how that's calculated?

Mr. LEHMAN. BLM is charging 19 percent for overhead.

Mr. FRY. BLM is charging 19 percent. MMS is charging 21 percent which includes executive direction. It's not being charged by BLM because BLM's operation is so field-oriented. It's charged against their State operations, whereas, in MMS, because there's one central operation, there are some additional executive direction costs that have gotten into that number.

I will be glad to submit to the committee a breakdown of how that's arrived at, and how we've gotten it.

There are a number of ways of calculating administrative overhead, and this has been calculated based on one of those formulas. We'll be glad to submit the formula that we're using.

[The information follows:]
The following is a breakdown of how MMS determines its indirect or "overhead" costs supporting the Royalty Management Program’s (RMP) onshore work efforts. All of MMS’ non-direct program support costs are in its General Administration (GA) subactivity.

(Dollars in thousands)

<table>
<thead>
<tr>
<th></th>
<th>GA FY 1993 enacted budget</th>
<th>1/ Percent of GA support to RMP versus all of MMS determined on a FTE basis: ( \frac{\text{RMP FTE}}{\text{RMP + OCS FTE}} = 41% )</th>
<th>GA support to all of RMP</th>
<th>2/ Percent of Federal onshore to total producing leases to determine GA support of RMP onshore work efforts</th>
<th>Net GA support of RMP onshore work</th>
<th>21% Percent of GA to RMP onshore budget ( \frac{10,353}{48,750} = 21% )</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$32,427</td>
<td></td>
<td>$13,429</td>
<td></td>
<td>$10,353</td>
<td></td>
</tr>
</tbody>
</table>

1/ FTE = Full Time Equivalent personnel, OCS = Outer Continental Shelf Lands Program which is the other program area within MMS

MMS’ ratio of overhead to direct costs is 21% versus BLM’s 19%. BLM and MMS differ organizationally and therefore many costs termed “overhead” by MMS are included in BLM’s direct costs. Examples include:

<table>
<thead>
<tr>
<th>Type of Cost</th>
<th>BLM</th>
<th>MMS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Administrative appeals and policy staff</td>
<td>Direct</td>
<td>Overhead</td>
</tr>
<tr>
<td>Non-GSA rent or utility payments</td>
<td>Direct</td>
<td>Overhead</td>
</tr>
<tr>
<td>Executive Management (public and congressional affairs, Directorate, etc.)</td>
<td>Excluded *</td>
<td>Overhead</td>
</tr>
</tbody>
</table>

* Per the Federal Land Policy and Management Act, BLM cannot include these functions for cost recovery/reimbursement purposes.

When adjustments are made for organizational differences, MMS’ overhead rate equates to 19% as well.
Mr. LEHMAN. I understand there's a gentleman from BLM here, if you want him to comment.

Mr. FRY. There is.

Mr. LEHMAN. Why don't you state your name.

Mr. HILDEBEIDEL. I'm Roger Hildebeidel of BLM.

As Mr. Fry said, our 19 percent is simply the relationship of general administration to total funding for operations at BLM. It is a very simple mathematical calculation that's applied to direct costs to come up to the whole cost share.

I understand that within BLM our activities related to mineral leasing are part of the overall costs. They're not royalty collection amounts, but they are the activity of BLM that issues the lease. We supervise the activities of oil and gas and minerals.

Mr. LEHMAN. Mr. Dewey, in your area of concern here, it seems to me there are two things to look at. One is what is going into the calculation to determine what is the cost and is that really a cost that ought to be passed on to you as an administrative cost.

And then the second is the question of whether or not it could be operated more efficiently and those costs could be reduced in that fashion.

Do you have any questions about the former or any opinions?

Mr. DEWEY. Mr. Chairman, to start with, we don't think that anything should be included.

Mr. LEHMAN. We're not selling our land either.

Mr. DEWEY. Right. We've given up on that one.

When you address the BLM issues, BLM is doing a lot of things—that you folks have said they should do—that really don't have much to do with the collection of royalties.

They're related to leasing but, for example, there's an enormous amount of environmental work that's done in the BLM. There is, in our opinion, no basis for putting any of it in.

Mr. LEHMAN. For charging that overhead off to the mineral leasing program.

Mr. DEWEY. It's hard for us to understand why that should be added in as collection costs.

The other part of the number that is of great concern to us is, can it be done for less.

There is a comparison, included with our testimony, of our State's royalty collection process on State-owned lands. And you'll see in there that our costs are significantly less than BLM's. That is truly apples and oranges.

["Proposal to Implement Federal Royalty Collections Program for the State of Wyoming" follows:]
Proposal to Implement

Federal Royalty Collections Program for the State of Wyoming

July 1993

This document represents a proposal to plan, design and implement a Federal Royalty Collections Program for the State of Wyoming. The document was prepared by the State of Wyoming with assistance from Andersen Consulting.
State of Wyoming
Proposal to Implement
Federal Royalty Collections Program

Table of Contents

I. Background and Program Information
   • Department of Interior and Mineral Management Service ...............I-1
   • Wyoming .......................................................................................I-1
   • Issue ..............................................................................................I-3
   • Proposed Program Objectives ....................................................I-3

II. Proposed Program Overview
   • Scope of the Program ....................................................................II-2
     • Collection Functions to be Performed ........................................II-2
     • Roles of Wyoming, MMS, and BLM ............................................II-3
     • Organizational Structure .........................................................II-4
     • Information System .....................................................................II-5

III. Implementation Approach
   • Time Line .....................................................................................III-1
   • Implementation Phases and Tasks .................................................III-2
   • Project Oversight ........................................................................III-6

IV. Cost Estimates
   • Summary Cost Estimates and Analysis ........................................IV-1
   • Re-engineer Processes ..................................................................IV-3
   • Organization Costs ........................................................................IV-3
   • Information System Costs .........................................................IV-4
   • Assumptions ................................................................................IV-5
I. Background and Program Information

This section provides background and an overview regarding the proposal to implement a Federal Royalty Collections Program for the State of Wyoming.

