MINERAL ROYALTY MANAGEMENT

HEARING

BEFORE THE

SUBCOMMITTEE ON ENERGY AND MINERAL RESOURCES

OF THE

COMMITTEE ON RESOURCES HOUSE OF REPRESENTATIVES

ONE HUNDRED FOURTH CONGRESS

FIRST SESSION

ON

REVIEW OF ADMINISTRATION'S PROPOSAL REGARDING MANAGEMENT OF ONSHORE FEDERAL MINERAL LEASING TASKS AND CONSIDERATION OF BLM'S OIL AND GAS PERFORMANCE REVIEW DRAFT PROPOSALS

JUNE 8, 1995—WASHINGTON, DC

Serial No. 104–26

Printed for the use of the Committee on Resources

U.S. GOVERNMENT PRINTING OFFICE

93–198 CC WASHINGTON : 1995

For sale by the U.S. Government Printing Office
Superintendent of Documents, Congressional Sales Office, Washington, DC 20402
ISBN 0-16-047699-2

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MINERAL ROYALTY MANAGEMENT

Thursday, June 8, 1995

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

The subcommittee met, pursuant to call, at 2:05 p.m., in room 1334, Longworth House Office Building, Hon. Ken Calvert [chairman of the subcommittee] presiding.

STATEMENT OF HON. KEN CALVERT, A U.S. REPRESENTATIVE FROM CALIFORNIA, AND CHAIRMAN, SUBCOMMITTEE ON ENERGY AND MINERAL RESOURCES

Mr. CALVERT. The Subcommittee on Energy and Mineral Resources come to order. The subcommittee meets today to review the Administration's proposal for "reinventing government, specifically those ideas outlined in late March by Secretary Babbitt regarding management of onshore Federal mineral leasing tasks conducted by the Minerals Management Service and the Bureau of Land Management.

Further, the Subcommittee will consider the BLM's Oil and Gas Performance Review draft proposals released by the Department of the Interior in April. The proposal to sell the revenue stream of offshore oil and gas leases is not a topic we will examine today, but the Subcommittee will review that and other Outer Continental Shelf leasing issues in the near future.

Also, today we will focus on States but not on impacts to Indian tribes. The Subcommittee is attempting to schedule a joint hearing with our sister Subcommittee on Native American and Insular Affairs to address how Indian tribes and allottees would be affected.

Over two months has passed since the Secretary of the Interior went public with his Department's ideas to "reinvent the government." Many an eyebrow was lifted in response to the suggestion of turning over the collection of onshore Federal leasing royalties to the affected States, wrapped in the rather cryptic term of "devolution of the MMS," and to let these States perform BLM's inspection and enforcement functions on oil and gas leases as well.

Reaction was mixed, at best. Some said the proposals were "provocative." Well, they said simply that they were somewhat less than provocative, and began to plot a strategy to ensure that they would not be implemented. The latter group may include a subset of the Department of the Interior.

However, at the outset, I want to praise the Secretary of the Interior for coming forward with these proposals. The devolution of the Minerals Management Service is among the boldest of the REGO II proposals I have seen in the entire executive branch. Secretary Babbitt deserves credit for putting it out there for all to see and comment on.

Cynics may question his true intentions (and do), but I believe the value of the devolution process is that this Administration has invited a dialog with Congress, States and the Indian tribes into the proper role—if any—for Federal Government management of lands and mineral resources.

Mr. Babbitt opened Pandora's Box on March 29 and there simply is no way of closing the lid back and sustaining the status quo. Does that "box" contain the path to transfer of the Federal mineral estate to the States or merely a larger role for the State and local governments in management decisions about the disposition of those minerals?

This remains to be seen, but clearly, the negotiations have begun. That is what we begin today and will continue in the weeks and months ahead. The Subcommittee is committed to serious inquiry into the way the Feds do business with mineral rights owned by the American taxpayers.

I urge all the witnesses today to speak their minds. Don't be timid about criticizing the status quo. From the viewpoint of the Chairman there appears to be plenty of room for improvement in government and this Congress is ready to witness the budget resolution process that we are having today.

Mr. ABERCROMBIE. I was reading it right up to that point.

Mr. CALVERT. Last February, the Subcommittee held hearings on the budget justifications for the Interior Department agencies under our jurisdiction. I said then that the public expected and demanded a smaller Federal Government, as manifested by the results of the November elections. I certainly believe that this still holds true and these provisions before us today which were not reflected in the President's Fiscal Year 1996 budget request, it appears that the Administration now at least partially agrees.

We will fight over the details, no doubt, for example, just what are "inherently Federal functions," but the message is clear, let us find a way to do business more efficiently and with better results.

Before I turn to the other members of the Subcommittee for any opening statements, let me welcome our witness from near and far. Today's Interior Department witness was going to be Bob Armstrong, but he has been taken ill. I understand he is doing better. His deputy, Ms. Sylvia Baca, will present the oral testimony accompanied by two assistants. Bob has testified at length before this panel in the past and we certainly wish him well in his recovery, and the record will note that it takes three people to replace him.

I would like to thank our State government witnesses and affected industry witnesses for traveling here to be with us today and rearranging your schedules after the postponement from the earlier date scheduled. Unfortunately, neither the Governor of California, Governor Pete Wilson, nor his Director of the Department of Conservation, Mr. Michael Byrne, could be here with us today as planned, but a written statement from Mr. Byrne will be placed in the record.

[At press time, Mr. Byrne's statement had not been received for the record.]

Next, I would like to say aloha to our Subcommittee ranking member, Mr. Abercrombie from Hawaii and he is recognized for his opening statement.

STATEMENT OF HON. NEIL ABERCROMBIE, A U.S. REPRESENTATIVE FROM HAWAII

Mr. ABERCROMBIE.

Thank you, Mr. Chairman. I think you have covered all the ground. I have no opening statement except for my little demurrer there about the budget. I agree that you have covered everything that needs to be said for the moment and I look forward to the witnesses' testimony and our questioning and observation time.

Mr. CALVERT. Thank you. And first I would like to recognize Ms. Sylvia Baca, Deputy Assistant Secretary for Land and Minerals.

STATEMENT OF SYLVIA BACA, DEPUTY ASSISTANT SECRETARY, LAND AND MINERALS MANAGEMENT, DEPARTMENT OF THE INTERIOR; ACCOMPANIED BY CAROLITA KALLAUR AND WALT ROSENBUSCH

Ms. BACA. Thank you, Mr. Chairman, members of the Subcommittee. I would like to begin first by introducing to my right, the Acting Deputy Director for the Minerals Management Service, Ms. Carolita Kallaur, and to my left, Walt Rosenbusch, who is a special assistant to Assistant Secretary, Bob Armstrong.

Mr. Chairman and members of the Subcommittee, thank you for the opportunity to appear before you to testify on management alternatives for the Bureau of Land Management and the Minerals Management Service with regard to mineral leasing, operation and royalty management. I understand that the emphasis of today's hearing pertains to management alternatives with respect to onshore minerals. Accordingly, I will focus my remarks in that area.

This hearing, and the issue it is intended to address, is a timely one. There is general agreement that the old ways of conducting the public's business through the Federal Government programs must be thoroughly analyzed, reinvented, and in some cases abandoned. We cannot and we should not be content to rely on the practices of the past to work in the 21st century. Furthermore, the general public has indicated its desire to see a government that is responsive, and yet leaner.

Given our desire to respond to changing needs and legitimate requests of the public we serve, both the Department and the Administration have embarked upon an unprecedented effort to restructure government. Recently, under the Administration's REGO II effort, the Department proposed significant shifts in several of the programs under its purview representing the Department's best assessment of how to perform its core missions.

Our goal is to obtain as much savings as possible, while ensuring effective programs. With those general remarks as background, I would like to now turn to the subject of today's hearings. My remarks will focus on REGO II proposals for the Minerals Management Service and for the Bureau of Land Management.

On March 27, 1995, the President proposed the elimination of the Minerals Management Service as part of the National Performance Review Phase II. The proposal to eliminate the MMS was based on the belief that some functions can be performed efficiently at the State and tribal levels. Specifically, the REGO II proposal recommends that the royalty collection program for onshore Federal lands be transferred to the States and on Indian lands, to the tribes.

The responsibility to be transferred would include all royalty collection functions except those that are inherently Federal such as enforcement of lease terms, issuing final policy and regulations, determining the value for royalty purposes, and adjudicating appeals. It should be emphasized that the MMS proposal is a proposal to consult regarding the elimination of MMS.

The proposal is just that, a proposal. It is a beginning of a consultive process. While the Department proposed a specific scenario with associated cost savings to devolve royalty management-related functions, it is also cognizant that States, tribes, and other affected parties may recommend a different approach. We are open to discussing different approaches if they achieve an equivalent level of cost savings.

At this time, we are in the process of undertaking extensive consultation with affected parties. Specifically, we have sent the devolution proposal to the Governor of each State receiving revenue from Federal mineral leases and to tribal leaders and Indian allottee associations with mineral leases. We are also seeking input from industry. We will be able to put more specifics to the proposal after we have consulted and reviewed the views and ideas of all the affected parties.

We plan to meet with representatives of the interested States, tribes, allottee associations and industries in July in order to provide more information about our proposal, to respond to initial comments, to explain our process for future consultation and to discuss any other alternatives.

Even before the Department announced this devolution proposal, the MMS was committed to reducing the cost of collecting royalties.

As part of the National Performance Review—Phase I, the MMS is undertaking several initiatives to improve on the way it conducts the public's business and is committed to continual improvement. Recent examples of MMS initiatives are the establishment of the Federal Gas Valuation Negotiated Rulemaking Committee to develop improved and simplified methods for valuing natural gas.

Also, the establishment of the Indian Valuation Negotiated Rulemaking Committee to reach consensus on valuation method and royalty collection procedures that benefit the MMS, Indians, and industry. And, finally, a Royalty Gas Marketing Pilot program that looks for streamlining and simplified ways for royalty collection processes by taking Federal royalty share in kind.

We are also interested in being fair to industry, and we have tried to improve on the timeliness of our compliance reviews. We perform contemporaneous audits to engage royalty payers and to complete audits within a six-year period.

I would now like to outline the BLM proposals contained in REGO II. The BLM REGO II plan proposes the transfer of certain oil and gas inspection responsibilities to the States and native American tribes and cost recovery for pre-lease and post-lease energy minerals programs.

Like the MMS, the BLM proposal also calls for consultation with the affected parties. REGO II proposes that the BLM transfers certain oil and gas inspection and enforcement responsibilities regarding product verification and service compliance in the onshore oil and gas program to individual States and native American tribes. This proposal will eliminate duplication of efforts by State and Federal Governments and promote tribal government involvement in the management of their oil and gas resources.

The BLM is forming a consulting Task Force consisting of State, tribes and Federal representatives to establish the initial ground rules surrounding the proposed transfer to the States and tribes. The BLM would not require legislation to implement this proposal. Currently, authority exists to delegate the inspection and enforcement program to the States.

Tribes are eligible to contract for programs through the Indian Self-Determination Act and the Tribal Self Governance Act of 1994. Currently, there is no mandate for either the States or the tribes to accept this responsibility. REGO II also proposes cost recovery for pre-lease and post-lease programs. Extensive pre-leasing activity is necessary for oil and gas operations. These activities include analysis required by the National Environmental Policy Act.

Individual leases may require environmental analyses and land use planning decisions informing the agencies and the public of potential effects of the proposed leasing action on the environment. The BLM currently recovers some costs under some circumstances. Under the REGO II pre-leasing proposal, the BLM will analyze and identify the costs necessary to perform these analyses, and will seek to recover those costs from the industries benefiting from these leasing actions.

The reinvention measures are designed to reduce dependency on appropriated moneys for processing land use authorizations. The cost recovery for NEPA compliance will be significant. Our REGO II proposal estimates that the BLM spends approximately $6,000,000 on pre-lease NEPA compliance. Post-lease NEPA compliance is substantially less, as the pre-lease work generally provides the basis for the post-lease analysis.

Due to current legislative authorities, the team does not foresee the need for legislation in this area. The team expects to re-engineer the existing cost recovery processes by regulatory and internal directive changes. Even before the Administration and the Department of the Interior announced the REGO II proposals, the BLM also was committed to identifying ways to improve the management of the public resources and providing improved services to all of its stakeholders.

The BLM Performance Review was initiated in late 1993 to review oil and gas program operations, regulations and policies, and to identify opportunities to improve the way BLM provides service to its customers. The review culminated in the establishment of issue resolution teams and process review teams comprised of BLM staff and personnel from other Federal agencies.

In conclusion, as we look at the proposals for MMS and BLM, it is important to keep in mind that the concept of transferring functions was discussed by States prior to this Administration. This Administration has now joined in the dialog with the REGO II proposal. This proposal is just that, a proposal to consult with the States, tribes and industry on how and whether the transfer of these functions should occur.

Finally, we will keep the Congress informed of our consultation process with the States, with the tribes, and with industry. Both REGO II and the streamlining initiatives discussed today are being pursued by BLM and MMS in a manner which includes the American people. The goal is to make these programs more efficient by improving the way we do business while still maintaining the health of the land.

We are working to ensure the timely collection and distribution of mineral revenues to the States, to the tribes, the allottees and to the U.S. Treasury. We want to reduce any unnecessary paperwork or duplication. We will strive to ensure continuous public and industry participation in finding improvements to the way we do business. Mr. Chairman, this concludes my testimony. I will be glad to answer any questions. Thank you.

[The prepared statement of Sylvia Baca can be found at the end of the hearing.]

Mr. CALVERT. Thank you, Ms. Baca. By proposing to give States limited responsibility for royalty accounting and inspections, the Department has opened the dialog about the appropriate role of the States in managing all Federal mineral activities, if not outright title to the mineral interests contained within their own State. From reading testimony provided for this hearing, I understand the Department did not consult with States or industry prior to releasing the REGO II proposals.

Given the Department is planning to initiate a consultation plan, is the Department going to seriously consider alternative recommendations from States and industry that are beyond the limited responsibility of royalty accounting and inspections such as possibly giving the States authority to manage all mineral activities and further convene the mineral interest?

Second, the Department's MMS devolution proposal suggests that you will talk to States and industry about refining the proposal. What will the process be for reconciling differences between the Department's REGO II proposals and alternatives endorsed by industry and States? Will you submit for the record a schedule and plan that will address all proposals and comments from the States and industries? That is a pretty long question.

Ms. BACA. Mr. Chairman, with regard to the first question on the resources themselves, I believe when this proposal was put together, the thought behind it was that the States have a direct financial interest in the efficient collection of royalty receipts because they are entitled to half of the revenues under the law. Because some States have argued in the past that they can do a better job of royalty collection than MMS, we thought that it was probably worthwhile to explore those ideas.

On the other hand, I believe the Administration's thought is that the public land and the resources themselves belong to all Americans, whether they reside in Virginia or in New Mexico. It is the Department of the Interior's responsibility as stewards of those resources to assure that they are managed for the benefit of all Americans. I believe that disposal of those resources to the States is not on the table with regard to this proposal.

Mr. CALVERT. The second part of that question, what will be the process for reconciling differences between the Department's REGO II proposal and alternatives endorsed by industry and States?

Ms. BACA. I believe that we are interested in having an open dialog. Therefore, all alternatives will be seriously looked at, and I think that we just have to wait until July until we know exactly what it is that they are proposing before we can seriously consider any of those alternatives.

Mr. CALVERT. And you will stay in contact with this committee. Could you give us a schedule of our plan and any proposals and comments that you receive from the States and industry as you receive them?

Ms. BACA. Absolutely. We will keep Congress informed of our consultation efforts with any of these entities.

Mr. CALVERT. The Administration has claimed specific cost savings associated with the proposals as part of the tax cut that has been proposed. How flexible will the Department be in its consultation process with industry and States, and will the Department step back from your publicly announced cost savings?

Ms. BACA. Mr. Chairman, in terms of the cost savings, I believe what we are really interested in is just maximizing as much as we can from the cost savings. When we put out the proposal, the analysis was done in such a quick fashion that a thorough analysis was not conducted. I believe that once we get back the comments and once we are able to negotiate some sort of a proposal, we will put the finishing touches on it, and we will be able to tell more exactly what those cost savings are. Again, we are just looking to find the cost savings that might occur from these.

Mr. CALVERT. The proposal to transfer mineral activities to States seems to sometimes hide behind a shield of inherently Federal functions and gives the States no authority to decide how best to manage the transferred operation. Will the Department work on developing legislative options that will allow States to administer critical royalty functions such as value determinations, enforcement, and policy establishment?