Background

*Department of Interior and Mineral Management Service*

The Department of the Interior (DOI) is responsible for the management of all mineral leasing activities on Federal and Indian lands. Authority for the royalty management activities involving Federal and Indian mineral leases has been delegated to the Mineral Management Service (MMS) within the Department of the Interior. The Federal Oil and Gas Royalty Management Act of 1982 required the Secretary of the Interior to establish a comprehensive collection and fiscal accounting and auditing system to provide the capability to accurately determine and collect oil and gas royalties. The MMS processes both on-shore and off-shore Federal leases with on-shore collections presently exceeding $900 million. Currently, states receive 50% of the royalties collected from Federal leases contained within each State.

*Wyoming*

The Wyoming Department of Revenue (DOR) is responsible for the collection and distribution of taxes as authorized and mandated by Wyoming statutes. Within the Department, divisions administer tax programs. The Mineral Tax Division is responsible for determination and collection of petroleum and solid mineral severance taxes as well as determination of related ad valorem valuation for Wyoming counties.

Wyoming is in the process of implementing a new comprehensive Mineral Tax System (MTS). MTS is scheduled to be implemented by October 1993. The Mineral Tax System provides functions to support data capture, error handling, remittance processing, accounting, revenue distribution, annual certification of ad valorem valuations, and management reporting. Wyoming recognized the differences between industry accounting levels for taxable properties, wells, leases or units, as well as potential differences in the way individual taxpayers perform their accounting functions. Therefore, MTS is designed to provide the flexibility to adjust to industry accounting levels. This is accomplished by utilizing relational database technology and allowing industry to align its property level reporting structure for severance tax reporting to its own internal accounting methods.
Federal Royalty Collections Program
State's Share of Royalty Collections and Net Receipt Sharing Deduction
Federal Fiscal Year 1992

State's Share of On-Shore Royalty Collections
Federal Fiscal Year 1992
(Millions)

- Wyoming: $93 (39%)
- Colorado: $46 (19%)
- New Mexico: $107 (42%)
- All Other States: $133.2 (38%)

State's Share of Administration Deduction by MMS
Current Net Receipts Sharing Method
Federal Fiscal Year 1992
(Millions)

- Wyoming: $34.2 (42%)
- Colorado: $2.5 (10%)
- New Mexico: $13.1 (16%)
- All Other States: $4.5 (29%)
Issue

In 1990, a Federal provision was enacted requiring net receipts sharing of costs relating to Federal land royalty collections starting with fiscal year 1991. As a result, states began sharing in the costs of collecting Federal royalties. Current net receipt sharing is 50% of costs, but has been proposed as high as 100%. It was also decided that allocation of costs would be based on the percentage of revenues received rather than on the actual costs associated with processing the revenues for each state. Basing states share of costs on the revenue received is itself a controversial issue since costs are typically more dependent on other factors such as number of payors or leases rather than revenue processed.

Wyoming Governor Mike Sullivan pointed out in a May 31, 1991, letter to selected congressmen that the issue pertains to the fairness of asking states to pick up an equal share of a cost that is far greater than that for which the states could perform the task themselves. In addition, states are asked to pay a cost in which they have little or no control over the management of the program. With FY 1992 Wyoming royalty revenues exceeding $365 million, Wyoming received in excess of $180 million dollars for their 50% share of royalties. With current MMS costs to administer the royalty program exceeding $55 million, the cost to Wyoming becomes difficult to justify. Using rounded figures, Wyoming’s receipts represent approximately 40% of total on-shore royalty revenues. Using the existing revenue-based sharing allocation, over $23 million of administration costs will be charged against Wyoming’s royalty receipts. Applying the current net receipt rate of 50% to the $23 million and using Wyoming’s FY 1993 estimated royalties of $200 million results in a cost to collection ratio of more than $55 per $1,000 collected. Contrasting MMS administrative charges to Wyoming’s costs to collect its mineral severance taxes raises many questions as to the efficiency of the Federal mineral royalty program. For example, Wyoming’s costs to administer the Mineral Severance Tax program is less than $5 per $1,000 collected. It becomes difficult for states to justify paying the MMS costs when it is a result of possible inefficiencies in MMS reporting and processing requirements and when it is possible for states to perform the royalty collections function for substantially less.

Proposed Program Objectives

The focus of implementing a Federal Royalty Collections Program in Wyoming will be to develop business processes and systems that simplify the requirements for royalty payors, the MMS, and the State of Wyoming, and provide an integrated and flexible framework to facilitate implementation by other states or the MMS.
Wyoming proposes to re-engineer or "re-invent" the business processes of collecting royalties for Federal leases. We believe the proposed royalty collections program must be re-engineered to gain efficiencies while maintaining appropriate standards. Guiding principles for the proposed royalty collections program are described as follows:

**Process Re-engineering:** It is imperative that royalty collection processes be reviewed and improved and/or alternative methods for performing the collections and accounting functions be developed. Simply taking current MMS functions and moving them to Wyoming would do nothing but aggravate and transfer problems and inefficiencies that currently exist. By reviewing current processes and requirements and becoming innovators, we propose to "re-invent" the Federal royalty collections function to simplify and modernize procedures, processes, and requirements.

**Standardization:** Critical to the proposed project is the identification of responsibilities and needs for standardization. It is important to establish standards and procedures for delegation to avoid unnecessary complications and burdens for industry if future delegations occur. The goal of this process should be to ease the requirements on industry while maintaining sufficient, but not excessive, information that allows for collection of revenue associated with Federal leases. To achieve this goal, a standardized, yet flexible, system should be developed and implemented to enable consistent reporting by industry to individual states or the Federal government. The system should allow reporting at accounting levels used by industry while supporting the information requirements of states and MMS.

In addition to the guiding principles that are the basis for the proposal to implement the Federal Royalty Collection Program, the project will strive to accomplish the following key objectives:

**Cost Reduction** - Current administrative costs for processing royalty collections is extremely high when compared to other collections processes such as the IRS or the State of Wyoming. The project should strive to significantly reduce the cost of collecting royalties.

**Simplified Reporting Requirements** - The actual collection of data on monthly returns will be reduced or simplified to require only information needed to calculate and collect royalties. Other data not required to calculate royalties, such as purchasers of products, can be collected on annual returns or during audits, as required. Reducing the amount of data reported and processed will simplify the program and enable efficiencies to be realized.

**Improved Efficiency** - Overall improvements in the collection process should be realized. Improved efficiency should be attainable if simplified reporting requirements and flexible reporting levels combined with up-to-date technologies are implemented. These include Electronic Data Interchange (EDI), Image Processing, Character Recognition, and Client/Server Technology.
Flexible Reporting Levels - The revised royalty collection program will provide the flexibility to adjust to reporting levels used by payors. Collecting royalty data at accounting levels used by payors will help to improve timeliness of collections, improve overall compliance, and may simplify collection of data for audits.

Integrated System - An integrated royalty collections system with a single source for data and common functions shared across functional areas should result from this project. System components must work together, sharing required information, to minimize data redundancy and increase processing efficiencies.

Structured and Maintainable - The royalty collections system should be developed using current technologies such as CASE products, client/server technology, and fourth generation languages to allow for more efficient system maintenance and adaptation to changing requirements.
II. Proposed Program Overview

Wyoming's proposed Federal royalty collections project will be designed to implement a more simplified, efficient Federal Royalty Collections Program to meet the needs of industry, the Federal government, and individual states, while avoiding unnecessary requirements and possible redundancies. Implementing such a program will require a well defined strategy to meet its goals. Re-engineering of royalty reporting, collection, and disbursement processes will be the first step toward the development of an overall strategy to simplify and improve efficiency in the Federal Royalty Collections Program.

The challenge to deliver systems that provide quantum gains in efficiency makes it imperative that information strategies are an integral part of an overall focus on the people, processes, and technology within an organizational structure. Stepping back and evaluating the royalty functions will likely result in dramatic changes in the way the program is conducted. Changes in industry marketing and accounting methods and antiquated reporting structures within the current MMS system have led to excessive costs associated with this function. New technologies can yield certain benefits when implemented without regard for re-engineering of processes, but the power of information can be exponentially enhanced when processes are streamlined, and people are skilled and empowered to succeed.

It is also necessary to recognize that this project will have a much greater chance of success if open and positive, cooperative participation by effected Wyoming agencies, other states, tribes, MMS, BLM, and industry is maintained. Any project with possible wide-sweeping changes require full cooperation from the entities involved. Therefore, it is crucial that proper communication and review procedures be implemented.
Scope of the Program

Several factors must be considered when determining the scope of the proposed program. While exact scope cannot be properly assessed at this time due to possible legislative, legal, or statutory mandates that may have impact, it is still necessary to define a scope for estimating effort and cost. The following describe the "expected scope" including functions to be delegated to the State of Wyoming, roles of the involved entities, organization structure, and information systems supporting the program.

Collection Functions to be Performed

Wyoming proposes to take responsibility for delegable functions associated with the collection of royalty payments on Federal lands within the boundaries of the State. These revenue-related activities include:

- **Payor Accounting**: Wyoming will process information establishing liabilities for each payor as related to identified reporting levels. This information, which includes sales volumes, sales values, royalty volumes, and royalty values, will be collected at a level that is easily accounted for by industry allowing simplified reporting and, therefore, improved compliance and auditability. Collections will occur at the payor level and will be reconciled with liabilities to allow efficient and timely billings or credits. It is anticipated that this information will be collected on a monthly basis in conjunction with the receipt of Wyoming severance taxes. Reporting and interface capabilities will be developed to properly support MMS and BLM requirements defined during the design.

- **Production Accounting**: In addition to the data reported for the payor accounting function, less frequent reporting may be required at a lower level of detail to allow cross-matching and allocation of revenue to individual leases. Reporting and interface capabilities will be developed to properly support MMS and BLM requirements defined during the design.

- **Revenue Distribution**: This activity will include determination of revenues associated with each involved entity and the distribution of these funds as required. Royalty receipts will be distributed at predetermined intervals with specific requirements defined during the design process. Distribution to the Federal government and State funds will be included.

- **Audit**: The State will continue with the responsibility for executing and conducting audits including those identified by MMS or BLM in accordance with current audit delegation of authority and the BLM referral program. Wyoming will continue to work in partnership with the Department of Interior and General Accounting Office on continued Federal enforcement actions.
Roles of Wyoming, MMS, and BLM

Definition of the respective roles of Wyoming and the MMS relative to the delegation of duties to be assumed by Wyoming can best be addressed from the operational perspective of what functions should continue to be centralized at the MMS versus those functions that should be delegated.

Matters involving policy formulation relative to what elements of a transaction are royalty bearing should continue to reside with the MMS Valuation Standards Branch. Matters involving the operational aspects of Federal royalty collections, reporting, and disbursement will be expected to reside with Wyoming. The activities of collection, disbursement, and accounting for on-shore Federal royalties represent activities which are a natural adjunct to functions already being performed by states, including Wyoming, in royalty and severance tax functions. Agreement will need to be obtained between the MMS and Wyoming as to information requirements which the Wyoming system would need to satisfy. This agreement would contain a clear and explicit understanding that the obligation to provide the required information does not equate to the implementation of a "mini MMS program or information system" at the state level.

MMS would continue to perform policy guidance services provided by the Valuation Standards Division. Other potential delegable functions such as Operational Processing and Transportation Allowance approval requests will stay with MMS but will be reported and registered with Wyoming to allow proper validation. MMS will continue to hear and adjudicate Interior Board of Land Appeals (IBLA) cases.