Ms. BACA. Mr. Chairman, with regards to the inherently Federal functions, we have been operating off the basis of the legal opinion that stated that anything that required the exercise of judgment, anything that required setting policy or regulations or adjudicating any sorts of claims were the responsibility of the Federal Government.

I do believe, however, though that once a proposal is on the table that we can go back and look at some of those things that I just mentioned and look for some flexibility. Right now, not knowing what a specific proposal is, we cannot say that we can turn over those sorts of functions. Our solicitor's opinion just does not allow us to do that.

However, we have been told that once we do have a proposal and we have the ink dry, we can look at it and see if there is any room for flexibility.

Mr. CALVERT. Could you please provide a copy of the solicitor's opinion for the hearing record?

Ms. BACA. Yes, we will.

Mr. CALVERT. I appreciate that. Mr. Abercrombie.

Mr. ABERCROMBIE. Ms. Baca, I do not understand why you are here. I mean it. I do not understand why this proposal is here. I do not understand. It does not make any sense that I can see. Why on earth would you come here before you even talked to the States or the tribes? It sounds to me like you are here six months or a year before you should be.

Now if the idea is that you want to reinvent government and—it looks like we are going to have a vote coming up. Maybe we are not. Anyway, talking about what is inherently Federal in your own testimony. Enforcement of the lease terms. Well, probably one of the lease terms is collecting royalties. I mean are you going to enforce it or are the States going to enforce it?

Issuing final policy and regulations. I do not have a clue what that means. I presume some of the regulations is determining, for example, who is going to monitor the amount of minerals that are extracted and what precisely will be subject to royalty and what won't, determining the value for royalty purposes. Adjudicating appeals, that is an interesting one. You say that that is inherently a Federal process.

If you get in an argument or the State gets in an argument about the method of payment or whether it is being lived up to. I understand that there is some argument right now in the Department about whether or not present royalties are being collected up to the amount that they are supposed to be.

If you take the logic of this a bit further and you go to the Indian lands, why shouldn't the Indian tribes be in charge completely if you take the logic of this out, not only the royalties but give everything over to the tribes. I would be open to discussing that. You say the transfer of royalty collection process to the tribes would be accompanied by compacting the royalty functions.

It seems to me, as I said, that the logic of that is you turn the whole thing over to the tribes. I do not understand what you are trying to accomplish here. Why should the States constantly want to take this over? Are they going to hire people to do this and they pay for it or are you going to contract with the States?

Ms. BACA. Mr. Abercrombie, the answer to that question is that we do not know. We do not know whether we are going to contract or whether they are going to take it over. We are waiting for some dialog to occur with the States.

Mr. ABERCROMBIE. Then why are you going ahead with it now? What is the object?

Ms. BACA. We have a proposal on the table and it is there as a starting point.

Mr. ABERCROMBIE. But why?

Ms. BACA. Because we were asked to look for cost savings within our Department.

Mr. ABERCROMBIE. What would lead you to think that this is going to lead to a cost savings? It seems to me the only thing this could possibly do is cause the States to spend more money. I am not essentially in argument with you because I am not too sympathetic with States that on the one hand complain about paying a Federal royalty, then they have got extraction taxes and sales taxes and every other kind of gimmick they can figure out to get money out of the minerals for the States and the reason that they are really against the royalty payment is they think that is a few bucks less then they will be able to put in their own pockets at the local level over and above the august philosophical points that they want to make in the process.

So it is not as if I am becoming a fall guy for the States on this but I cannot see how you are going to save any money at all other than unless you are talking about saving it by having the States spend more money to collect their half of the royalties. Right now aside from arguing about the royalties, the States have a pretty good deal. The Federal Government does everything and they get half of it.

Ms. CUBIN. Would the gentleman yield, please?

Mr. ABERCROMBIE. Sure.

Ms. CUBIN. With all due respect, I think that is the reason that we are here. As the witness said, the proposal is on the table and so we need to get as many facts on the table as we can, both to see from the benefit of the Federal Government as well as the benefit of the States. We are all one big organism, if you will, and so if it can be done a better way, it ought to be.

I would like to commend the witnesses for being here today and thank you.

Mr. ABERCROMBIE. OK. Can I get my time back now? I still would like an answer as to why you think there would be a cost savings.

Ms. BACA. Mr. Abercrombie, what this goes back to is a few years ago a proposal was forwarded to the Department of the Interior by the State of Wyoming, one I am sure you are well aware of. At that time the State of Wyoming told us that they felt that they could perform the royalty collection function in a much more efficient manner than the Federal Government was doing, that is, they could collect the royalties at tremendous cost savings over what we were currently having to put forward in terms of resources.

I believe that there were four other States who also expressed some interest in the royalty collection functions as well, and it all went back to the fact that they felt they could do it in a more efficient manner. All the Rego II proposal does is open up a dialog with those States to say, OK, here is the collection process out there, can you collect them more efficiently and more effectively?

Mr. ABERCROMBIE. OK, thank you.

Mr. CALVERT. We appreciate that. If we could suspend for 15 minutes and we will return right after a vote on an amendment. Thank you.

[Recess.]

Mr. CALVERT. I apologize for that long 15 minutes. We had a series of votes. We will resume the hearing. There will be another vote in about 10 minutes and allowing for a few minutes before we recess for the next vote, we would like to start right away.

Mr. ABERCROMBIE. Mr. Chairman, could I just conclude?

Mr. CALVERT. Certainly, Mr. Abercrombie.

Mr. ABERCROMBIE. Thank you. Ms. Baca, I just want you to know that I do appreciate the fact that you are trying to come to grips with this. I do believe it is a premature stage right now and I urge you to get to this discussion and consultation as quickly as possible although my guess is at the end that the States will end up picking most administrative costs up in this and if that is what they choose to do that is their business and I will certainly take it under consideration at that time. Thank you, Mr. Chairman.

Mr. CALVERT. Next, Ms. Barbara Cubin.

Ms. CUBIN. Thank you, Mr. Chairman. I do have just a couple of questions. First of all, if all substantive administrative decisions will remain the prerogative of the Interior Department then how does the Department intend to take advantage of the State's better knowledge of the producers of the land of the leases and just the businesses within this jurisdiction. Is there a plan, has that been discussed at all?

Ms. BACA. No, ma'am. Again, we hope that we can open up that dialog for discussion in July.

Ms. CUBIN. How will the States be able to realize the economies associated with combining their administration of similar programs with the Federal royalty program if all of the substantive issues are decided at the national level?

Ms. BACA. I am not really sure that I can answer that question. Again, what we based our proposal on was the information that was forwarded to us from the State of Wyoming. That proposal was sent out to all of the other States along with our proposal so that they could evaluate what Wyoming looked at in terms of those sorts of comments so I believe that all of the States and all of the people who are looking at it will certainly do the proper analysis to see if those sorts of economies are justified or not.

Ms. CUBIN. There is one thing that kind of troubles me and that is a term inherently Federal. First of all, what are the criteria that would make something inherently Federal? What makes something inherently Federal? I mean when I think of inherently Federal, I think of Federal legislation.

Ms. BACA. Ms. Cubin, I am not an attorney and all I can go by is the solicitor's opinion that was forwarded to our office when this decision was made. The opinion states that the inherently Federal functions would be any sort of decision that requires you to exercise some sort of judgment as it pertains to formulating policies or regulations.

I believe the third thing that was on there was adjudicating disputes and I believe enforcement was something else that was on there. We were told that if we had a specific proposal, then we could look at those things and see if there was any flexibility for those. However, to go out and say that we could just give away those sorts of rights that are reserved to the Federal Government, we just could not do that broadly. Rather, we would have to have a specific proposal.

Ms. CUBIN. OK, now I want you to know that I am not trying to be picky but rights that are granted to the Federal Government, that is just kind of a phrase that bothers me. You know, rights are granted to the people and then there are certain powers that the Federal Government has to have to protect those rights. And this inherently Federal really does trouble me and I wonder if in dealing with legislation or possible legislation to devolve the MMS, we might make a definition of what inherently Federal is. Would you consider that to be something good to do?

Ms. BACA. Ms. Cubin, again, I think that it is something that the attorneys are going to have to work out.

Ms. CUBIN. So you think attorneys should do that rather than the Congress?

Ms. BACA. Well, I believe the attorneys and probably Congress should be involved in that as well.

Ms. CUBIN. OK. If the title to the land, rather than the accounting functions, I know you are aware of the discussion at least of turning some of the BLM lands back to the States, so if the title to the land rather than the accounting functions was devolved to the States then do you think that the problem of inherently Federal would disappear, then that there would not be Federal——

Ms. BACA. I suppose if the lands themselves were devolved to the States, that probably would ring true.

Ms. CUBIN. What in the Administration's view is the advantage of the Department's devolution plan over a plan to transfer title to the States?

Ms. BACA. I am sorry, could you repeat that question?

Ms. CUBIN. Yes. What in the Administration's opinion is the advantage of devolving the MMS rather than turning title over to the States, title to the land?

Ms. BACA. Again, when the Department put the proposal together what they were looking for is cost savings and the fact that the Federal Government would no longer have to collect the royalties, which could mean savings to the Federal Government. They did not consider turning over the lands themselves.

Ms. CUBIN. Well, do you think that the Administration, that Secretary Babbitt's plan gave any incentive for the States to want to do this? I mean why in the Administration's view would they want to do that? Would they want to only take over the bookkeeping, if you will, would it cost them more money, just take over the bookkeeping and still have no input or, well, maybe they would have at most input but would have no authority whatsoever in any of the decisions, why would the States want to go along with that?

Ms. BACA. Again, our proposal was based on the Wyoming proposal which did not include what we considered to be the "inherently Federal" functions. It is strictly the administerial types of activities—the collection and the accounting type functions. I really think that Wyoming would want more than to just collect and disperse, but I do not have the authority to say that either.

Ms. CUBIN. I have no further questions, Mr. Chairman.

Mr. CALVERT. This is a question that was in my mind from your testimony. I understand that Wyoming was certainly troubled by the amount that MMS was charging for collection versus what they thought was a reasonable amount. Now I understand that Wyoming's previous figures may not be that realistic but they certainly were not happy with the MMS figures either.

Ms. BACA. I believe that is true.

Mr. CALVERT. That is true. I understand also you received a number of comments regarding devolution of MMS and alternative suggestions for streamlining your existing operations and certainly there has been criticism, not just from Wyoming but from many other States that MMS is not operating as efficiently as it should. Have you received any detailed information or comments from States and industry outside of Wyoming that we could look at?

Ms. BACA. I believe that we have received initial letters back that they received our devolution proposal but I do not believe that we have received specific alternatives. I think that is because we have told them that we are waiting to hold this meeting in July but we would like people to bring alternative proposals forward for discussion.

Mr. CALVERT. Well, if you receive any of those comments, please pass them on to the committee. I am sure there are a number of alternatives for having a much fairer and simpler royalty collection process and a more efficient onshore minerals program that promotes domestic development. We have a witness here today from State and industry who will discuss a number of those alternatives that will save money instead of increasing costs for both industry and the States which I am sure wants that to occur.

I would ask how will the Department respond to one total transfer of the Federal minerals and surface estate to the States? You have probably been asked this question several times but we will listen to your answer one more time. How will the Department respond to a total transfer of the Federal minerals and surface estate to the States?

Ms. BACA. Again, I believe the Department's position is that we are willing to look at turning over the royalty collection, however, the Department feels that the land and the resources themselves belong to the American people, that the Department has been charged with the stewardship of those resources, and that they have a fiduciary responsibility to maximize the income for the good of all American people.

Mr. CALVERT. Don't you believe the States are competent enough to manage those resources for the United States government?

Ms. BACA. I believe the Department of the Interior believes that it is the Department's responsibility at this point, it is basically the Department's stewardship.

Mr. CALVERT. You say you have enough trust in the States to collect the revenue from these resources but you don't have enough faith in the States to be in charge of the decisionmaking processes in order to collect that revenue in the first place?

Ms. BACA. Well, I believe the Department feels that the Federal Government is here to make decisions on behalf of all American people and we believe that, again, the States probably have an interest in going after a more aggressive royalty collection because they share in 50 percent of the net receipts. But, again, the Department's position is that turning over the resources and the land is not on the table at this time.

Mr. CALVERT. Just all of the cost but none of the responsibility.

Mr. ABERCROMBIE. Would you yield a moment?

Mr. CALVERT. Certainly.

Mr. ABERCROMBIE. I want to make sure I understand that answer. When Mr. Calvert said all of the responsibility but not the authority—I want to make sure I understood exactly what you said or what the meaning of it is. If it is the net receipts, is the proposal that you will take to the States and/or the tribes that they will take the administrative costs from their end of the gross and then what is left over will be the net to be divided up 50/50 or will their administrative costs be taken and included with respect to how you determine the net? In other words, are you taking it off the top?

Ms. BACA. I would like to defer to Ms. Carolita Kallaur on that.

Ms. KALLAUR. OK. I believe the way the devolution proposal is written is that the costs that would be incurred by the States together with the Federal cost would be taken off the top from the gross and then you would end up with the net. I hope I am answering your question.

Mr. ABERCROMBIE. OK, so then the States won't be taking it out of their share then, the administrative overhead will come out of the gross share and then what is left over?

Ms. KALLAUR. It is similar to the way it works right now. It is just the costs of operating the program that are deducted from the gross receipts in order to get the net. It is the same procedure we currently use.

Mr. ABERCROMBIE. OK. So from a bookkeeping point of view, it is now the Federal Government's responsibility to assess and take care of the costs out of the gross end for the collection and you want to switch it to the State?

Ms. KALLAUR. The only thing we propose to switch to the States is that a State would be performing a greater portion of the functions. So those costs would be included in the calculation together with the residual Federal costs.

Mr. ABERCROMBIE. OK, my final point then, and I do believe this comes from the question the Chairman asked, does that mean those folks will be State employees?

Ms. KALLAUR. The people who will be performing the functions, they will be State employees, that is correct.

Mr. ABERCROMBIE. So the State, whether it is Wyoming or anybody else, will have to take care of whatever retirement or workers' comp or anything of that nature. It will no longer be a Federal responsibility?

Ms. KALLAUR. That is correct, but we would be providing additional funds to the States to carry out these functions.

Mr. ABERCROMBIE. OK, I will believe that when I see it. Thank you.

Mr. CALVERT. Let me go back to this. Out of the collection for royalty, let me hear this again, you say that we are going to take the costs off the top and then divide by two and the Federal Government receive 50 percent of the balance and the States receive 50 percent of the balance, is that what you just said?

Ms. KALLAUR. Yes, that is correct. That is similar to what we do right now except that what the States are currently paying is 25 percent versus 50 percent, but the way you do the arithmetic is the same.

Mr. CALVERT. Do you have a cap on the amount of money that the State can charge for those collections?

Ms. KALLAUR. Well, under the devolution proposal, and I have to stress that this is really a proposal, and clearly I am sure what we end up with is not going to be what we begin with, but we do have a cap in terms of the amount of money that we are proposing would be provided to each State.

Mr. CALVERT. Is it commensurate to the amount of money that is being paid out today for administration and overhead?

Ms. KALLAUR. No.

Mr. CALVERT. What was that answer again?

Ms. KALLAUR. I believe if I understand your question correctly, the answer is no because what we are proposing is a system that is based on the costs projected by Wyoming back in 1993 which are much lower.

Mr. CALVERT. If those costs exceed those estimates that Wyoming did several years ago, who is responsible for the additional costs going over that cap?

Ms. KALLAUR. Under the proposal that is on the table today, which is only a proposal, it would be the responsibility of the States.

Mr. CALVERT. So, in other words, the cost of administration and overhead that is first taken off the top is considerably less than what the Federal Government is now charging and if in fact the States are not able to meet the expected cost savings, then that cost would be born solely by the State?

Ms. KALLAUR. That is correct, but I think we all realize that the only way this proposal would ever become a reality is if the States really believed that they could assume those functions with the costs Wyoming projected. We also would have to go back to Congress and change the Federal Oil and Gas Royalty Management Act.

We realize we need to have a dialog with all the people who would be affected by this proposal. We cannot mandate this.

Mr. CALVERT. OK, I just wanted to make sure that we are on the record to State that it is not an open-ended cost the Federal Government is proposing that the States could receive but you have set a proposed cap on the amount of money that could be charged for administration overhead?

Ms. KALLAUR. That is correct.

Mr. CALVERT. That is the debatable issue as far as the States are concerned.

Ms. KALLAUR. Well, it is clearly one of the debatable issues.