This proposal does not contemplate the assumption by the State of duties and responsibilities currently performed by either the Bureau of Land Management (BLM), Forest Service or Bureau of Indian Affairs (BIA). Accordingly, those functions relative to undeveloped leases currently residing with the BLM or Forest Service (Federal Leases), or BIA (Tribal and Allotted Leases) will continue to be performed by these respective agencies relative to Federal leases in Wyoming. The production monitoring functions currently being performed will continue to be BLM functions.
Organizational Structure

Wyoming is well aligned to perform the functions associated with royalty collections. For example, the Department of Revenue Mineral Tax Division currently processes severance taxes and ad valorem valuations for mineral production in the State and the Department of Audit performs tax as well as Federal royalty audits on mineral production and valuations. As a result, it would be a natural progression to implement an organization within the State of Wyoming with the responsibility to collect and process Federal royalty payments. The focus of the new organization could expand to encompass processing all extractive mineral product sources and types. Sources of revenue include oil, gas, coal, and other solid minerals, while types of revenue will include Federal Royalty, State Severance Tax and County Ad Valorem tax. Such an organization must incorporate a knowledge base sufficient to determine value for both Federal Royalty and State Severance Tax purposes. This organizational structure could facilitate single source remittance processing for taxpayers and royalty payors in the State, thereby reducing industry reporting and payment requirements.
Wyoming will undertake the primary responsibility for development and maintenance of the new Royalty Collections Information System. It is expected that MMS will have input in the design and development process but, Wyoming will ultimately be responsible for design decisions and implementation of the system. The system will provide appropriate accounting and data management to collect and account for revenues, and to collect, manage, and retrieve revenue and production information. Functions of the proposed royalty collections system are depicted in the following diagram.

As illustrated by the diagram, these functions will be designed to work together as a seamless, integrated system. A summary description of each function follows.

- **Registration**: Registration includes identification and establishment of the entities involved in the royalty collections process. Registration of items such as wells or mines, leases, payors, purchasers, and product codes will be performed and include set up of data related to each entity.

- **Data Capture**: During data capture, forms associated with processing royalty collections will be entered via manual data entry, magnetic media, or EDI technology. On-line, real time, edits will be performed to help identify user data entry errors or erroneous payor reporting.
• **Remittance Processing:** Processing of various types of payments such as wire transfers, cash receipts, payments to lock boxes, and checks must be performed in a timely manner with proper controls. This function processes remittance activities including deposit processing and verification.

• **Returns Processing:** Returns processing provides centralized transaction processing for each form/return. It edits and validates return transactions and suspends transactions for review and correction.

• **Financial Accounting:** Financial accounting posts transactions to payor accounts, calculates applicable penalty and interest charges, summarizes affected payor period records, and evaluates the summarized period in order to bill a royalty payor for any underpaid amounts or credit for overpayments.

• **Production Accounting:** Production accounting posts transactions associated with sales and production data of mineral properties such as wells, mines, leases, and units. This function also performs cross-checking between production and sales figures in the royalty collections system as well as comparisons of royalty production and sales figures against severance and ad valorem tax data.

• **Revenue Distribution:** Revenue distribution will generate reports and provide interfaces, where needed, for revenue disbursement allocations to various State funds and the Federal government. Distribution will be based on actual cash receipts, including adjustments for credits, refunds, insufficient funds, and payment adjustments.

• **Audit and Collections Support:** This function provides a tool to identify and collect from payors who are deficient in their royalty payment responsibilities. Audit and Collection Support works in conjunction with production and financial accounting to evaluate comparisons and identify potential audit candidates.

• **Management Reporting:** A number of management reports will be produced by the system. Reports will be produced on a scheduled and automatic basis. Additional features will allow ad hoc reporting capabilities.
III. Implementation Approach

This section describes the proposed project approach to implement the Federal Royalty Collections Program in Wyoming. Implementation of the Federal Royalty Collections Program in Wyoming will require approximately two years to ensure the current processes and reporting requirements are re-engineered and simplified and to allow sufficient time to design and implement an organization and information system capable of processing royalty payments. The following project time line depicts phases and tasks that will be performed during the project. Descriptions of each phase are contained on the following pages.

State of Wyoming
Federal Royalty Collections Program

Implementation Approach
Implementation Phases and Tasks

The project will be divided into several phases to facilitate restructuring of reporting requirements, design decisions and implementation. A phased approach will allow for review and approval of concepts and creation of legislative changes that may be required before proceeding with the establishment of an organization and the design and implementation of support information systems. The phased approach will allow for implementation costs to be refined as design decisions and reporting requirements are determined. This will increase reliability of estimated costs and work effort, thereby reducing risk and increasing the efficiencies gained by implementing the program in Wyoming. The following briefly summarizes each of the project phases:

Re-engineer Royalty Collections Process

Re-engineering the royalty collections process including reporting requirements will provide the basis for implementation of an organization and information system. Only by re-structuring and simplifying the program and by careful alignment of people, processes, and technology will efficiencies be realized.

During this phase of the project, the royalty collection process will be re-engineered including design of each of the functions delegable to the State. The project team will estimate the potential benefits of re-engineering these processes. Simplifying the reporting requirements will drive benefits exponentially. Substantial benefits can be gained by eliminating non-value added tasks and data reporting requirements and, through decreased data capture, data maintenance and overhead associated with the large amount of unnecessary data now maintained. A more streamlined program will increase the ability to verify compliance, conduct audits and provide better service to royalty payers. The following briefly describes the tasks that will be performed during the re-engineering phase.

- Establish Industry Committee: A mineral industry committee will be established to facilitate input from mineral companies. Policies, reporting requirements and electronic data interchange (EDI) will be some of the topics addressed by the industry committee.

- Review/Assess Alternative Reporting Structures: Reporting structures including reporting levels and procedures will be reviewed, alternatives developed and recommendations made.

- Assess State Impact and Integration: The impact to Wyoming and potential impact to other states will be analyzed. Integration with Wyoming’s revenue information systems will also be assessed.
Finalize Simplified Reporting and Policies: Reporting structure recommendations will be finalized. Ensuring simplified reporting structures will be a major goal of this task.

Identify State Organization Structure: Given the finalized reporting structure and policies, the organization requirements necessary to manage and operate the Federal Royalty Collections Program will be finalized. Specific personnel requirements will be determined and a detailed organization plan will be developed.

Hire Personnel: Initial program personnel will be hired to allow their participation throughout the design and implementation phases.

Draft Proposed Bills for Statutory Changes: As a result of the recommended reporting structure and finalized organization, proposed bills will be drafted and submitted for both Wyoming and Federal statutory changes.

Design System

The system design and implementation phases will include development and implementation of the information system necessary to process royalty payments. During the system design phase, information system requirements that were identified during the re-engineering phase will be finalized and system functional and technical specifications will be developed. A system prototype will be developed and reviewed to ensure the design is proceeding according to the requirements. A finalized installation schedule and cost/benefit analysis will be developed to enable executive management to make informed decisions regarding system implementation. In addition, key management checkpoints and quality assurance reviews will be conducted during the system design phase.

The design phase will produce a system prototype and design documents that will serve as the "blue print" of the information system. Appropriate time will be allocated to review the design with State of Wyoming, mineral industry and other personnel as required. Design revisions will be incorporated and the final design published before proceeding with the installation phase. The following briefly describes the tasks that will be performed during the design phase.

Design Forms and Reporting Structure: Forms required for reporting under the simplified program will be designed, reviewed and approved. Procedures for processing the forms will be designed.

Design System Functions: Information system functions required to process royalty registration, processing and management reporting will be designed. System data modeling will be performed and system inputs and outputs will be identified.

III-3
• **Prototype Functions:** A system prototype will be developed to demonstrate system functions. The prototype will be reviewed with State users and management. Changes will be made to the prototype, as required, until the system meets the requirements of the State.

• **Conduct Industry Meetings:** Industry meetings will be conducted on a regular basis to review the system design including the prototype. Input from the industry will assist in finalizing the design.

• **Finalize Design:** The design will be reviewed via the prototype and documentation. Changes will be made and reviewed by the State. Design tasks will proceed in an iterative fashion until the design is finalized.

• **Review and Approve Design:** Formal State approval will be obtained before proceeding with the installation phase.

**Install System**

System installation will include development of detailed system module specifications, coding and testing programs, system testing and conversion of the system to a production environment. In addition, supporting system documentation will be developed to facilitate system implementation and maintenance, user procedures will be developed and training materials prepared to facilitate transition to the new system. A comprehensive and thorough system test will be conducted with extensive user involvement and approval. The following briefly describes the tasks that will be performed during the installation phase.

• **Code and Test Functions:** Information system functions will be designed in detail, programmed, and tested to ensure compliance with the design.

• **Conduct System Testing:** Upon completion of the coding and testing of system functions, the entire system will be tested using a business testing approach. This will ensure the system will function as planned in a production environment.

• **Develop Procedures:** Detailed procedures will be developed for processing registration and royalty collections. The user procedures will include both the personnel and computer components necessary to accomplish a business procedure.

• **Train Users:** Training materials will be developed and system users will be trained prior to system conversion.

• **Conversion:** Conversion to production requires many preparatory tasks such as establishing royalty payor information, system parameter files and migrating system programs to the production platform. The system will be converted to production and processing will be initiated.

III-4
Implement Organization

Implementation of the organization will entail finalizing policies, procedures and personnel requirements including establishing position responsibilities. Additionally, this phase will include establishing the facility such as location and infrastructure (microcomputers, supplies, telephones, etc.) to support the program.

A key component of this phase will be the establishment of an organization mission statement, objectives, performance measurements and service level requirements. Managing the organization's performance against internally defined standards will help ensure the focus is on more efficient operations, compliance and royalty payor service.

Since the State will be implementing a new function including an information system, this phase will also include "change management" support to assist new personnel with assimilating the changes in information as well as the methods and procedures required to perform the royalty collections function. The following briefly describes the tasks that will be performed during the Implement Organization Phase.

- **Develop Policies and Procedures:** Royalty collections organization policies and procedures will be developed including the organization mission statement, objectives and guiding principles.

- **Establish Performance and Service Level Criteria and Measurement Methods:** Organization performance measurements will be established to ensure the focus is on providing a satisfactory level of service.

- **Finalize Personnel Requirements:** Personnel requirements developed during the re-engineering phase will finalized. This includes writing position descriptions and requirements.

- **Establish Facility:** The physical location for the Federal Royalty Collections Program organization will be acquired and refurbished as needed. Telephone, computer wiring and other infrastructure requirements will be installed.

- **Hire Personnel:** Available positions will be advertised, candidates interviewed and personnel hired.

- **Train Personnel:** Program training will be performed including training in areas such as management, information system and the Federal Royalty Collections Program.

- **Initiate Royalty Collection Program:** Upon completion of the previous phases and tasks, the Federal Royalty Collections Program will begin.
Project Oversight

Implementation of the Wyoming Federal Royalty Collections Program will be a very important task with significant financial implications for the State of Wyoming. As a result, the project team should consist of dedicated State of Wyoming personnel knowledgeable of the current federal mineral royalty program and who are familiar with Wyoming's management of public lands and Mineral Severance Tax Program.

Gaining mineral industry input and support will also be an important component during the project. As indicated in the first section of this document, a goal of the project will be to develop new procedures and reporting requirements that are more beneficial to both the State and the mineral industry. To this end, a mineral industry advisory committee should be established and meet on a regular basis to review and assist in determining reporting requirements and other program changes. The mineral industry should also assist with the design and implementation of electronic data interchange (EDI) technology to facilitate reporting.
IV. Cost Estimates

This section contains "broad-based cost estimates" for the State of Wyoming to implement and operate the Federal Royalty Collections Program. One-time and on-going (annual) organization and information system costs have been estimated. Costs were not estimated for MMS administration of functions that will not be processed by Wyoming. Costs for certain functions that do not directly relate to collection of Federal royalties (e.g. administration and processing of Indian or off-shore leases) or that the Federal government performs by its choice (e.g. Royalty-in-kind and associated processing) have not been estimated. Other functions may inherently be required as a result of Federal land ownership. These were not estimated because the costs could change dependent on the resolution of the re-engineering phase.