Mr. CALVERT. Go ahead.

Ms. CUBIN. If you have more questions.

Mr. CALVERT. I have a fly running around here anyway. I will leave it to you.

STATEMENT OF HON. BARBARA CUBIN, A U.S. REPRESENTATIVE FROM WYOMING

Ms. CUBIN. Thank you, Mr. Chairman. I truly regret that Mr. Armstrong cannot be here and I know that it creates a difficulty for those of you who are here to try to give us information. But I am getting more and more sympathetic with Representative

Abercrombie's original remarks. In the first place it just seems to me that this is really not much of anything, that there hasn't been much thought put into this, that, you know, the Wyoming proposal that was done in 1993, I think everyone knows that there were some major flaws in that.

And if you don't, you really should have known that and so I mean I think we are here just kind of playing jacks. We need more substance to deal with but if our suggestions, if we can make suggestions here and then you can take them back and possibly incorporate them into a plan, then I would see some value could come from this hearing and so I hope that between us and the other people that you hear that you will really be able to do that.

I recently became aware of a report that was issued by the project on government oversight that alleges that over a billion dollars in royalties and interest are owing from Federal leases in offshore California. The report says that the peculiarities associated with the California market are the cause of the large royalty shortfall.

Jimmy Shaw, whom you know, the MMS Associate Director, is quoted in Oil Daily as suggesting that MMS valuation regulations, at least over periods from 1988, may prohibit the collection of California royalties and interest. And, you know, one of the major disagreements that Mr. Armstrong and I have had is his claim to want to put more money into the United States Treasury, more money that rightfully belongs in the United States Treasury, while at the same time it appears that he is ignoring the United States Department of Commerce studies that say if you increase the royalty from 5 to 8 percent, you will cause a loss of jobs and possibly a closing of plants.

Well, that is probably less money in the Federal treasury. We are looking at, and this is not necessarily under Mr. Armstrong, but through the Interior we are looking at ASQ in national forest of 14.3 and then only 2.2 being allowed to be harvested.

I am very frustrated by the lack of direction from the Department of the Interior by lack of any overall planning and I want to work with you on this. If this is going to be best for the States and for the Federal Government then that is certainly what I want to do but I won't waste any more time now.

I do have an opening statement. It is too late to give that now but I wanted to welcome some people here, Jim Magagna, who is the Director of Public Lands from Wyoming, Deimer True, who will be here to testify but also I wanted you all to wish the Chairman happy birthday.

Mr. CALVERT. Thank you very much. After listening to some of the testimony, one thing that we also need to consider is an option. If in fact this one particular devolution process doesn't move forward in lieu of transfer, how can we streamline existing accounting practice and combine all mineral activities possibly into a single minerals bureau?

There has certainly been some criticism that MMS is not operating as efficiently as it should and certainly we do not want to increase cost to the States nor industry in this process and so could we look to the Interior to do a study on how they could operate MMS more efficiently as a second option?

Ms. BACA. I believe that that is probably something the Department would be amenable to through our REGO II process. We put this out as a proposal but, as I stated earlier in my testimony, the Department is doing a number of things to streamline their activities. There are several committees that have been set up that include not only officials of the Department but officials from industry, from the tribes.

We have brought them to the table and said now let us sit down and let us talk about what are the obstacles out there and what can we do to better serve you?

Mr. CALVERT. But we may have you back in the future sometime this summer and hopefully by that time there will be some more specific answers to our questions and certainly maybe a second option of how much better the MMS could operate. So with that, if there are no further questions, I want to thank you and thank the panel for coming out today, and we will introduce our second panel.

Ms. BACA. Thank you, Mr. Chairman.

Mr. CALVERT. Thank you. I think we do have a vote, so let me introduce the second panel and if you could go ahead and sit down, we will go vote and be right back. Panel two, Mr. Jim Magagna, Director of Federal Land Policy, and Ms. Christine Hansen, the Executive Director of Interstate Oil & Gas Compact Commission.

And if you could go ahead and take your seats at the table, we will suspend for a few minutes and go vote and be right back so thank you very much.

[Recess.]

Mr. CALVERT. Thank you for your indulgence. There are no further votes this afternoon, thank God, so we won't have any more delays. So, first, Jim Magagna, Director of Federal Land Policy, State of Wyoming. You may begin your testimony.

STATEMENT OF JAMES MAGAGNA, DIRECTOR OF FEDERAL LAND POLICY, STATE OF WYOMING

Mr. MAGAGNA. Thank you, Mr. Chairman. I am also the Director, incidentally, of State Lands for the State of Wyoming and as such collect mineral royalties from our State lands. I am here today on behalf of Governor Geringer. I thank you for providing the State of Wyoming with the opportunity to testify. More minerals are produced from Federal land in Wyoming than from any other State, and we are vitally interested in those proposals that affect those mineral properties.

Wyoming believes that it can do an efficient and effective job at collecting royalties at less cost to all entities involved. We have a proven track record at collecting royalties on our State lands. We are the largest player in this discussion, but at the same time we are very sensitive to the issues that devolution might create for smaller producing States and welcome and seek participation of each and every involved State.

We would be most pleased to act as a leader and as a facilitator in this process. The question of costs associated with MMS mineral collection and related functions has been on the table for years as you are well aware. It is time to craft a solution that will benefit the State and the Federal budget.

First, allow me to briefly comment on the Department of Interior's devolution proposal dated March 27. Under that proposal, MMS would transfer to the States the responsibilities associated with collecting royalties but none of the authority which must accompany the responsibility. It is obvious that MMS believes at this point that few of these functions are delegable.

The States would have no policymaking ability, no rulemaking authority, no funds management authority and no enforcement authority. We too have reviewed the solicitor's opinion with regard to inherently Federal functions, and while I offer no legal opinion on that solicitor's view, we do believe that the opinion that is being relied on does not, in fact, address the issue of functions of the Federal Government being delegated to the States. We believe it deals in a different arena and as such is not a valid analysis of the authorities involved here.

However, while the MMS did not propose to give any of the authority to the States, they did advise that a financial penalty system may need to be developed and applied to States that do not collect all royalty due in a timely manner, hardly consistent with a true Federal/State partnership. This is obviously unacceptable to us.

It is also our understanding that part of the takeover would involve inspection and enforcement currently performed by the Bureau of Land Management. We have no information at this time which defines what those responsibilities will be, how they will be paid for or what oversight might be imposed in that case as well. This proposal as has been addressed earlier refers to a 1993 Wyoming study and proposal. This 1993 Wyoming Plan has limited applicability today and does not represent Governor Geringer's administration's views on a proper devolution. The subsequently implemented Wyoming automated system of mineral tax valuation and collections would change the assumptions on Wyoming's part in a new Wyoming Plan developed today. Quite frankly, Mr. Chairman, Wyoming urges that the March 27 Mineral Management Service proposal be quickly discarded in favor of a plan to be developed by the affected States.

The thirty eight States involved have varying degrees of interest in taking over the MMS function, particularly the States which have relatively small collections. Several of these States began their dialog last month, and a variety of ideas have been discussed. As an example, perhaps the minerals should be deeded to those States which receive relatively small amounts of Federal mineral royalties while conveyance of the minerals to States which produce large amounts of minerals should be accompanied by an overriding mineral royalty to the Federal Government.

Under this scenario, there would be no inherently Federal function to blur the lines of authority between the Federal and State government. The States would own all of the minerals, perform all of the functions, and the Federal Government would simply get a royalty check each month. Another possibility is for the States jointly to develop a uniform reporting remittance form and procedure.

The most fundamental issues to be resolved involve what an Interior Department solicitor deems constitutional limitations. Those must be addressed as the first items for agreement. Wyoming is committed to this project and intends to retain a project manager to work with the other States and the affected industries. The primary role of the Mineral Management Service should be to serve as a resource to the States in the development of a plan and, following adoption, to effectuate an orderly transfer of authority and operation.

Currently if our reports are correct, the primary role of the MMS has been to lobby this Congress against devolution in conjunction with some of the major oil and gas producing companies. It seems to be a conflict, or at the very least, disingenuous, to have an agency which is hostile to the notion of devolution as the shaping force behind the debate.

We in Wyoming envision a system which is developed jointly by the affected States with strong input from industry, a system which is simple, efficient, less costly and more innovative. The States, collectively, must have the freedom to make acceptable choices and the authority to implement the agreed upon system.

In summary, our objectives are simple: design a uniform system which can be used by all participating States, lower collection and recordkeeping costs for both government and industry; achieve uniformity between Federal and State land systems, which can eliminate duel royalty and severance tax reporting and increase efficiency for royalty payers; and in the process, foster a renewed sense of State responsibility and ability in the management of mineral resources for the benefit of the States, the Federal treasury and the mineral industry.

We look forward to the dialog that it has been indicated today will begin in July under the direction of the Mineral Management Service but we firmly believe that that dialog should have proceeded the announcement of a proposal for devolution. Again, thank you, Mr. Chairman, Representative Cubin for allowing the State of Wyoming to participate in this hearing today.

[The prepared statement of James Magagna can be found at the end of the hearing.]

Mr. CALVERT. Thank you. Ms. Christine Hansen, Director of Interstate Oil and Gas Compact Commission.

STATEMENT OF MS. CHRISTINE HANSEN, DIRECTOR, INTERSTATE OIL AND GAS COMMISSION

Ms. HANSEN. Thank you, Mr. Chairman, Congresswoman Cubin, I am pleased to be here today on behalf of the Interstate Oil and Gas Compact Commission and its Chairman, Governor Ed Schafer of North Dakota. I am pleased that the committee is looking at this issue. I have filed with the committee testimony which I understand will be spread on the record so I will just mention a couple highlights in my testimony.

The Administration's proposal made in March that onshore royalty collections will be transferred to the States by the fall of 1997 was made without consultation with the States. We are pleased to work with the MMS and the Department of Interior at this point. The Interstate Oil and Gas Compact Commission is an organization of 35 States, 29 oil and gas producing States, and six associate members.

California was one of the six founding States of the IOGCC in 1935 and Wyoming has been a long-time member of the IOGCC and several governors of each of those States have been past chairman. As the subcommittee is well aware, interstate compacts are very special legal organizations authorized by the United States Constitution.

The IOGCC is one of the earliest compacts authorized by Congress, and I talk about the history of the IOGCC in my testimony. The governors have always believed that the States have and continue to have an obligation to prevent avoidable waste of oil and gas and that States acting cooperatively are as capable of solving multi-State problems as the Federal Government.

The States are now working in several directions to address the proposal of the President. Governor Schafer has appointed a committee of governors which is co-chaired by the governor of Wyoming and the governor of Nevada. There is a steering committee working under that group and I have attached to my testimony a list of all of the steering committee members right now.

Our steering committee consists of State people, industry people, trade representatives. We have no restrictions in any of our work. We are working cooperatively with industry and have over our 60-year life done all of our work by talking to industry and working directly with them.

It is important that the committee understand that this proposal did not come from the States as the Department of Interior testified here earlier this afternoon. Former Wyoming Governor Mike Sullivan, also a past chairman of the IOGCC, was an advocate of Wyoming taking over the royalty collection function. The analysis of his administration was that Wyoming could handle the function in a more cost-effective way, and that may be true.

The States at this point do not have a firm opinion about that but the States are willing to look at it and to honestly analyze it. The States are developing individual proposals and then will come together and work on those as a cooperative group. There is also a need to address this question in two separate directions, one from the view of the States with larger collections of royalties, and one from the view of States with collections which are insignificant in terms of their overall State budget.

In this regard, Governors Schafer, Geringer and Miller have called the governors, personally telephoned the governors in States with relatively smaller royalty collection and requested that they designate a representative to work with the IOGCC to fashion some recommendation which would address the needs of those States. The group will be headed by Don Mason of Ohio who is chief of the Division of Oil and Gas in the Department of Natural Resources in Ohio.

The small royalty collections pose a real opportunity for Congress even apart from how you choose to deal with the overall recommendation of the President. The Department of Interior has reported that royalty payments were distributed to 38 States in 1994. The most recent published accounting, that for 1993, represents 35 States. A news release of the Department dated April 17, 1995, reports first quarter distributions to 34 States, including a payment to Tennessee of $57.46.

Perhaps there is something else the Federal Government could do with that Tennessee leasehold than collect a royalty, process it, audit it, and split the net with the State amounting to $57.46. I was distressed to hear the absolute opinion of the Department of Interior today that they will not discuss with the States the disposal of resources to the States. I think when you look at a situation like Tennessee and we could go through the Subcommittee books, I am sure, and look at States with relatively small royalty collection.

I want to just touch on the solicitor's opinion which has been mentioned today. In finding a superior solution, Congress has complete discretion. You are not bound by the laws that were written in the past. That is the whole reason that Congress gets elected. It is an excellent opinion from the solicitor's office and the Department of Interior discussing inherently Federal functions and it is a fine description of the limitations on the flexibility of Federal agencies and the requirements placed on Federal agencies by the Congress.

We need not argue with the conclusions of the opinion. We need only say that the basis for the opinion is the law written by Congress and Congress can change the law. The President has already expressed his desire that this transfer of royalty collection responsibility take place, thus signaling his willingness to sign a Congressional initiative which would accomplish this end. So, the inherently Federal functions issue is not an issue because you are Congress.

I do have a law degree and I cite my legal credentials in my testimony. I am pleased to take your questions.

[The prepared statement of Christine Hansen can be found at the end of the hearing.]

Mr. CALVERT. Thank you, Ms. Hansen. As you know, the subcommittee has spent a considerable amount of time studying the proposals in the overall minerals management issue. We fully expect the parties involved to put forth a sincere effort in developing successful management alternatives as we have been discussing. Ms. Hansen, could the IOGCC provide for the record a schedule and an implementation plan including your strategy to work with DOI and industry that addresses the topics that have been covered in today's hearings?

Ms. HANSEN. Well, I would be glad to provide more detail than is reflected in my testimony. The fact is that we do not have a set schedule. The States are individually analyzing this and some of the States are taking a little longer than in other States and some of the States don't have very high interest in analyzing it so bringing those States together will take a little longer. We have an organizational meeting of the steering committee scheduled for this Sunday and then we are going to hopefully present an outline of a proposal to the Western Governor's Conference meeting in late June.

Mr. CALVERT. Well, we are fortunate. It doesn't seem that BLM has any kind of schedule either so possibly we could work with you and put together some ideas. As you know, the new Republican Congress has initiated a lot of new ideas and many block grant programs ranging from the school lunch programs to some of our welfare programs. Following along in this theme, are the States ready to seriously consider a significant role of managing all the Federal mineral activities, including conveyance of the minerals interests? I think that is probably a good question for you, Jim.

Mr. MAGAGNA. Mr. Chairman, I can only speak, of course, for the State of Wyoming. Most certainly the State of Wyoming is extremely interested in assuming a far more significant role in the management of the Federal mineral resources. They are extremely extensive in our State and we realize that is a very heavy responsibility. We are willing to commit the resources to doing that provided that that delegation of responsibility includes the necessary authority to adopt and enforce those types of policies that allow us to perform that function in a cost efficient manner and in a manner which is workable, not only for the State but which is cost efficient and production efficient from the perspective of the companies involved as well.

We realize that in the development of these vast resources that we have in Wyoming, we are at the mercy of the private sector companies that develop those resources and we need to take those steps that we can reasonably take to make it economically and financially feasible for those companies to go further not only in the development of new resources but in maximizing the recovery of those current resources that are being produced from both the Federal and the States mineral resource.

Mr. CALVERT. Certainly that is important and one of the reasons we are here is to understand what the particular State, and certainly Wyoming in this instance has the most to gain and the most to lose, your management philosophy, how you could reduce your royalty costs while increasing, we would hope, development activities and explore in the resources that are in Wyoming to increase revenue both to Wyoming and to the United States Treasury in an efficient way and hopefully as this process continues, we can hear your ideas and your comments as this moves forward.

One of the problems that we have talked about in Ms. Hansen's and your testimony of the 38 States that effected this proposal, 18 States receive a total of $1.5 million a year, a very small amount spread over those States. Could you tell the subcommittee more about your initial ideas for allowing these 18 States to officially manage the small amount of revenues?

Ms. HANSEN. Well, one of the great things about being executive director of an association of States is that I don't have to have any ideas, the States come to me with them.

Mr. CALVERT. If you go to Congress.

Ms. HANSEN. And I think the States will come up with some good ideas. The fact is that before the President put this proposal on the table those States had not honestly looked at this issue. They had not—Wisconsin just had not been clamoring to collect the $864 or whatever it was last year.