Summary Cost Estimates and Analysis

The following table depicts the estimated costs for implementing and operating the program in Wyoming.

<table>
<thead>
<tr>
<th>State of Wyoming</th>
<th>Federal Royalty Collections Program</th>
<th>Summary Cost Estimates</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>(Thousands)</td>
</tr>
<tr>
<td>Cost Category</td>
<td>Start-up Cost (First Two Years)</td>
<td>Annual Cost</td>
</tr>
<tr>
<td>Re-engineer Processes</td>
<td>$630</td>
<td>$0</td>
</tr>
<tr>
<td>Organization</td>
<td>$891</td>
<td>$750</td>
</tr>
<tr>
<td>Information System</td>
<td>$5,570</td>
<td>$650</td>
</tr>
<tr>
<td>Total</td>
<td>$7,091</td>
<td>$1,400</td>
</tr>
</tbody>
</table>

By calculating the 10 year estimated cost (not discounted) and comparing to the current MMS administration charges, the expected benefits to Wyoming and the Federal government are considerable. With the current level of administrative charges deducted from Wyoming's share estimated to be over $15 million annually, Wyoming could save an estimated $100 million over 10 years. This savings includes the cost to develop and operate the Federal Royalty Collections Program.
The estimated cost for the proposed Wyoming program includes development and implementation costs incurred plus the estimated Federal net receipt sharing deduction for the two years during which the Wyoming program is being developed. The Wyoming program estimates do not include Federal costs after the Wyoming program goes into operation.
When comparing estimated costs to operate the Federal Royalty Collections Program in Wyoming to the current costs reported by MMS and the current net receipt sharing deduction allocated to Wyoming, the differences are significant. The chart on the facing page shows the estimated cost to collect $1,000 of revenue utilizing the proposed Federal Royalty Collections Program in Wyoming as compared to the cost currently reported by MMS and the net receipt sharing deduction charged Wyoming. Additionally, the current cost reported by the Internal Revenue Service (IRS) and Wyoming Mineral Severance Tax Program are shown to provide a comparison with other revenue collection program costs. After the Federal Royalty Collections Program is implemented (first two years) the estimated cost to operate the program in Wyoming is $7 per $1,000 collected. This compares with the current cost reported by MMS of nearly $59 per $1,000 and the net receipt sharing deduction charged against Wyoming's royalties of $77 per $1,000.

The remaining portions of this section describe the components of each cost category for development, implementation and operation of the Federal Royalty Collections Program in Wyoming.

**Re-engineer Processes**

The first phase of the implementation project will be to re-engineer the processes and reporting requirements for the Federal Royalty Collections Program. Appropriate time and effort should be devoted to ensure processes and reporting requirements are analyzed in depth. The cost to perform the re-engineering phase is estimated to be $630,000.

**Organization Costs**

Organization costs include costs associated with managing and operating the Federal Royalty Collections Program in the State of Wyoming. Both start-up and on-going costs were estimated.

*Initial Organization Costs*

Initial or start-up organization costs include establishing organization mission, objectives, performance measurements and service level criteria as well as personnel hiring and training. Organization costs also include the cost for State personnel dedicated to the project. Since additional State personnel would be hired to manage the Federal Royalty Collections Program, it is suggested that at least two persons be hired at the beginning to participate throughout the project.

It is estimated that initial organization costs will be $890,600 during the two year project.

- Implementation Project (two year cost)
  - Staff Participation $546,800
  - Project equipment and supplies $218,800

- Additional support services - first year $125,000
**On-going (Annual) Organization Costs**

On-going organization costs include payroll, supplies and support costs for the Federal Royalty Collections Program, and additional personnel required for fiscal control and information system support. The on-going organization costs are estimated to be $750,000 annually.

- Royalty Collections Staff $500,000
- Fiscal Support Staff $62,500
- Information Technology Support Staff $62,500
- Equipment and Supplies $125,000

**Information System Costs**

Information system costs include design, development and on-going costs to provide an information system capable of processing Federal royalty payments including accurate account maintenance, distribution, and automated audit reporting.

**Information System Design and Development Costs**

The cost to design, develop and implement a Federal royalty collections information system for the State of Wyoming is estimated to be $5,570,000 as follows:

- Implement Information System $1,130,000
  - Registration Function $925,000
  - Data Capture Function $3,305,000
- Hardware and System Software Upgrades $210,000

**On-going (Annual) Information System Costs**

On-going information system costs include the cost to operate the information system including system operators, technical support, and data and system security. Additionally, on-going information system costs include standard system maintenance. Estimated on-going information system costs are $650,000 annually.
Assumptions

The estimates contained in this document assume Federal royalty collections processes and data reporting requirements will be re-engineered. Only by re-engineering processes and reporting requirements can simplification and efficiencies occur. Re-automating the existing processes and reporting requirements would cost considerably more and achieve minimal benefits.

The estimates assume implementation of the Federal Royalty Collections Program as defined in the program description and implementation approach sections of this document. Additionally, the implementation assumes that the State of Wyoming with input from royalty payors would serve as the oversight body for the project. MMS or any other Federal agency approvals of issues such as reporting requirements, processes and system design is not assumed and if included would increase the effort and cost considerably.

The cost estimates include project related services for State and contractor personnel but do not include the cost for new hardware or system software. It is assumed that existing Wyoming hardware and software will be used at an upgrade cost of $210,000.
Mr. Dewey. BLM is doing all of these other things. It would certainly seem to us that that is not appropriate to be included in the charge. We've focused pretty heavily on the MMS side of it, and we just feel that most everything that Mr. Fry has said earlier that they have to do, we do as well.

We keep track of all those things that he mentioned. Some of them we don't keep track of as frequently, and some of them we keep track of on an accounting basis that is the accounting of the payer, whereas they make the payer disaggregate everything down in the lease base.