Mr. CALVERT. Couldn't afford to return a phone call.

Ms. HANSEN. Even the amounts in States like Illinois, Ohio, New York are not very big amounts compared to the total State budget and the demands of State government. So the honest answer to your question is that the States are just beginning to look at that process but I think they will come up with real creative ideas and

I think it is great that the Department of Interior has laid this question on the table and has opened the dialog.

I think the Department of Interior has certainly in the two years I have been in this job demonstrated a real interest in working with the States. They have reached out to the States. They are working cooperatively with the IOGCC on a couple projects and I think some ideas will be forthcoming but they are not here now just because it is such a new proposal.

Mr. CALVERT. Thank you. Ms. Cubin.

Ms. CUBIN. Thank you, Mr. Chairman. I have a comment and then a question to follow it up. I was a member of the subcommittee on the Wyoming State legislature where we recodified the mineral valuation and taxation statutes. And I think we spent $250,000 over the course of one summer and I never, ever, ever could have conceived that mineral taxation could be so complicated.

One of the problems that we dealt with while I was in the State legislature was constantly should we raise our severance taxes, and I recognize severance and royalty are different and that will be part of my question, but should we raise our severance taxes? Will that make us non-competitive with another State? And, you know, the valuation process itself was so complicated that we could not tell because there are different methods that are used in calculating different formulas all the States use.

There are different points where the mineral is exactly valued, and then there are deductions allowed for certain aspects in production. I mean there is dirty gas and there is clean gas and there is light oil and heavy oil and wet coal and dry coal, you know. The minerals themselves are so different. Then on top of that, we kind of wanted to value all of the minerals the same and so that one industry wasn't carrying more of the burden than the others but then that is like comparing apples or oranges and how do you do that in some sort of a reasonable fashion.

So I cannot imagine that anyone would ever be fascinated by something like that but we sort of got to be junkies and by the time it was over it was fun. So the reason I bring all this up is that in concept I am in favor of the devolution of the MMS. I certainly see how it could be helpful but I am very, very concerned that this might be a much more complicated issue than we know at this point in time.

I want to know, do you think, and this would be to you, Jim, probably, but, Christine, either one, do you think that severance tax systems and I mean there are so many different severance tax systems for so many different minerals that you cannot conceive of that, do you think they can be integrated with royalty payment systems into a single accounting system that will fit the 38 States?

Mr. MAGAGNA. Ms. Cubin, I believe that the process that we would go through with the States working together to develop a State proposal for taking over the function of the Mineral Management Service would provide an opportunity to address some of those issues. Currently there is no incentive for the States to talk about their relative taxation systems and what the differences are and the problems that that creates for the mineral companies in doing their reporting.

This would provide an opportunity for that without going so far as to suggest that we would achieve uniformity of taxation necessarily among States or that that is even desirable. I would suggest that what could come out of this is not only a consistent reporting format at least for mineral royalty collection on both Federal and State lands in all of these involved States but the same consistency in reporting system that is used for the collection of the various types of taxes that the different States may impose. This represents an opportunity to create a real benefit for the mineral industry which indirectly, I believe, is a benefit then for each of our individual States as well as for the Federal treasury.

Ms. CUBIN. I certainly agree with that and I certainly think uniform reporting is most advantageous to everyone involved. I wonder also, have you had any feedback? It seems that maybe some of the majors are opposed to this and some of the smaller independent producers are more in favor of this. Do you have any indication or have you had any feedback that there will be an effort to work together for them to iron out their—I know it is pretty early since we don't really even have a plan but that is a major concern of mine also.

Mr. MAGAGNA. At this point we in Wyoming at least have not made an attempt to contact individual companies. We have heard much of the same. We have had some indications of that. I think though that that needs to be judged as a reaction to the Department of Interior proposal and when I hear that a major oil company is opposed to it, I have to respond and say, well, we in Wyoming are opposed to it too as it has been presented.

We have attempted, working through a number of the industry associations as well as of other people in the State, to say: Would you be willing to sit down with the involved States, at least the major beneficiary States, and talk about developing a plan that reflects the concerns of those States and the concerns of industry? To this point I have not had anyone representing any part of the industry say, no, we would not come to the table.

Ms. CUBIN. Well, I certainly appreciate your style in dealing with all of the interested parties and I know that reflects the style of the governor and I commend you for that. I don't have any further questions at this time.

Mr. CALVERT. I would like to thank this panel for coming out to testify today and I appreciate your indulgence while we were voting this afternoon and so you are excused. Next I would like to introduce our next panel, Mr. Deimer True of the True Oil Company on behalf of the Independent Petroleum Association of Mountain States; Mr. Terry M. Belton, Texaco Exploration and Production, on behalf of the Rocky Mountain Oil and Gas Association; and Mr. Larry Nichols, President of Devon Energy Corporation on behalf of the Domestic Petroleum Council and the Independent Petroleum Association of America. First, Mr. Deimer True.

STATEMENT OF DEIMER TRUE, TRUE OIL COMPANY

Mr. TRUE. Mr. Chairman, thank you. It is a privilege to be here. I have pondered why exactly I was here today. The last time I testified in front of a committee that Ms. Cubin served on, I was advocating a battery recycling bill and her no vote led to a 100 percent no vote on the bill that I sponsored so it must be today that the MMS devolution proposal as advocated by DOI must—the proponents of my being here today must know about the history of my success in front of Ms. Cubin.

Ms. CUBIN. Mr. Chairman, if the witness wouldn't mind my interrupting just for a moment.

Mr. CALVERT. Certainly.

Ms. CUBIN. He happens to be the President of the Senate in the State of Wyoming and when he was the majority floor leader in charge of the bills that would be heard every year he was President of the Senate, every single bill that came to the Senate was heard except for one year and that was my bill.

Mr. TRUE. It was a bad bill. I can tell we are not getting along well today. Mr. Chairman, it is a pleasure to be here and I am representing the Independent Petroleum Association of the Mountain States. We have about 750 members. We basically operate oil and gas production in the 10 Rocky Mountain States.

I am a partner in True Oil Company based in Casper, Wyoming and we produce oil and gas in most of the IPAMS States. After listening to much of the testimony that has previously been given, I think my written remarks are sufficient and my oral comments I think can be in summary form. First of all, let me say that IPAMS and True Oil Company applaud and support the efforts of downsizing the Federal Government and reducing the Federal budget in the concept of devolving MMS but we are not in favor of the DOI's March 27 proposal to devolve responsibilities of the MMS.

I think others have said it very well that that proposal transfers very limited royalty collection functions but none of the authority or responsibility. It is our opinion that what you will have is you will have the Federal checkers checking on the State checkers who will be driving the industry compliance checkers back to checking with the Federal checkers to find out if they are consistent with what the State checkers are being told to do and it will actually significantly expand the amount of regulation.

We think that the total transfer of the Federal mineral and surface estate to the States is the way to go. We believe that it will lead to an overall reduction in the size of government. It will strengthen State governments and generate economic prosperity for the Rocky Mountain region and we wholeheartedly support the testimony of State Land Commissioner, Jim Magagna. We think they are on the right track.

The States, each and every one of the States, are unique and different and we hear some of the arguments against devolution are that the individual companies will have to deal with multiple regulators. Well, heaven knows, we deal with multiple regulators now and we feel that dealing with State officials who know firsthand what is unique about their State and what the customs of their State are, while it is a trade-off, it is a worthy trade-off and one that will benefit all parties in our opinion.

I mentioned that True Oil Company produces oil and gas in almost all of the Rocky Mountain States and several other States as well so we are not looking at this just from the standpoint of dealing with the State of Wyoming. We believe we can deal with North

Dakota, South Dakota, Montana, and all of the other States successfully directly even though we are a small independent.

The time is truly now to begin. I think to think in limited terms would miss an absolutely golden opportunity to see the natural resources of this country to put to best use and optimum use for all of the people of the country. In the meantime, I would like to mention a couple of intermediate steps that MMS might consider. I think they could eliminate the payor information Form 4025, eliminate audits for low volume wells producing less than 200 MCF per day, increase training for current MMS staff, combine MMS and BLM into a single Federal minerals agency, and take Federal royalty in kind.

I also urge you to favorably consider the proposed legislation entitled the Royalty Fairness Act. In summary, I believe the current proposal is fatally flawed and would be counterproductive. We think that the Congress should look to the Federal royalty recipient States to develop a comprehensive proposal where all parties benefit and we at IPAMS and the True Oil Company certainly stand ready to help and participate in that endeavor.

Mr. Chairman, thank you very much, and I hope there is a resounding no vote on the current MMS proposal from DOI.

[The prepared statement of Deimer True can be found at the end of the hearing.]

Mr. CALVERT. Thank you, and I am glad to hear you like my royalty fairness bill too. I appreciate that. Next, Mr. Belton.

STATEMENT OF TERRY M. BELTON, TEXACO EXPLORATION AND PRODUCTION, INC.

Mr. BELTON. Thank you, Mr. Chairman, members of the committee. I delivered a written statement to you which will detail a lot of our recommendations and our concerns. We are reacting to the MMS proposal as well as the BLM proposal on reinvention and will also discuss the national performance review onshore portion which I believe is part of this testimony today but which has not been discussed too much, so bear with me.

If I run out of time, you've got my comments and I will be happy to answer any questions. With regard to the DOI reinvention proposals, i.e., the MMS devolution, RMOGA supports leaving MMS actually intact and streamlining the operations. At least given what we have seen so far, we are opposed to decentralizing the Federal royalty collection and production reporting functions for a number of reasons.

We support the government's efforts to reduce costs. However, the decentralization transfer of the mineral royalty collection reporting functions to States and tribes may not be the best way to achieve that cost savings. In fact, we view it as simply a cost shifting measure which may not actually benefit the States. It would simply transfer the cost of the program and end up costing the taxpayers money.

We are proposing a number of alternatives in lieu of devolution and we hope that some of those will achieve significant cost savings. I know that it does not do any good to come up here and oppose something without coming up with some alternatives, things like simplifying oil and gas valuation, better defining gross proceeds, simplifying the reporting systems, redefining thresholds. Those kinds of suggestions I think are very concrete.

These are also things that we believe the MMS has been working on. In all fairness to the MMS, I think there are a number of efforts under way right now that are looking at some of these issues and I hope that they will be considered in the final outcome. I would like to move forward and talk a little bit about the BLM reinvention proposals. First of all is the oil and gas pre-lease compliance. What this would do is require industries "benefiting" from oil and gas leasing actions to actually pay for those environmental analysis.

Our industry already pays for this activity through lease rentals and bonus bids. In fact, we have paid $130 million in rentals and bonus bids in 1994. We are also seriously concerned about BLM actually abrogating its statutory authority under FLPMA. It is true, the agency is a steward of the public lands and the effect is this would abrogate that responsibility to industry. I am not sure the environmental community would be very happy with that actually so I think it is something that—I don't know that a lot of thought went into this.

But I think it is unclear, there are a lot of questions about this particular proposal. How would you decide who would pay for these leases? How would the agency apportion analysis cost to lessees? Why would companies want to pay for the costs not knowing they would even get a lease? What stipulations would be in the lease? So I think there are a lot of serious concerns there.

As to cost recovery, BLM proposes to recover administrative costs associated with the minerals program by their estimating about $3 million savings over four years; however, the onshore oil and gas program potentially generates about $3 billion over the same time period. We feel that our industry is being singled out to pay for these routine administrative services. They are not looking to recreation, to timber, to mining some of the land uses for this kind of thing.

These additional costs, when you combine them with the cost, the added cost of having to pay for archeological surveys, T&E inventories, project EIS, all of which are the responsibility of the Federal Government but which we pay for really, renders a lot of our projects, could render a lot of our projects uneconomic. As an alternative, we suggest that BLM streamline its organization; perhaps reevaluate the three-tiered management system.

And also we have a number of recommendations in our written statement dealing with regulatory reform that we think will lead to tremendous cost savings. Let me talk just shortly—oh, one other subject is the transfer of inspection and enforcement responsibilities to States and tribes. This concept is not a bad concept, by the way, but I think that currently the Department can do this through MOUs. They can do this administratively. Why do you need to completely delegate all of your responsibility? In fact, that is what is going on in Colorado right now. There is an MOU between BLM and the State.

The unfunded mandates is the other issue we are concerned about there. The States, do they want it, do they have the money to pay for it? Finally, let me talk just very briefly about the BLM performance review. As opposed to reinvention proposals, this was done in a very deliberate, collaborative process. BLM reached out to affected groups, industry, environmental groups, the general public and sought their input on identifying issues on action plans, objectives, and then finally policy options.

This is the kind of process that we would have liked to have seen with regard to reinvention proposals. We think out of this will come some very concrete beneficial benefits implemented that will benefit both the government and industry in the general public. There are two high priority areas for our industry. Of course, number one would be incentives. We would like to see royalty rate reduction for high cost and marginal wells. We believe this will lead to increased oil and gas production. It will reduce the decline in domestic oil production and prevent abandonment of marginal wells.

The only thing you can really do, you cannot control price, is control the cost element there. And we think this will increase production and ultimately help the State and Federal entities. We also would like to see royalty credits for the added cost incurred on the projects I mentioned such as surveys, inventories, and the EIS activity. This is very costly, very time consuming, and we get no reimbursement for this so we think we should get royalty credits in the form of ECO credits, whatever you want to call them.

Finally, regulatory reform probably is one of our major issues. We would like to see broad-based regulatory reform. API just recently conducted a study of EPA proposed regulations and found that it would cost our industry probably $14 billion over four years and a loss of about 19,000 jobs in industry. The government has got to conduct, we feel, risk assessment and cost benefit analysis before imposing these kinds of requirements on our industry.

As well, we should look for streamlining regulations and eliminating regulatory duplication among Federal and State entities, such as delegating some of the down home responsibilities to the States, consolidating reporting forms, automating permitting approval process, and research data. Those kinds of ideas would be very helpful.

Let me say one more thing about NEPA planning. Land management decisions, we feel should be based on sound science and not on emotional rhetoric and not based on controversy. We would like to see a comprehensive research data base, consolidated, put together and maintained, that all of the different agencies could use and land users affected by it could also use. This is a good basis for making land use decisions.

This is the direction we would like to see NEPA go in expediting the environmental review process. It takes way too long, it is way too expensive, and these are the kinds of things that we think need to be addressed in NEPA. We do not think endless studies on controversy is going to achieve that and I think all it is going to do is flame those controversies so we look more for efficiencies. Thank you very much.

Mr. CALVERT. Thank you, Mr. Belton. Next, Mr. Larry Nichols, President of Devon Energy Corporation on behalf of the Domestic Petroleum Council and Independent Petroleum Association of America.

STATEMENT OF LARRY NICHOLS, PRESIDENT, DEVON ENERGY CORPORATION

Mr. NICHOLS. Thank you, Mr. Chairman. I am representing the Domestic Petroleum Council, which is approximately 20 of the larger independents, as well as the Independent Petroleum Association, which is the largest trade association in the United States representing 5,000 oil and gas independents scattered throughout the country.

When many of our members first heard the word devolution of MMS, it had some appeal because we immediately conjured up images of savings of government, reduction of cost in royalty calculations, and other attractive objectives. When we studied the Administration proposal though, it soon became clear that this was not really devolution but more convolution. With regard to transferring effective things to the State, it really only transfers certain ministerial functions, functions that are related to audit.

The MMS proposal would retain all the policies that previous witnesses have described that would preclude the States from doing much more than audit functions. The alleged cost savings were based on a 1992 Wyoming study that we have earlier had the State of Wyoming itself disavow. And, indeed, those cost savings are not immediately apparent under this halfway proposal that has been proposed.

For example, under the existing arrangement, the Minerals Management Service does a very credible job of trying to have consistency among their auditors. Even with their credible efforts given the complications of Federal royalty calculations, it is not unusual to have different auditors interpreting the same regulations differently. Imagine what would happen when you have up to 38 States and a host of Indian tribes without any internal mechanism to resolve those audit disputes, each having their own audit interpretations on what the Federal Government was proposing.

As Mr. Deimer earlier suggested, the checkers would go around checking the checkers and the checkers and the checkers, and the cost of both the government and the State governments and the industry under this halfway proposal would go up rather than down. The problem is that the States cannot integrate under this proposal the Federal royalty collection into their own State royalty collections so that you would have a State auditor trying to implement both audits on State royalties, on State lands, applying State audit principles and State guidelines, and at the same time that State auditor would be applying a different set of Federal regulations when he went out to do audits.

Imagine the consistency and the confusion that that would cause. The fundamental flaw with the proposal is that it either goes too far or not far enough. The Administration proposal gives up the economies of scale that are inherent in the current centralized system but by retaining the substantial amount of the authority and power precludes the States from taking advantage of the own local knowledge that the States have and precludes the States from integrating the Federal system into their own State system. We are disappointed to hear that the Administration said it would consider all proposals but has already rejected the idea of a total transfer.

It says the objective is cost savings but it says it is unwilling to consider what may be the greatest cost savings which is a total transfer of these lands to the States retaining the economic benefit in the Federal Government. The reason we are told is a solicitor's opinion that has opined that there is something inherently Federal about these lands. They really fall into two categories.

Many of the States, as have been earlier suggested, have been paid very, very minor Federal interest. There is something inherently Federal about owning by the Federal Government a mineral interest in Tennessee worth $57. I doubt that, or any of the other minor States. If an oil and gas company owned these minor interests, the first thing we would do would be put them up for sale. The cost of administering them clearly exceeds their economic benefit.

With regard to the two major States that we are talking about, Wyoming and New Mexico, where the vast majority of the Federal royalties are collected, again is there something inherently Federal about the Federal Government owning grasslands in sage brush country in those two States? And that is, after all, where most of this oil and gas production comes from. It is not enforced, it is not in pristine country. It is in grasslands and sagebrush in two States.

Again, there is nothing inherently Federal about the Federal Government owning that land, so most of our members think that the proposal either goes too far or not far enough. We would rather suggest that there be a total transfer of the responsibility as the State of Wyoming has suggested they would be interested in considering, so that you could integrate the Federal and the State system into one system for each State, yet with the government retaining its economic interest so there is no loss to the Federal budget or try and make the current system better.

MMS has been doing a good job recently to try and make their system better and we applaud them for that effort. There are two particular things that we should focus on. First, they have started a royalty-in-kind program on a tentative basis offshore which has met with resounding success both within the Administration and also within the industry. We would encourage you to encourage them to be more aggressive in that royalty-in-kind program. It generates the same amount of money for the Federal Government and substantially reduced the cost of collecting that money, both to the Federal Government and to the industry.

Finally, the royalty fairness bill that has been proposed also solves some of the administrative problems and some of the fairness problems that are inherent in the current legislative scheme. Thank you very much.

[The prepared statement of Larry Nichols can be found at the end of the hearing.]

Mr. CALVERT. Thank you, Mr. Nichols. One thing, or two things actually that we have heard all day long is that we are interested in cost savings and we are interested in more revenues both to the State and to the United States government. And I think it is interesting to note that all three of our panels, including the Deputy Assistant Secretary of Land and Minerals would agree that there must be a more efficient and better way to collect revenues from the States.

And so the question here is how do we get there? If we transfer those costs as some believe may be happening under the BLM proposal to the States, do you believe that the States in fact will then in that situation transfer some of those costs to you, industry, in some method? Is that a fear of industry?

Mr. NICHOLS. That is a fear of industry. In fact, I can give you an example of that. My company is headquartered in Oklahoma City. We have a good number of leases in the State of New Mexico. The State of New Mexico would like to audit our leases and our records and they would like us to bring our records to the State of New Mexico because they do not have the authority under their current system to send auditors to Oklahoma City to audit our records.

Obviously, to pack up our accounting department and our people and send them in a van to New Mexico is costly and inherently infeasible so that is a concern. Now if the system were devised where one State were going to do it, the States would have to address that funding question, recognizing that they are not just auditing entities within their States but are auditing companies that are headquartered nationwide.

Mr. CALVERT. Do you believe that even if BLM transfers all authority and the responsibility for collecting royalties, couldn't the same cost transfer occur?

Mr. NICHOLS. Yes, it could.

Mr. CALVERT. However, industry believes that you may have a better chance of being treated fairly by the States than you are today by the Federal Government if, in fact, the entire responsibility and the collection responsibility goes to the States, would that be accurate?

Mr. NICHOLS. Well, I will plunge in with an answer to that too. It is not a question so much of fairness, it is a question of we are currently operating under two totally different systems where the States have their rules and the Federal Government has its rules so we have a duplication of efforts. It is not at all unusual for us to have representatives on the same day from the EPA, the State authorities, and the BLM inspecting the same lease at the same time.

If that total transfer were made to the States so that you would only have one set of agencies in the State administering those rules, both royalty collection and lease administration, well controls and things of that sort, the savings by the elimination of duplication and sometimes triplication of effort would be apparent.

Mr. TRUE. Mr. Chairman, perhaps I would respond a little differently. It has been our experience that the response time between our company and our accounting section in the States versus our company accounting section in the Federal Government, it is much shorter in dealing with the States. We get a much quicker reply. We are able to deal with them on a much more timely basis.

One of the current frustrations we have is with the current Royalty Reduction Act and we file for those royalty reductions based upon the high cost wells and low production wells. And it is a very long time between the time that we find out that that has been accepted by MMS or not. That is not entirely analogous to the situations we have with the States but it is somewhat.

We find that we can deal on a first name basis with individuals in the respective States where it is much more difficult to deal long distance with the Federal Government. So I think you would shorten the time in which decisions are made. You can make quicker decisions by dealing with the States if we ended up actually transferring the mineral estate to the States.

And then I want to, of course, endorse also what Mr. Nichols said about going to one uniform system. That would be very, very helpful.

Mr. BELTON. I think we probably would take a little different perspective. We would prefer the centralized system of accounting, royalty collection, and production reporting. And what is kind of interesting is back in 1982 the Linowes Commission, a commission that the research committee actually worked with, concluded that the Federal Government required some kind of centralized method of determining oil and gas production from Federal leases, collecting royalties from these leases.

It also concluded that fragmentation of the Federal Government's centralized and uniform accounting system might compromise all efficiencies and savings achieved during the first decade of the Minerals Management Service so I am not really sure that everybody assumes that the States might do a better job in the accounting side of it and production reporting and so forth. I am not sure that that is a foregone conclusion.

I think that we think there is benefit in the centralized system of accounting and so forth so we have some concerns about giving that out to the very States. We have a lot of concerns about the possibility of differing interpretations. Obviously, we have a new issue out here where you are talking about transferring everything to the States but at least under the current proposal the problem with differing interpretations by the States of one set of Federal regulations could be a real problem.

As far as the transferring to the States of the whole land management process, this is something we do not have a position on right now. It is something we need to study so I am not really positioned to come out and say we are for or against that at this time.

Mr. CALVERT. Well, it would seem to me after testimony from the Department of Interior that they seem not really prepared to defend their own proposal as of yet so we have a way to go before we have a final determination. But certainly one thing I think rings true through this hearing is that MMS needs a fix, that they could operate certainly more efficiently, that we could receive more revenue at less cost, both to the Federal Government and to the States.

Certainly, at the end of this if that occurs then this would be a successful task. Mr. Nichols, one more question. You suggest that the Department expand the gas royalty in kind from the Gulf of Mexico pilot program. Is this workable for oil onshore and how does this cost to the government and the decline when royalties are taken in kind?

Mr. NICHOLS. The costs decline because if the government is taking its gas in kind, and I will start with gas because that is primarily where the effort has been, if the government is taking its gas in kind the only audit function that the government needs to do is to verify that it got its percentage of the gas that was produced out of the well. That is one simple calculation.

You immediately eliminate all the extremely complicated facts of what is the gas worth, where do you evaluate it, what deductions do you make. Under the old regulated scheme of gas that used to be simple. Gas was sold at the well head for a regulated price and we all knew what that price was. It was easy to determine what the government's revenue share was. Under the deregulated gas system, we have all kinds of very complicated ways in which we sell gas.

Sometimes gas is sold at the well head, sometimes it is sold at various pipelines at different parts around the country. Sometimes the gas is not sold until it actually reaches the city gate in Boston so going back to the well head and trying to determine what the gas price is can be a very complicated thing. By the time that gas, that volume of gas gets to Boston, it is commingled with gas coming from different States that are owned by that same owner, Federal lands, fee lands, State lands, a minced allocation problems that are there.

So, if instead of trying to wrestle with those evaluation problems, the government has delivered the gas at the well head and the government can aggregate that gas and sell it on its own, the audit problem both from the industry standpoint and from the government standpoint essentially goes away.

All these complicated valuation questions are eliminated. The only question the government has to verify is how much gas was produced from a well in a given month and did the government get its 12–1/2 percent or whatever. That is all. So you eliminate a tremendous amount of the problem and the same principles are true onshore just as much as they are offshore.

Now onshore a question that might be raised is, well, offshore we can aggregate the gas because they are large volumes. Onshore the same thing is true with regard to the major States where most of the gas production is. I have forgotten the statistic. It is something like 80 percent of the gas is in just Wyoming and New Mexico. There the government could easily aggregate that gas and sell it too.

The other gas that is scattered around the country, one wonders why the government should own that in the first place because it is not cost effective to collect revenue from those scattered and very minor gas wells anyway. And it is primarily in gas where the royalty-in-kind question arises and it is because of the valuation questions.

Oil is still sold at the well head the way it always has, so the whole methods of determining a Federal royalty calculation still work fairly well for oil. It is gas that causes the problems. But I do not see anything inherently that the government could not do the same thing with oil if it wanted to.

Mr. BELTON. RMOGA would concur with that, by the way. That is one of our recommendations, to expand the royalty-in-kind program.

Mr. CALVERT. Thank you. Ms. Cubin.

Ms. CUBIN. I just have a couple of brief questions. I have been getting lots of messages back and forth. The other committee that

I serve on is having a markup and voting on legislation so I am hearing about that and trying to decide whether to stay here or not. I make that explanation because I know that Mr. True would think I ignored his testimony if I didn't.

So I would like to ask you a question, Deimer. You said that you oppose this legislation or this proposal, as we see it. I know you said this, I just missed it, what would you require in order for us to go through with the MMS devolution?

Mr. TRUE. Well, Representative Cubin, I really think the State of Wyoming is on track and Mr. Nichols said it also in a little different way. This proposal either goes too far or not far enough and I think we ought to think in global terms, if you will, and actually think in the concept of transferring the mineral estate and the surface estate of the Federal lands back to the States.

Now I do not think in any way that means we take the economic interest of the Federal Government and reduce that at all. The concept of giving the Federal Government a royalty, if you will, that is a matter of number crunching. That is just something that you can compute. I think that is what we ought to be talking about and then devolution is complete and you have the States move to administer these, particularly the mineral estate.

Ms. CUBIN. Are the members of RMOGA willing to pursue other alternatives? Obviously, as you said, that you would like total transfer or just improve the current system. I mean here is the deal. I come from a family of seven children and, you know, we all had seven different opinions and we were always right and I loved all of them and I feel somewhat that way about this situation.

I have people that I have philosophically been aligned with through the years and in lots of other ways and there seems to be a major difference. And I wonder do you think there really is any willingness to try to work together to achieve this or do you think maybe it is better to not achieve it at all?

Mr. BELTON. Well, first of all, there are a number of different proposals that I just became aware of in the last few days and I do not want to create a knee jerk reaction. These are things that need to be taken very seriously because in my opinion they are very complex issues. For example, in transferring the Federal functions to the States completely, you would then dispose of a couple different legal frameworks.

You would be disposing of FLPMA which has to do with land management planning functions. It also would be disposing of the Mineral Leasing Act, as I understand it, which is a Federal leasing law because now you would have the minerals, the management of lands, the collection of royalties and all of that under the authority and control of the State.

Currently in the State of Wyoming under the State Land Commission the royalties are one-sixth, they are not one-eighth. The lease terms are five years, they are not 10 years. Actually the terms are not as favorable, I guess, as they would be on a Federal lease, so if you look at it from that perspective, you know, I would have some concerns just as an oil company in terms of profitability or the feasibility aspects of it, so I think that is part of it.

The other part that would definitely need to be addressed is, is the State really ready to take on land management planning? Are you really ready to take on NEPA, compliance with NEPA and do all the environmental impact analysis, pre-lease, and so forth and so on? That is a very complicated issue that I do not think anybody can really answer today.

I think that needs some study and it may require industry to get together with the Federal Government and the States and talk about some of those kinds of things. I am just not prepared to come forth with a position at this point. I need to study that.

Ms. CUBIN. I will ask Mr. Nichols this question. I understand that industry had an interaction, some kind of a meeting with an MMS reinvention team to recommend streamlining by combining all minerals activities into a single bureau and then that bureau would deal with only mineral issues. Have you been able to obtain a copy of that study from the Department?

Mr. NICHOLS. Are you referring to the negotiated rulemaking that has been going on with regard to trying to add clarification to the way gas valuation is done?

Ms. CUBIN. I do not think so. What I am referring to, as I understand it anyway, and maybe it is a misunderstanding, but that there was what was called reinventing government proposal that included reinventing MMS.

Mr. NICHOLS. Yes, the REGO II, I think, as it is called. There are a variety of things in there some of which we applaud. I think those are addressed in the detailed testimony of both me and the other witnesses.

Ms. CUBIN. OK.

Mr. NICHOLS. There are some things in there that we applaud and there are some things in there that we object to.

Ms. CUBIN. OK, good. I did not know if that was in your testimony or not. OK, thank you. I do not think I have any other questions, Mr. Chairman.

Mr. CALVERT. Thank you. I want to thank you for your testimony and to all the panels testimony today. It has been an informative hearing. Certainly we have a ways to go before we have final recommendations as to the future of MMS. I do not believe the Administration proposal will work in my mind and I get the opinion that they may agree.

However, we do need to do a better job, whether we transfer all of the mineral activities into a single bureau or we transfer the land and the activities of mineral collection to the States and the responsibilities that have been referred to as inherently Federal activities.

But we intend to stay in touch with all of you and we hope that you will stay in touch with us and hopefully by the end of summer we can come up with some concrete proposal. So again I thank you very much and have a good day.

[Whereupon, at 5:02 p.m., the subcommittee was adjourned, and the following was submitted for the record:]

Testimony of

Sylvia Baca
Deputy Assistant Secretary, Land and Minerals Management
United States Department of the Interior

Before the

House Resources Committee
Subcommittee on Energy and Mineral Resources

June 8, 1995

Mr. Chairman and Members of the Subcommittee, thank you for the opportunity to appear before you to testify on management alternatives for the Bureau of Land Management and the Minerals Management Service (MMS) with regard to mineral leasing, operation and royalty management. I understand that the emphasis of today's hearing pertains to management alternatives with respect to **onshore** minerals. Accordingly, I will focus the majority of my remarks in that area.

This hearing, and the issue it is intended to address, is a timely one. There is general agreement that the old ways of conducting the public's business through Federal government programs must be thoroughly analyzed, reinvented, and in some cases, abandoned. We cannot and should not be content to rely on the practices of the past to work in the 21st century. Furthermore, the general public has indicated its desire to see a government that is responsive, yet leaner.

Given our desire to respond to changing needs and legitimate requests of the public we serve, both the Department and the Administration have embarked upon an unprecedented effort to restructure government. Recently, under the Administration's REGO II effort, the Department proposed significant shifts in several of the programs under its purview representing the Department's best assessment of how to perform its core functions.

With those general remarks as background, I would now like to turn to the subject of today's hearing. Understandably, a portion of my remarks will focus on the REGO II proposals for the BLM and the MMS. However, I would also like to touch briefly on some other initiatives that we are undertaking to operate more efficiently while enhancing service to our regulated community and other constituencies.

PROPOSAL WITH RESPECT TO THE MINERALS MANAGEMENT SERVICE

As you are aware, MMS is responsible for managing two major programs--the Royalty Management Program and the Offshore

Minerals Management Program. Although the recent Departmental REGO II proposal addressed both programs, I will limit my remarks to the proposal to consult with States and Indian Tribes on a possible devolvement to state governments of the responsibilities of the MMS for the management of **onshore** mineral revenues.

On March 27, 1995, the President proposed this consultation as part of the National Performance Review's Phase II. The proposal was based on the belief that some of the functions of the MMS can be performed more efficiently at the state and tribal levels.

Specifically, the proposal recommends consulting on the issue whether the royalty collection program for onshore Federal lands should be transferred to the States and for Indian lands to Tribes. The responsibilities to be transferred would include all royalty collection functions except those that are inherently Federal, such as enforcement of lease terms, issuing final policy and regulations, determining value for royalty purposes, and adjudicating appeals. The transfer of the royalty collection process to the Tribes would be accomplished by compacting the royalty functions under the Self Governance Act to interested Tribes.