I can tell you that when you go into an accounting operation of an oil and gas company and make them disaggregate, that's going to be one of the great creators of errors that they wind up having spent a lot of time with.

I don't find any real value in the disaggregation. Some of that is imposed by you folks.

There is another issue here. In the audit function, we do what we call a risk-based analysis. We have limited dollars that we can spend. Much as my legislature likes what we do, they don't give me all the dollars that I would like to have.

So we put our dollars where they pay off, and we look for expenditures that are going to bring us the greatest return. Some of what MMS does, and again some of it is imposed upon them, costs more than it brings in return.

I think that's a piece of it. In our testimony, in our proposal, we have said, you have got to let us do it in a reasonable way, not by the rules as they are in place today.

That's a long disorganized attempt to respond to your question. Mr. Lehman. That's fine.

Before I turn it over to Mr. Thomas, let me ask one other question.

You have advocated a pilot program, and I assume Wyoming would be the pilot.

Mr. Dewey. We are prepared. We would support the program, even if it were in another State.

Mr. Lehman. How would you want to fund that program?

Mr. Dewey. I think it ought to be funded out of royalties before the sharing. In other words, it winds up being partly a cost of the Federal Government, partly a cost to the State.

I'll be very frank with you as to why. It isn't an unwillingness on our part to put out dollars. I just don't personally want to be in the process of negotiating a project, approval by two legislatures, one in Cheyenne and one in Washington. There's no way to get out of working with you folks, so I'd like to eliminate our legislature.

Mr. Lehman. And you're prepared to meet the financial standard required by OMB and the Congress and GAO?

Mr. Dewey. Yes, sir.

Mr. Lehman. Thank you.

Mr. Thomas?

Mr. Thomas. Thank you, Mr. Chairman.

Thank all of you for your testimony.

Let me ask, Roger, in the beginning, do you collect royalties on the same production that MMS does?
Mr. DEWEY. Congressman, we collect it on the same production and more. Earl and I were talking earlier today. We have roughly 900 severance taxpayers. Roughly 500 of those are the same people who are paying lease on the fees production.

Mr. THOMAS. So all of the production on federal lands is taxed on a severance basis, and the State collects it that way.

Mr. Fry, what do you think the completeness of your collection is? What percentage of what is due is collected, do you know?

Mr. FRY. No, sir. I don't have the answer to that. I think because we are catching so many dollars in the audit process, it indicates to me that we're probably not collecting everything that's out there. Because when you get to the audit process, you're not looking at every transaction, you're looking at systemic problems.

So I'm not convinced that, as of this date, we're collecting all the dollars that are out there.

Mr. THOMAS. Do you have any sort of an arrangement on this barrel of oil that's produced, what was paid to the State? It seems to me the area that is important is the production. It's pretty easy to levy the royalty on the production, and when you've nailed that down, do you cross-check with others who are dealing with the same oil?

Mr. FRY. Yes, that's one of the requirements. I think it's a good idea, but it's also one of the requirements that was put on this program by the Congress. And we're spending about 6 percent of our collection dollars on this kind of production reporting, royalty reporting comparison.

That's something that has only come into being in the last several years or so. It took a lot of work to bring that up on the computers, but now we are doing that.

Mr. THOMAS. I'm not an auditor, nor am I familiar with it, but it doesn't seem like it's a task of discovery. The stuff's out there. It isn't too hard to know what production is. There's lots of sources to find out.

Roger, is the State doing some auditing now?

Mr. DEWEY. Yes. The State did not audit severance taxes until 4 years ago. And with a completely unaudited program, I was trying to scramble, because I knew you were going to ask me the question, what percentage do we collect.

And that's a pretty difficult question for either one of us to answer. But I can tell you that we are just wrapping up audits of years in which the taxpayers did not expect to be audited.

So if there were going to be games playing, those are the years; and the findings we have brought in over a 10-year period would be just about 10 percent.

I would anticipate that now that we are in an era where they are making their payments expecting to be audited, that that percentage would probably drop significantly.

Mr. THOMAS. Does the State do auditing with the Feds?

Mr. DEWEY. Yes, we do audit under a contract arrangement with the MMS. We do royalty audits.

Mr. THOMAS. How long has that been going on?

Mr. DEWEY. Approximately 12 years.

Mr. THOMAS. It was initiated, I believe, by Jim Griffith in the Auditing Department of Wyoming?
Mr. DEWEY. Jim Griffith.

Mr. THOMAS. So we've been doing some of that.

I won't take a lot of time on questions. I think the significant issue before us is whether or not we are willing to look at something and try something, as opposed to what I've perceived over the last several years as some kind of a turf protection situation.

It's interesting that you're reinventing Government this year when you got a prize last year for being an outstanding operating group.

Mr. FRY. We always want to try to improve. [Laughter.]

Mr. LEHMAN. That's the right answer.

Mr. THOMAS. Well, let me ask a couple more questions.

Some of us were a little surprised at that. Tell me a little bit about the BLM thing.

Now the BLM, out of these funds, you said over $71 million. How does that fit into your budget? Is that on top of what you already get? Is that part of the budget that's put out by the Appropriations Committee?

I guess my bottom line is, what incentives do you have to make that less, or do you just send the number over?

Mr. HILDEBEIDEL. Mr. Thomas, generally, we just supply the number to MMS and it reflects that portion of the budget that we get through the appropriations process that is devoted to the mineral leasing programs on federal land; oil and gas, coal and other leasable minerals. We deduct from that Indian land work. We're not including Indian land work, and we're not including any activity related to minerals that are not subject to the Mineral Leasing Act.

So if the fund is within our budget, then we supply that number to MMS and that becomes part of the overall calculation.

Mr. THOMAS. I guess I'm searching for some kind of an incentive—I don't know what it is—to do it for less, be more efficient. What is the incentive to do that?

Mr. HILDEBEIDEL. Well, sir, I don't know that I can answer that directly. I think what we're trying to do is comply with the laws and regulations that we have to deal with.