It should be emphasized that the MMS proposal is a proposal to consult regarding the elimination of MMS. While the Department proposed a specific scenario with associated cost savings to devolve royalty management-related functions, it also is cognizant that affected States, Tribes, and other affected parties may recommend a different approach. We are open to discussing different approaches if they can achieve an equivalent level of cost savings.

At this time, we are in the process of undertaking extensive consultation with affected parties. Specifically, we have sent the devolution proposal to the Governor of each State receiving revenue from Federal mineral leases and to Tribal leaders and Indian allottee associations with mineral leases. We are also seeking input from industry. We will be able to put more specifics to the proposal after we have consulted and received the views and ideas from these affected parties.

We plan to meet with representatives of the interested States, Tribes, allottee associations and industry associations in July in order to provide more information about the proposal, respond to initial comments, explain our process for future consultations and discuss other alternatives. This meeting would be followed by additional sessions in late summer as needed.

The cost savings associated with the devolution proposal is an extrapolation assuming all 38 States and Tribes are willing to accept royalty collection functions based on the proposal submitted to the House Natural Resources Committee in July 1993 by then-Governor Sullivan of Wyoming. It calls for a simplified and redesigned royalty accounting system which is included in the devolution proposal. This redesigned accounting system is estimated to cost almost $65.5 million to design and transfer to States and those Tribes accepting the royalty accounting functions--approximately $16.1 million will be needed to develop a new system and approximately $49.4 million will be needed for system implementation and start-up costs. However, for those Tribes that decline to assume these functions, it is the Department's intent to provide to those Tribes the same level of service that is currently provided.

The savings to the Treasury described in the proposal assume all States and Tribes will take over the royalty function and also is predicated on an increase the cost recovery provisions (net receipts sharing) of the mineral leasing administrative program costs to 50 percent from the current 25 percent that was included in the Omnibus Budget Reconciliation Act (OBRA) of 1993. Legislation will be needed to change current provisions in the Federal Oil and Gas Royalty Management Act and the OBRA and to enact appropriations consistent with the proposal. Overall, the proposal is estimated to generate net savings of $59.8 million over a four year period.

Significant segments of the oil and gas industry have raised concerns about the elimination of MMS. Their concerns focus on the increased regulatory burden of having to deal with multiple states and absorption of the offshore program into a large agency that lacks mineral expertise.

Many states, while philosophically supportive of a greater state role, have expressed concern about performing ministerial functions for the compensation included in the proposal. They are more interested in the functions which have been determined to be inherently Federal functions. Tribal leaders have raised concerns about being provided the same level of service as is currently the case with MMS.

<u>Ongoing Efforts to Simplify Royalty Management</u>

Even before the Department announced this proposal to consult on the issue of devolution, the MMS was committed to reducing the costs of collecting royalties. As part of the National Performance Review-Phase I, led by Vice President Gore, the bureau initiated a number of actions to simplify the valuation of gas production and reduce the overall costs of compliance.

Royalty collections are based on three elements: royalty rates, amount of production, and value of production. Valuation is by far the most controversial of the these elements. Because producers have a multitude of different types of contracts for selling their gas, it is often difficult to determine exactly how much the producer received for minerals extracted from Federal lands and to ensure there were no deductions from the royalty value for services that are the sole responsibility of the producer. This is further complicated by the existence of many non arms-length contracts, where MMS cannot simply assume that the price a purchaser paid to an affiliated producer is an accurate measure of value.

Resolution of issues relating to valuation often lead to costly administrative appeals and litigation. If we can simplify the process for the valuation of gas production in a way which is fair to industry and the revenue recipient, we can reduce the overall cost of royalty management. The following initiatives represent some of the most important actions we have started to accomplish this goal.

Negotiated Rulemaking

Federal Gas Valuation Negotiated Rulemaking Committee

In February 1995, the Federal Gas Valuation Negotiated Rulemaking Committee completed its negotiations on how royalties should be paid on natural gas produced from Federal leases. Specifically, the Committee's negotiations focused on improving the methods for valuing gas sold to affiliates, gas produced from unitized and communitized leases, and gas sold remote from the wellhead under the new marketing environment brought about by Federal Energy Regulatory Commission Order No. 636 (Order No. 636). The culmination of these negotiations is a series of recommendations that should improve and simplify the payment of royalties as well as help save both the government and industry administrative costs.

The Secretary chartered the Committee effective June 27, 1994, although discussions began in December 1993. The Committee represented a diverse cross-section of MMS's constituents, including States, major oil and gas companies, marketing companies, large independent producers, and small independent producers, as well as representatives from MMS. Decisions and recommendations were reached by consensus; that is, all recommendations needed the support of each Committee member for approval. The Committee operated under the Federal Advisory Committee Act, but generally followed the guidelines of the Negotiated Rulemaking Act. Meetings were held publicly and recorded for the public record. A final report containing the Committee's recommendations is also available to the public.

The Committee set out specific objectives for developing improved and simplified methods for valuing natural gas. These objectives were to:

(1) provide certainty to both producers and government auditors in determining value;

(2) facilitate timely and accurate remittance of royalties;

(3) use information to which the producer has access; and

(4) provide administrative cost savings to all parties.

The Committee's recommendations may provide the certainty and simplicity sought by MMS's constituency.

- The option to allow producers to use published index prices could result in simpler and more definitive royalty values closer to the wellhead. Index prices are published monthly, are specific to each pipeline, are readily available to the public, and represent sales closer to the wellhead than those typically occurring under Order No. 636.

- For processed gas, producers may have the option to value their gas at the wellhead, eliminating multiple line reporting and complex downstream computations.

- For unitized and communitized leases that involve multiple royalty owners, producers would simply pay royalties based on their ownership interest in the lease. Complexities associated with tracking where the gas actually went and who sold it would be eliminated.

- For independent producers not wishing to use index prices, the recommendations allow them to continue using their sales proceeds. For qualifying small producers in unitized and communitized leases, a waiver would allow them to pay on actual sales interest-free for one-year.

- For all producers recommendations may remove some regulatory burdens:
  (1) the preparation and filing of gas transportation allowance forms and processing allowance forms;

  (2) the reporting and valuation of natural gas liquids in most areas, including the calculation of a processing allowance;

  (3) the requirement to dually account for Federal gas;

  (4) ambiguities in determining allowable gathering and compression; and,

(5) obstructions to using third party transportation rates and regulatory tariffs.

Indian Gas Valuation Negotiated Rulemaking Committee

In January 1994, MMS formed the Indian Gas Valuation Study Group. Throughout 1994, MMS met with representatives of several Tribes and allottee associations. The MMS used an informal study group format to obtain and clarify varying viewpoints. Discussions focused on methods of improving regulations implementing the specific Indian lease term requirements concerning major portion analysis and dual accounting. The MMS published the first work product of the study group on August 4, 1994, an Advance Notice of Proposed Rulemaking soliciting comments on new methodologies being considered to establish value of production from Indian leases.

The Committee, chartered on February 1, 1995, grew out of the Indian Gas Valuation Study Group. It is comprised of representatives of MMS, Bureau of Indian Affairs, Indian mineral owners and their representatives, and the oil and gas industry. The Committee has met three times. Much progress is being made in the areas of major portion analysis, dual accounting, gross proceeds, and transportation allowances.

The Committee is currently working on a formula to value gas produced from Indian lands using publicly available spot market index prices and a discount factor. The formula-derived price would be applied to the wellhead MMBtu volume and would be used in lieu of gross proceeds and major portion calculations. Under this scenario, filing of forms for transportation allowances would not be necessary. The Committee is also working on a formula-based valuation method in lieu of dual accounting calculations. Less paperwork and fewer reporting requirements for industry mean less administrative oversight by the government.

The goal of the Indian Gas Valuation Negotiated Rulemaking Committee is to publish regulations that will maximize royalty revenues for Indian tribes and allottees while streamlining administrative activities. The regulations will also satisfy the oil and gas industry by being clear, economizing on the information needed by a lessee to properly compute royalty, and making it easier for a lessee to comply in a timely manner.

The Committee is confident that it will reach consensus on a valuation method and royalty collection procedure that benefits the MMS, Indians, and industry by assuring:

- Fairness
- Simplicity
- Predictability
- Adaptability
- Maximization of revenue consistent with laws and lease terms
- Timely Compliance (certainty and closure)
- Ease of administration
- Enforceability
- Consistency with market
- Availability of data
- Longevity

Gas Production Taken in-Kind

The MMS has initiated a Royalty Gas Marketing Pilot, currently underway in the Gulf of Mexico. Although the pilot involves only offshore leases, we may be able to institute similar programs onshore in the future, and therefore are bringing this pilot to the Committee's attention today. The purpose of the pilot is to streamline and simplify the royalty collection process by taking the Federal royalty share in-kind. In light of the potential benefits offered by this new approach to royalty collection, the Department officially designated the pilot as a National Performance Review Laboratory in 1994.

Under the pilot, MMS takes the Federal royalty share of gas production from 77 volunteered leases (representing approximately 8 percent of the gas in the Gulf of Mexico) and immediately sells it to 13 competitively chosen marketers. The pilot is scheduled to run from January 1995 through December 1995. Potential benefits of the pilot include:

- Lessees will no longer determine the value of production for royalty purposes.
- Lessees will no longer have to submit as much information as they would on the normal royalty report.
- Audit streamlining will occur, a simpler compliance system will be created and there should be reduced litigation.
- MMS auditors or systems processing will only be responsible for confirming the delivery of the Federal royalty share of gas production to the marketer.
- Administrative costs should be reduced for both industry and MMS.

The MMS will conclude its evaluation of the pilot by mid-1996. The focus of the evaluation will be on revenue neutrality and the administrative cost savings of taking royalty in-kind. The MMS will make a decision if it should extend the pilot with differing features in 1996.

Royalty Fairness Issues

In addition to improving on the way we do our royalty management activities, we are also interested in being fair to industry and have tried to improve on the timeliness of our compliance reviews.

Contemporaneous Audits

The MMS began a Contemporaneous Audit Initiative in the fall of 1988 in an effort to become contemporaneous in its audit efforts. This required an accelerated audit effort to finish off old, unaudited periods. That effort was successfully completed in November 1992. Completion of that effort means that it is now feasible for field audit personnel (Federal, state, and tribal) to engage royalty payors and complete audits within a 6-year period.

Companies with audit teams in residence (now the 11 largest companies) and major payors (now 111 large companies) targeted for audit are responsible for paying about 87 percent of all mineral revenues on Federal and Indian leased lands. The current audit strategy for the 11 largest companies is to audit the 3-year period October 1989 through September 1992 within a 3-year period ending September 1995, completing the audit cycle within 6-years.

For the 111 major payors, the current strategy is to audit a 5-year period in 1-year. Thus, for one-fifth of the major payors, MMS will complete audits by September 1995 for the period 1989-1994. In October 1995, MMS will begin audits of a different one-fifth, covering the 1990-1995 period. This policy is consistent with the record retention policy of the Federal Oil and Gas Royalty Management Act.

Contract Settlement Audits: The majority of these audits are also being accomplished within 6-years of when payments are believed to have passed from purchasers to royalty payors. However, we have often found that settlements dated in the early to mid 1980's contain provisions for allocation of proceeds to future production in periods of current audit coverage. These settlements must be reviewed to make such determinations. Accordingly, some payors have been engaged for audit or have been asked to provide records for periods extending beyond 6-years.

Except for the contemporaneous audit effort, the few contract settlement audits which require reviewing records older than 6-years, and potential findings associated with companies' use of posted prices to value California crude oil, we are considering issuing further guidance to MMS auditors that they should limit their bills and orders to no longer than six years back from the date the royalty is due.

Interest on Royalty Overpayments

The MMS is undertaking several initiatives to improve on the way it conducts the public's business, and is committed to continual improvement.

PROPOSALS WITH RESPECT TO THE BLM

I will now outline the proposals contained in Reinventing Government (REGO II), as well as the final report of the Onshore Oil and Gas Performance Review.

BLM's Plan for REGO II Proposals

Pursuant to REGO II, the BLM will consult with the States and Indian Tribes on the proposal to transfer certain oil and gas inspection responsibilities to the States and Native American Tribes, and cost recovery for pre-lease and post-lease energy and minerals programs.

Transfer of oil and gas inspection and enforcement

REGO II proposes that the BLM transfer certain oil and gas inspection and enforcement responsibilities regarding production verification and surface compliance in the Onshore Oil and Gas program to individual States and Native American Tribes. This proposal will eliminate duplication of efforts by State and Federal governments, and promote tribal governments' involvement in the management of their oil and gas resources. The BLM is forming a Consultation Task Force consisting of State, Tribal and Federal representatives to establish the initial ground rules surrounding the transfer to the States and Tribes. The joint Task Force will complete its analyses and prepare an report for the BLM Director no later than October 1, 1995. Letters have been sent to Governors and Tribal Chairmen requesting the names of their representatives for the Task Force.

The Task Force plans to have several meetings to develop options and to draft a report with recommendations on the transfer of the inspection operations. The Task Force will be instructed to implement an outreach and consultation plan, which includes the general public, Tribal governments, constituents in the industry, environmental and other interest groups, and local and State governments. The draft report will be distributed for review and comment. After comments are received and analyzed, the Task Force will prepare a final report with recommendations.

The BLM would not require legislation to implement this proposal. Current authority exists under Section 205 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), P.L. 97-451, to delegate the inspection and enforcement program to the States. Tribes are eligible to contract for programs through the Indian Self-Determination Act and the Tribal Self Governance Act of 1994. Currently, there is no mandate to require either the States or Tribes to accept this inspection responsibility.

The Task Force will analyze the regulations at 43 CFR § 3190, et seq., which provide for delegation of authority of oil and gas inspections mandated under FOGRMA cooperative agreements with States and Tribes. As determined by the Consultation Task Force, there may be modifications to certain oil and gas operating orders to insure oversight and consistency with respect to the inspection and enforcement standards. In addition, the Task Force will analyze the regulations at 25 CFR § 211, which apply to Tribes.

The BLM estimates that most of the federal employees affected by this proposal would be the Petroleum Engineering Technicians and their support staff. A buyout opportunity was made available to these groups, and eighty-five people have elected to take the buyout opportunity. These employees are scheduled to leave Government service on March 3, 1997. The estimated cost savings over five years, beginning in FY 1997, is $9,000,000 and 99 FTEs.

Cost recovery for pre-lease and post-lease programs

Extensive pre-leasing activity is necessary for oil and gas operations. These activities include analyses required by the National Environmental Policy Act. Individual leases may require environmental analyses and land use planning decisions informing the agencies and the public of potential effects of the proposed leasing action on the environment. The BLM currently recovers some costs under some circumstances. Under the REGO II pre-leasing proposal, the BLM will analyze and identify the costs necessary to perform these analyses, and will seek to recover those costs from the industries benefiting from the leasing actions.

The BLM also incurs administrative costs from actions necessary to conduct mineral operations. These administrative costs include, but are not limited to, preparation of licenses, permits, and other land use authorizations individuals and companies need to use the public lands. Currently, charges are imposed for several of these land uses, but are outdated and must be revised to meet present circumstances.

The cost recovery for NEPA compliance will be significant. In our REGO II proposal, we estimate that the BLM spends approximately $6,000,000 on prelease NEPA compliance. Postlease NEPA compliance is substantially less, as the prelease work generally provides the basis for postlease analysis.

A cost recovery Consultation Team has been established to review and analyze the way BLM processes land use applications, and monitors the land uses, the fees charged to process and monitor the actions, and the financial systems BLM uses to distribute the collected fees. The analysis will identify the strengths and weaknesses of the existing program. The goal of the re-engineering initiative is to build upon the strength of the existing programs, while eliminating weaknesses and adding other attributes to make the system more effective to users of the public land and fairer to the American taxpayers.

Due to current legislative authorities, the team does not foresee a need for legislation in this area. The team expects to re-engineer the existing cost recovery processes by regulatory and internal directive changes. Major changes to the regulations and other internal directives that currently directs the cost recovery efforts would be needed if costs for administering land use authorizations are to be appropriately and efficiently recovered. The appropriate changes to other BLM directives would follow the finalization of the regulations.

The reinvention measures are designed to reduce dependency on appropriated monies for processing land use authorizations.

Ongoing efforts to improve management of onshore minerals

Even before the Administration and the Department of the Interior announced the REGO II proposals, the BLM was committed to identifying ways to improve the management of the public resources and providing improved services to all of its stakeholders.

BLM Performance Review

The BLM Performance Review (BPR) was initiated in late 1993 to review oil and gas program operations, regulations and policies, and to identify opportunities to improve the way BLM provides service to its customers. The review culminated in the establishment of issue resolution teams and process review teams comprised of BLM staff and personnel from other federal agencies.

These teams were asked to develop recommendations for innovative changes to improve BLM's ability to manage oil and gas resources while sustaining the health, diversity and productivity of the public lands for the use and enjoyment of present and future generations.

The final report of the BPR was issued on April 27, 1995. The report recommends numerous changes to the BLM's oil and gas program. The next task for the BLM is to review the recommendations. Some of the options are short term; others require more time. Some options will be more popular than others. All of the options should improve the way the BLM conducts its oil and gas business by improving the quality of decisions to lease, providing incentives to industry for increased production, reducing unnecessary paperwork and duplication, holding industry accountable for environmental problems it creates, maintaining the health of the land, improving BLM's on-the-ground monitoring efforts, and ensuring continuous public and industry participation in finding improvements to the way business is done.

I will now outline some of the specific recommendations contained in the report.

Royalty rate relief and reductions

The report recommends that the BLM consider royalty rate reductions for high operating cost wells, such as those with a high water cut. The granting of royalty rate reductions on a case-by-case basis is also recommended for enhanced recovery projects. The enhanced recovery project must be capable of producing additional reserves not recoverable under existing operations. The report also recommends that the BLM grant royalty waivers on a case-by-case basis for drilling wildcat and deep wells, for drilling horizontal or directional wells, or multiple wells from a common drill pad. Further, the BLM will consider eliminating the minimum royalty provisions on leases qualifying for the stripper well royalty rate reduction program. All of these proposals have been or are being studied to estimate the effect on Federal and State revenues. Once the analysis is complete, a determination will be made of which, if any, royalty rate relief/reduction scenarios is adopted for rulemaking.

Environmental compliance self-certification

The report recommends that the BLM establish a one-year pilot program to allow industry to self-certify environmental compliance in an area office, such as the BLM's Buffalo Resource Area of Wyoming. The BLM Wyoming State office would then do an analysis of the pilot program, and devise a policy that can be adapted in other offices. The pilot would be limited to operators with a history of compliance.

Responding to cumulative impacts

The report recommends that this effort be used as a model to incorporate analysis of cumulative impacts. This will allow the BLM to: (1) test the BPR recommendations under field conditions; (2) refine its planning techniques; (3) evaluate proper use of mitigation measures; and (4) improve the quality of post-lease monitoring. A key element of the effort will be to include the concept of "net effect" into the concept of cumulative impacts.

Streamline the unitization process

The report recommends that the unitization approval and administrative process be streamlined and simplified. This would save operators and the BLM time and money, and provide flexibility to operators.

Reducing or eliminating unnecessary costs to operators

The report recommends that the BLM identify policies and regulations that impose unnecessary costs to the operators and can be resolved by reinterpretation, waiver, or a variance, without compromising the intent of the regulations. The report further recommends that, in conducting this review, the BLM solicit input from local oil and gas trade associations.

Bonding and unfunded liability recommendations

There are several recommendations to improve the Government's ability to reduce its liability in the event of bankruptcies or operators who abandon the site, while at the same time reducing costs to industry. The BPR recommends that the BLM eliminate or minimize duplicate bonding between State and Federal agencies, revise assignment forms to more clearly lay out the relationship between assignor and assignees, provide for selective increases in bond amounts when a situation so warrants, develop an improved data base on shut-in wells, and adopt a new policy to reassess risk and bonding needs prior to assignments.

BLM Performance Review implementation

The initial implementation phase may begin on several of the proposals, including options which can be accomplished within the framework of existing statutes, options which have a relatively high degree of consensus support or the absence of opposition from any one group of stakeholders, options which will have a substantive impact on our ability to better serve our stakeholders, and options which can be implemented within a time-frame of four to twelve months.

CONCLUSION

Both the REGO II and the streamlining initiatives discussed above are being pursued by the BLM and MMS in a manner which includes the American people. The goal is to make these programs more efficient by improving the way we do business, ensuring the timely collection and distribution of mineral revenues to the States, tribes, allottees and U.S. Treasury, reducing unnecessary paperwork and duplication, maintaining the health of the land, and ensuring continuous public and industry participation in finding improvements to the way business is done.

Mr. Chairman, this concludes my written testimony. However, I will be happy to address any questions you may have at this time.

TESTIMONY OF THE STATE OF WYOMING CONCERNING THE MANAGEMENT OF ONSHORE FEDERAL MINERAL ACTIVITIES

Before the
House Committee on Resources
Subcommittee on Energy and Mineral Resources
Ken Calvert, Chairman
June 8, 1995

I am Jim Magagna, Director of Federal Land Policy for Wyoming Governor Jim Geringer. I am also Director of the State Lands and Farm Loan Office, which collects mineral royalties from State land. I am here today representing the State of Wyoming. Thank you, Mr. Chairman, for providing the State of Wyoming with the opportunity to testify here today. More minerals are produced from federal land in Wyoming than from any other state, and we are vitally interested in proposals which affect those mineral properties.

Wyoming firmly believes that it can do an efficient and effective job at collecting royalties at less cost to all entities involved. It has a proven track record at collecting royalties on state lands. We are the largest player in this discussion, but we are also sensitive to the issues that devolution might create for smaller producing states and welcome participation from every state involved. Wyoming would be pleased to act as a leader and facilitator. The question of costs associated with MMS collection and related functions has been on the table for years. It is time to craft a solution that will benefit the states and the federal budget.

First, I will briefly comment on the Department of Interior's *Proposal to Devolve the Responsibilities of the Minerals Management Service* dated March 27, 1995. Under the Proposal the MMS would transfer to the states the responsibilities associated with collecting royalties but none of the authority which must accompany the responsibility. It is obvious that MMS believes that few of the functions are delegable. The States would have no policy making ability, no rule making authority, no funds management authority and no enforcement authority. However, the proposal advises that a financial penalty system may need to be developed and applied to states that do not collect all royalty due in a timely manner. This is obviously unacceptable. It is also our understanding that a part of the takeover would involve inspections and enforcement currently performed by the Bureau of Land Management. We have no information which defines what those responsibilities will be, how they will be paid for or what oversight will be imposed.

The Proposal draws on a study conducted for Wyoming in 1993 by Arthur Andersen Consultants. The 1993 Wyoming Plan has limited applicability today and does not represent the Geringer Administration's views on a proper devolution. The MMS uses estimated figures from the Wyoming Plan to make further projections. The subsequently implemented Wyoming automated system of mineral tax valuation and collections would change the assumptions in the Wyoming Plan and in the MMS Proposal.

Wyoming urges that the March 27, MMS Proposal be quickly discarded in favor of a plan drafted by the affected states.

The thirty eight states which receive MMS mineral royalties have a varying degree of interest in taking over the MMS function, particularly the states which have relatively small collections. Several of these thirty eight states began their dialogue last month, and a variety of ideas have been discussed. For example, perhaps the minerals should be deeded to those states which receive relatively small amounts of federal mineral royalties, while conveyance of the minerals to states which produce large amounts of minerals should be accompanied by an overriding mineral royalty. Under this scenario, there would be no inherently federal function to blur lines of authority between the federal and state government; the states would own all the minerals, perform all the functions, and the federal government would simply get a royalty check each month. Another possibility is for the states to develop a uniform reporting and remittance form and procedure. The most fundamental issues to be resolved involve what an Interior Department Solicitor deems constitutional limitations. Those most certainly must be addressed as the first items for agreement.

In any event, this is a formidable task and the states and the royalty payers need sufficient time to reach a consensus and a course of action. Wyoming is committed to this project and intends to retain a project manager to work with the other states and the affected industries.

The primary role of the MMS should be to serve as a resource to the states in the development of a plan and, following adoption, to effectuate an orderly transfer of authority and operations. Currently if our reports are correct, the primary role of the MMS is to lobby this Congress against devolution in conjunction with some of the major oil and gas producing companies. It seems to be a conflict, or at the very least, disingenuous, to have an agency which is hostile to the notion of devolution as the shaping force behind the debate.

The State of Wyoming would be pleased to continue our dialogue with the Department of Interior and will participate at every opportunity, but we believe the appropriate next step is for the States to work together through the National Governors Association, Western Governors Association and the Interstate Oil and Gas Compact Commission to develop a plan which is acceptable to the States and to the producers. The collective efforts of the States will begin to take shape this month, and we look forward to involving the Department of Interior at such time as the states deem proper.

We in Wyoming envision a system which is developed jointly by the affected states with strong input from industry - a system which is simple, efficient, less costly and more innovative. The states, collectively, must have the freedom to make acceptable choices and the authority to implement the agreed upon system.

Our objectives are simple: design a uniform system which can be used by all participating states; lower collection and record keeping costs for both government and industry; uniformity between federal and state land systems, which can eliminate duel royalty and severance tax reporting and increase efficiency for royalty payers; and in the process, foster a renewed sense of state responsibility and ability in the management of mineral resources for the benefit of the states, the federal treasury and the mineral industry.

Again, thank you, Mr. Chairman, for allowing the State of Wyoming to participate in this hearing today.

STATEMENT OF
INTERSTATE OIL AND GAS COMPACT COMMISSION
TO THE UNITED STATES HOUSE OF REPRESENTATIVES
SUBCOMMITTEE ON ENERGY AND MINERAL RESOURCES
COMMITTEE ON RESOURCES
June 8, 1995

Mr. Chairman and members of the Committee, I am Christine Hansen, Executive Director of the Interstate Oil and Gas Compact Commission. I am pleased to present the following comments on behalf of the Commission and its Chairman, Governor Ed Schafer of North Dakota.

I am honored to be with the Subcommittee on Energy and Mineral Resources this afternoon and appreciate an opportunity to discuss the approach that states are taking to the Administration announcement that onshore royalty collections now handled by the Minerals Management Service (MMS) will be transferred to the states by the fall of 1997. In particular, my testimony will focus on the analysis being conducted by the states and will discuss the positive attempt the states are making to do an honest analysis and propose workable solutions.

I am pleased today to be representing the thirty-five states which make up the Interstate Oil and Gas Compact Commission (IOGCC). The bulk of the royalty collections under consideration to be transferred to the states stem from production of oil and natural gas. However other collections are also involved -- from hot water in California to quartz crystals in Arkansas to purge liquor in Wyoming to an unknown substance in Wisconsin. The IOGCC is an unique entity suited to coordinating the state responses because of its "compact" nature.

As this subcommittee is well aware, interstate compacts are a special legal organization authorized by the United States Constitution (Article I, Section 10). The IOGCC is one of the earliest compacts, and one of the largest today. The vehicle of a Congressionally approved Compact to assist in the regulation of oil and gas was first recommended to the producing states in 1929 by then President Herbert Hoover. Groups of governors held a series of meetings over the next several years, and were pressed by President Franklin Roosevelt to initiate action forming a Compact, or face federal regulation of oil and gas.

The IOGCC was created in 1935 by a group of oil-state governors who strongly believed that regulation of oil and natural gas should be the exclusive purview of the states and not of the federal government. These governors were dedicated to the principles of petroleum conservation. In 1935, domestic petroleum supplies were at a surplus level and production was out of control. It had been out of control for several years, and the U.S. Department of the Interior was urging the President to move on a plan which would transfer all control over exploration and production of oil and natural gas to the federal government. President Roosevelt called the newly elected Oklahoma governor -- E.W. Marland -- and urged him to immediately assemble interested governors and approve a formal compact.

The Compact grew out of a recognition by these governors that voluntary agreements among producers were not working and a recognition that the way to prevent federal control of the industry was through joint state action. New Mexico was the first state to ratify the Compact after it was approved by Congress in the fall of 1935. The governors believed then, and our current member state governors believe now, that states had and continue to have an obligation to prevent avoidable waste of oil and gas, and that states acting cooperatively are as capable of solving multi-state problems as the federal government.

The IOGCC states have been working to analyze the MMS takeover issue since the March 27, 1995, announcement by President Bill Clinton that as part of the Department of the Interior's initiative to "reinvent government," the MMS would be eliminated and the Administration will consult with the states and Tribes to determine how onshore authorities can be transferred to the states and the Tribes, resulting in saving $69 million and eliminating 708 full time federal jobs over a five-year period. Early in the year when I had heard that this proposal was circulating within the Department of the Interior, I asked that the states be consulted prior to any announcement. Had the states been involved at an earlier phase, they would be much further along in their internal and joint analysis of the plan and in "how onshore authorities can be transferred to the states..."

It is important for this committee to understand that this proposal did not come from the states, but that the states are not rejecting it out-of-hand. Former Wyoming Governor Mike Sullivan (also a former chairman of the IOGCC) was an advocate of Wyoming taking over royalty collection, as this committee knows. The analysis of his administration was that Wyoming could handle the function in a more cost effective way. The current Wyoming administration (as you have heard this afternoon) is also of that general belief, and is diligently working on a proposal which would result in President Clinton's directive becoming a reality.

Individual producing states are in the process of internal analysis and are beginning the process of coordinated analysis of this plan. Interior Secretary Bruce Babbitt said on March 27 of this year that the transfer to states of the on-shore MMS royalty collection function came about after a "rigorous review of the eleven bureaus and offices within the Department," having reached the conclusion that the MMS royalty collection program can be "handled more efficiently by state government." The states of the IOGCC generally believe that guiding principle to be true -- we do believe that we are more efficient than the federal government or we would not have fought for sixty years to retain oil and gas regulatory jurisdiction at the state level. Secretary Babbitt said that the Department of the Interior should focus on "core functions" and that analysis led to the decision to move this function to the states.

However, on this issue, the states have not yet developed individual proposals nor have they begun the work of coordinating individual proposals into some unified proposal. IOGCC Chairman, North Dakota Governor Ed Schafer has appointed a "Governors' Committee" headed by Wyoming Governor Jim Geringer and Nevada Governor Bob Miller. The support group to the Governors' Committee is a Steering Committee under the direction of the IOGCC Public Lands Committee co-chairmen -- Richard Griebling of Colorado and Pary Schofner of Oklahoma. The Steering Committee consists currently of 30 volunteers from state government, trade associations and industry (both independents and majors). I have attached a list of current members for the information of the committee. Membership on the Steering Committee is open to all interested in participating. All meetings of the Steering Committee (as with all IOGCC meetings) are open to anyone wanting to attend and the structure of IOGCC meetings generally lends itself to anyone in attendance participating, though only committee members may vote on issues.

In addition, each IOGCC member governor has been asked to designate a small group of state employees to evaluate the state's internal ability to assume these royalty collection functions and to develop a position on their interest in assuming these functions. The individual state team members have begun to talk to their counterparts in other states to compare information -- finance person to finance person, land office person to land office person, etc.

The IOGCC Governors' Committee has also recognized the need to address the issue of royalty takeover in two separate directions -- one from the view of the states with larger collections of royalties and one from the view of states with collections which are insignificant in terms of the overall budget of that state. In this regard, Governors Schafer, Geringer and Miller have called the governors in the states with the relatively smaller royalty collections and requested that they each designate a representative to work with the IOGCC to fashion recommendations which would address the needs of those states. This group will be headed by Don Mason of Ohio, chief of the Division of Oil and Gas in the Department of Natural Resources.

The small royalty collections pose a real opportunity for Congress -- even apart from how you chose to deal with this recommendation of the President's. The Department of the Interior has reported that royalty payments were distributed to 38 states in 1994, though that accounting is not yet available. The most recent published accounting, that for 1993, reflects payments to 35 states. A new release of the Department dated April 17, 1995, reports first quarter royalty distributions to 34 states -- including a payment to Tennessee of $57.46. Perhaps there is a something else the federal government could do with that Tennessee leasehold than collect a royalty, process it, audit it, and split the net with the state amounting to $57.46. It might be more cost effective to give the lease to Tennessee. Using Tennessee as an example, the Mineral Revenues for 1993 publication of the Department notes that from 1920 through 1993, a total of $14,000 was distributed in minerals royalties to that state.

The IOGCC group of states with smaller federal royalty interests will strive to make some creative alternatives to extensive collection and audit procedures currently required of the Department of the Interior. At a time when the Department is advocating a plan to sell the huge off-shore minerals stream, it seems especially incongruous to advocate continuing to collect these small dabs of royalties -- and require states to establish collection and audit methods for them, complete with threats to fine the states if they do not collect the $57 to the satisfaction of the Department of the Interior. Surely there is a superior way.