Like I said, BLM is not in the royalty collecting business, we're in the leasing business and mineral supervision and the inspection and enforcement business. And we've been told by the Congress and by others that we need to do those in a certain way and be very thorough.

Mr. THOMAS. You're basically in the land management business, are you?

Mr. HILDEBEIDEL. That's correct.

Mr. THOMAS. And this does not stand alone. Your guy goes out there to look at a number of things. He's not doing one thing alone, right?

Mr. HILDEBEIDEL. That's correct.

Mr. THOMAS. However, you don't budget that way. You budget by minerals and you budget by grants.

Mr. HILDEBEIDEL. We'd love to budget on a broader basis.

Mr. THOMAS. Yes, really. It's really kind of a mess the way it is now, as I understand it from our local folks. And they can't set any priorities really. And you're kind of like the Forest Service. You
work 5 years on a plan and then get a line item budget that may or may not even fit.

Mr. HILDEBEIDEL. Absolutely.
Mr. THOMAS. Bad news.
One more question, Mr. Fry.

You said you think there are some different things that constitute the comparison between $5 and $60, and I understand that may be so.

What if you made it $30 and $5? Isn't that still quite a difference?

Mr. FRY. Absolutely. And until we can resolve the apples and oranges question, I'd hesitate to testify as to where we are. I'm sure that we're probably spending right now more dollars than the State spends on the same apples. And I want to surround that question as quickly as we can.

Mr. THOMAS. You separate onshore and offshore completely?
Mr. FRY. Yes, we do. So there are no offshore dollars included in these figures that we charge to the States.

Mr. THOMAS. Did you get your new computer system in Colorado?
Mr. FRY. Yes. We've got two we're working on; one's for the offshore.

Mr. THOMAS. Wonderful. Thank you very much. I appreciate it.
Mr. LEHMAN. Thank you.
Mr. ALLARD. On your auditing process, do the States do their audits and then you do your audits on top of theirs?
Mr. FRY. No. For the federal leases, in many cases, we have cooperative agreements with the States, and they really become a part of a team which consists of the State and the federal audit process. It's one audit.

In the case of Wyoming, by way of example, they have entered into an audit agreement, and they do the auditing for the federal leases for, shall we say, the Federal Government in their area.

And we do not do a second audit.

Mr. ALLARD. And you go in as a team, both made up of state personnel as well as federal personnel?
Mr. FRY. I think the State personnel go in. I think that's correct.
Mr. ALLARD. So we don't have a duplication of auditing there?
Mr. FRY. No. Basically, we contract the work out to the State.
Mr. ALLARD. Thank you very much.
I don't have a lot of questions.
Mr. THOMAS. If the gentleman would yield, I think that's a good point.

And I understand your reluctance, sometimes, to contract. But we've contracted that for a very long time. That's a very integrated part of the whole thing.

And we've turned that over to the State, and you have a way of seeing whether the State does it properly or not.

And I think, basically, that's one of the arguments that we make. There are other things that could be done similarly.

Mr. FRY. And we're most pleased with that program.

You asked a question, about BLM, and there are some of the Indian tribes who are now doing production verification.
However, there are no States who have entered into cooperative agreements to do production verification. So that when you're talking about the incentive question or whether or not BLM is doing it, there is a question as to whether the States want to be involved in that process. We encourage it. We'll be happy to work with the States to try to enter into those kind of cooperative agreements.

Mr. THOMAS. My question on incentives, of course, is that if the State does this, where there's a twist on the part of the legislature and the governor who, by the way, in Wyoming, has been very helpful in this matter and very positive about it. They have an incentive. Old Roger's tail gets twisted to get as many dollars as he can, and that's good.

You may not like it, Roger, but it's a good thing. I believe Mr. Kabeiseman has a comment.

Mr. LEHMAN. Certainly, proceed.

Mr. KABEISEMAN. I'd just like to make a comment in response to Mr. Fry's comments about where the $60 and the $5 come from, and we're supposedly comparing apples and oranges. I would disagree with that, in that I copied down some of the functions that he does. And we do similar functions. We do them on the severance tax basis, and then we certify those down to our counties to collect the ad valorem taxes.

We have about 950 taxpayers that pay on a monthly basis. Last year, we collected about $260 million. We do that with 18 people. We do the document processing. We do the document corrections. We maintain databases on leases also. We do the verification.

Roger does the audit in his department and we make distributions also, whereas the MMS shares their royalties with us, we share it with political subdivisions and other entities.

We can do it, and when we put our costs together, we have the $5 costs.

I don't think it's apples and oranges; I think it's apples and apples. We probably tend to do it better. We're doing it cheaper, and we're doing it more effectively.

Mr. Fry is hoping to reinvent Government. I think in Wyoming, given budget constraints and probably the legislature has a little bit better control on us—Mr. Thomas called it tail twisting—but I think while you're trying to reinvent Government, we've probably reinvented it in Wyoming.

And these costs are apples and apples. We're doing it cheaper and we're doing it more efficiently.

Mr. LEHMAN. I don't know if there's any other comments here. But let me hold the record open for a couple of weeks.

The Committee is going to continue to look at this. We think the concerns expressed here are real and the Western Governors brought it to my attention, as well, so it's not just simply Wyoming and Mr. Thomas.

We're aware of the opportunity here with the new Administration looking at the operations, and they're using this perhaps as a model. I hope something good can come from that.

And we're also aware of our own role and this problem here in Congress, as we put out numbers in the budget, and we're doing
it right now, we're doing it in this room just shortly before you got here in the conference committee.

Often, the Members just sit there, and those of us who crank them in don't really know what the effect of them is out there, what we're telling you that you've got to do that may not make any sense at all, in order to come up with that.

So I think there's room for a lot more discipline on our part in this process as well.

Thank each of you for being here today.

We appreciate it very much, and we'll look forward to working together.

Thank you.

[Whereupon, at 2:30 p.m., Thursday, July 29, 1993, the Committee was adjourned, subject to call of the Chair.]