In finding that superior way, Congress, of course has complete discretion. You are not bound by the laws you wrote in the past -- you are able to write new laws. The excellent opinion of the Office of the Solicitor, Department of the Interior, dated December 16, 1994, dealing with "Inherently Federal Functions" is a fine description of the limitations on the flexibility of federal agencies and the requirements placed on federal agencies in carrying out the laws passed by Congress. We need not argue with the conclusions of the opinion -- we need only say that the basis for the opinion is law written by Congress, and Congress can change the law. The President has already expressed his desire that this transfer of royalty collection responsibility take place, thus signaling his willingness to sign a Congressional initiative which would accomplish that end.

I have not taken the time to do a detailed legal analysis of the above mentioned opinion, because the base assumption is clearly set out in the opinion -- Inherently governmental or Inherently federal tasks are determined by looking at laws passed by Congress. (By way of information, I have a J.D. degree from Drake University in Des Moines, Iowa, awarded in 1972 and a LL.M. from Georgetown University in Washington, D.C., awarded in 1977. I am admitted to the bars of Iowa, Pennsylvania, Kentucky and the District of Columbia, as well as the U.S. Supreme Court Bar. I have practiced law for the federal government, for a state prosecutor's office and for large corporations.)

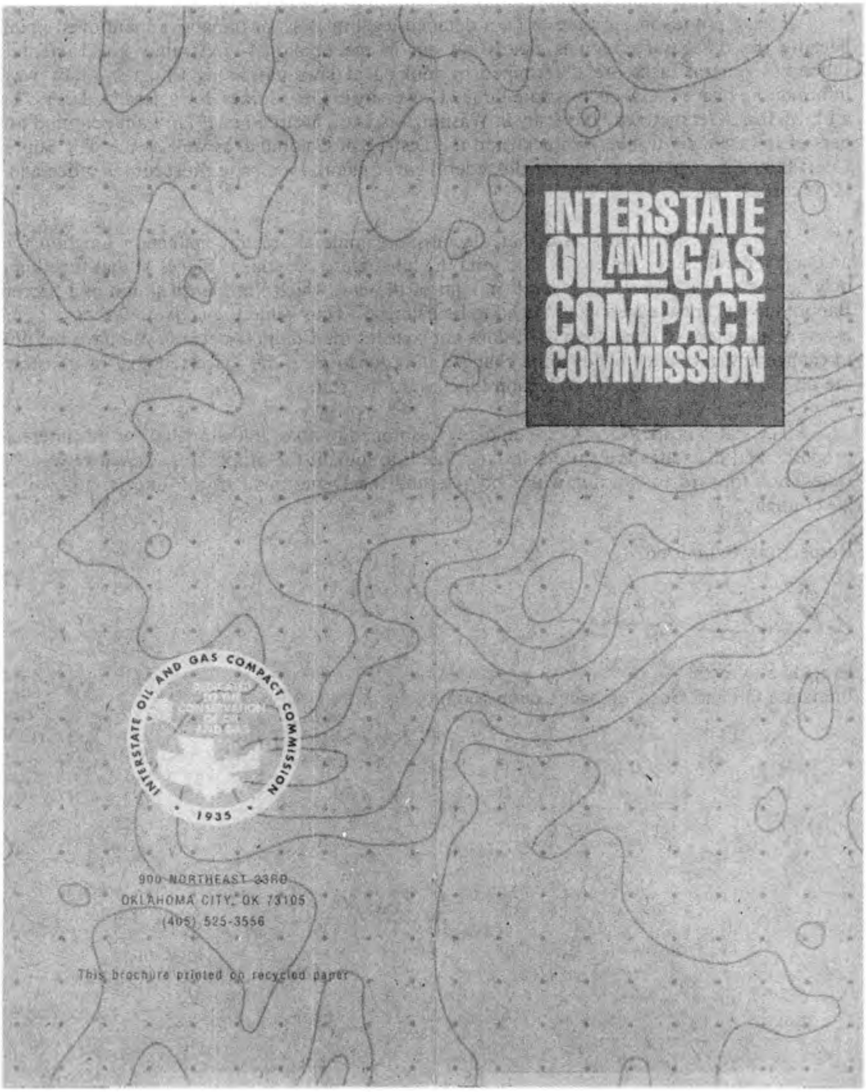
Secretary Babbitt has said that the on-shore minerals royalty collection function is not uniquely federal, hence his proposal to send the function to the states. Pieces of that function can only be viewed as "inherently federal" in light of the law, which President Clinton and Secretary Babbitt have acknowledged would need to be changed. Thus while the above referenced opinion is a very fine piece of legal analysis, it does not concern the Congress because you have the power to change any law which needs to be changed in order to meet the suggested goal of transferring the on-shore minerals royalty collection function to the states.

The states of the IOGCC are uniquely positioned to assist in the analysis of this interesting proposal, and the states are sincere in their intent to look at the proposal in a creative way. The states look forward to working with Congress and the Department of the Interior to "re-invent government."

Respectfully Submitted,

Christine Hansen

Christine Hansen
Executive Director
Interstate Oil and Gas Compact Commission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Idaho
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Oregon
Washington

In 1990, the name of the organization was changed to the Interstate Oil and Gas Compact Commission to reflect the growing role of natural gas in the nation's energy future.

Today, the Compact consists of 29 oil-and-gas-producing states and six associate-member states.

In its nearly 60-year history, the Compact has recorded significant contributions to the mission of minimizing waste and maximizing production of oil and gas.

For example, the Compact has:

• Played an important role in increasing reservoir production from a typical yield of 10 percent to more than 35 percent. This accomplishment alone has resulted in an additional 85 billion barrels of oil production in the United States.

• Served as a forum for state regulators seeking to standardize laws, rules, and regulations in energy-producing states.

• Taken the lead in promoting environmental protection in oil-and-gas production activities.

The charter has never been more relevant. In the coming years, minimizing the waste of non-renewable energy sources will be a top priority. The Compact will continue serving as forum for voices of reason, balance, and wisdom in developing the nation's energy supplies.

A STATEMENT OF MISSION

The Interstate Oil and Gas Compact Commission is responsible for ensuring that the nation's supplies of oil and gas are produced with minimum waste. As stated by its charter, the Compact is charged with encouraging conservation of these vital, domestic energy sources.

The Compact approaches this mission with a variety of programs and initiatives, including helping to develop government policies consistent with its goals, serving as a forum for diverse interests to exchange views on technical innovations and regulatory requirements, and monitoring consistency in related state programs.

The Compact represents 29 states that hold virtually all domestic oil and gas production. Six states are associate members.

FOUNDING PRINCIPLES

The United States Constitution gives states the right to compact—or agree to work together—to address common issues. The IOGCC is one of dozens of compacts, which are recognized as governmental agencies.

The governing body consists of the governors of the states. Each governor has one vote that may either be exercised or delegated to the governor's official representative. There are no other voting members.

Non-voting positions are held by state regulatory officials and representatives from industry who are appointed by the governors and serve on Compact standing committees.

Those committees include Energy Resources, Enhanced Recovery, Environmental Affairs, Legal, Research, and Regulatory Practices.

Member states fund the majority of Compact operations. Funding is also accepted for specific projects from federal agencies such as the Environmental Protection Agency and Department of Energy. The Compact receives no funds from the petroleum industry.

THE WORK OF THE IOGCC

Today, the Compact is carrying out its mission in a number of ways. The focus of its membership includes:

• Serving as a clearing house for information on techniques and technology that improve resource recovery.

• Identifying and addressing barriers to the expanded use of domestic natural gas in the nation's energy strategy.

• Assessing state efforts to manage oil-and-gas-related environmental activities.

• Promoting incentives for production from marginal wells.

• Providing education through training sessions, seminars, and midyear and annual meetings.

• Serving as a resource for government, industry, and the media on oil and gas conservation matters.

HISTORY AND ACCOMPLISHMENTS

With the discovery of the East Texas oil field in 1930, domestic oil production rose dramatically. In a matter of months, there was more oil than the nation could use, export, or store.

In the absence of effective regulation, well owners were forced into a spiral of increasing production to protect themselves from adjacent owners doing the same thing. Reservoirs were being rapidly depleted of the pressure needed to bring the oil to the surface, leaving millions of barrels of oil lost forever in the ground.

It became obvious to consumers, producers and the states responsible that regulation was needed to deal with overproduction and the resulting waste of oil.

In 1935, six states joined together to ratify the Interstate Compact to Conserve Oil and Gas. This agreement resulted in the creation of the Interstate Oil Compact Commission.

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INDEPENDENT PETROLEUM ASSOCIATION OF MOUNTAIN STATES
TESTIMONY BEFORE
THE SUBCOMMITTEE ON ENERGY AND MINERAL RESOURCES
OF THE HOUSE RESOURCES COMMITTEE
OF THE UNITED STATES HOUSE OF REPRESENTATIVES:
OVERSIGHT HEARING ON SOUND ALTERNATIVES FOR STREAMLINING MANAGEMENT OF ONSHORE FEDERAL MINERAL ACTIVITIES
THE HONORABLE KEN CALVERT, CHAIRMAN

TESTIMONY PRESENTED BY MR. DIEMER TRUE, PARTNER,
TRUE OIL COMPANY, CASPER, WYOMING
JUNE 8, 1995

THE INDEPENDENT PETROLEUM ASSOCIATION OF MOUNTAIN STATES (IPAMS) IS A NON-PARTISAN, NON-PROFIT TRADE ASSOCIATION REPRESENTING THE INTERESTS OF OVER 750 INDEPENDENT OIL AND NATURAL GAS PRODUCERS, ROYALTY OWNERS, CONSULTANTS, AND SERVICE/SUPPLY COMPANIES OPERATING IN A TEN-STATE ROCKY MOUNTAIN AREA: NEW MEXICO, WYOMING, COLORADO, UTAH, MONTANA, NORTH DAKOTA, SOUTH DAKOTA, NEVADA, AND ARIZONA. INDEPENDENT PRODUCERS ARE PRODUCERS WHOSE MAIN SOURCE OF REVENUE IS AT THE WELLHEAD AND WHO DO NOT HAVE DOWNSTREAM REFINING AND MARKETING.

TRUE OIL COMPANY IS AN INDEPENDENT EXPLORATION AND PRODUCTION COMPANY BASED IN CASPER, WYOMING WHICH HAS BEEN IN BUSINESS SINCE 1948. WE PRODUCE OIL AND NATURAL GAS IN NORTH DAKOTA, MONTANA, WYOMING, UTAH, COLORADO, KANSAS, AND SEVERAL OTHER STATES. IPAMS APPRECIATES THE OPPORTUNITY TO ADDRESS THIS COMMITTEE. WE APPLAUD YOUR INITIATIVE IN INVITING INDEPENDENTS FROM THE ROCKY MOUNTAIN STATES TO ASSIST YOU IN ADDRESSING IMPORTANT FEDERAL MINERAL ISSUES.

IPAMS' TESTIMONY FOCUSES ON THE DEPARTMENT OF INTERIOR'S (DOI) MARCH 27, 1995, PROPOSAL TO DEVOLVE THE MINERALS MANAGEMENT SERVICE (REGO II PROPOSAL) AND OFFERS ALTERNATIVES WHICH WE BELIEVE WILL ENHANCE THE FEDERAL ONSHORE MINERALS PROGRAM.

THE INDUSTRY IN THE ROCKY MOUNTAIN STATES

INDEPENDENTS IN THE ROCKY MOUNTAINS ARE THE MOST ACTIVE PRODUCERS DRILLING FOR OIL AND NATURAL GAS ON FEDERAL LANDS IN THE STATES OF WYOMING, NEW MEXICO, COLORADO, MONTANA, UTAH, AND NORTH DAKOTA. INDEPENDENT PRODUCERS LIVE AND WORK IN THE ROCKY MOUNTAIN REGION.

INDEPENDENTS PRODUCE APPROXIMATELY 60 PERCENT OF THE OIL AND NATURAL GAS IN THE ROCKIES. INCREASINGLY, INDEPENDENTS ARE PURCHASING THE PRODUCING PROPERTIES OF THE MAJOR COMPANIES. INDEPENDENT PRODUCERS ARE THE FUTURE OF THE INDUSTRY IN THE ROCKY MOUNTAIN STATES. THEY ARE LEAN, AGGRESSIVE COMPANIES THAT MAKE THE ECONOMICS OF THE ROCKY MOUNTAIN REGION WORK.

THE ROCKY MOUNTAIN REGION IS RICH IN OIL AND GAS, MUCH OF WHICH IS PRODUCED ON FEDERAL LANDS. THE ROCKIES ALSO CONTAIN VAST POTENTIAL FOR CONTINUED DISCOVERIES OF OIL AND NATURAL GAS. IN FACT, THE GAS RESEARCH INSTITUTE (GRI) IN ITS STUDY THE LONG-TERM TRENDS IN U.S. GAS SUPPLY AND PRICES: 1994 EDITION OF THE GRI BASELINE PROJECTION OF U.S. ENERGY SUPPLY AND DEMAND TO 2010 FORECASTS THAT THE ROCKY MOUNTAIN REGION WILL PLAY A CRITICAL ROLE IN THE NATIONAL ENERGY PICTURE IN THE FUTURE. AS PRODUCTION IN THE GULF OF MEXICO DECLINES, THE NATION WILL RELY ON NATURAL GAS PRODUCED IN THE ROCKIES.

GENERAL REMARKS ON THE DOI PROPOSAL

THE DEPARTMENT OF INTERIOR'S PROPOSAL LEAVES THE IMPRESSION THAT INTERIOR HAS NO INTEREST IN MANAGING THE NATION'S VAST MINERAL

RESOURCES AND, IN FACT, SEEMS INTENT ON DISCOURAGING THE DEVELOPMENT OF OIL AND GAS BY INDEPENDENT PRODUCERS ON FEDERAL LANDS. INCREASINGLY, IPAMS WONDERS WHETHER THE FEDERAL GOVERNMENT IS INTERESTED IN MANAGING AN ONSHORE OIL AND GAS PROGRAM AT ALL.

BACKGROUND ON MINERALS MANAGEMENT SERVICE

THE ROYALTY MANAGEMENT PROGRAM IN LAKEWOOD, COLORADO, EMPLOYED APPROXIMATELY 676 PEOPLE IN 1993 WITH A TOTAL BUDGET OF $65 MILLION. IN ADDITION, THE RMP EMPLOYED APPROXIMATELY 380 CONTRACT EMPLOYEES AT A COST OF $15.1 MILLION ANNUALLY.

FEDERAL MINERAL ROYALTIES ARE IMPORTANT TO THE ROCKY MOUNTAIN STATES. IN 1994, THE MINERALS MANAGEMENT SERVICE (MMS) DISTRIBUTED MORE THAN $537 MILLION TO 38 STATES FROM ROYALTY REVENUE FROM OIL, NATURAL GAS, COAL, AND OTHER MINERAL PRODUCTION. DISTRIBUTION TO THE IPAMS STATES ARE AS FOLLOWS: WYOMING $215.4 MILLION; NEW MEXICO $138.7 MILLION; COLORADO $36.8 MILLION; UTAH $32.7 MILLION; MONTANA $24.6 MILLION; NEVADA $9.4 MILLION; NORTH DAKOTA $2.5 MILLION; ARIZONA $82,000. THESE REVENUES ARE CRITICAL TO THE STATE GOVERNMENTS OF THE ROCKY MOUNTAIN REGION.

DEPARTMENT OF INTERIOR PROPOSAL TO DEVOLVE THE MINERALS MANAGEMENT SERVICE

WHILE IPAMS APPLAUDS AND SUPPORTS THE EFFORTS OF DOWNSIZING THE FEDERAL GOVERNMENT, REDUCING THE FEDERAL BUDGET, AND THE CONCEPT OF DEVOLVING THE MMS, IPAMS IS NOT IN FAVOR OF THE DEPARTMENT OF INTERIOR'S MARCH 27, 1995, PROPOSAL TO DEVOLVE THE RESPONSIBILITIES OF THE MINERALS MANAGEMENT SERVICE. ESSENTIALLY, INTERIOR PROPOSES TO TRANSFER VERY LIMITED ROYALTY COLLECTION RESPONSIBILITIES TO THE STATES. INTERIOR WOULD STILL RETAIN CONTROL OVER POLICY AND REGULATORY ISSUES.

IPAMS IS CONCERNED THAT THE PROPOSAL WOULD INCREASE COSTS TO INDUSTRY AND THE STATES. INTERIOR'S PROPOSAL IS INEFFECTIVE AND FAILS TO ACHIEVE THE GOALS OF ALL AFFECTED PARTIES. IPAMS IS SKEPTICAL THAT A NET COST SAVINGS EXISTS IN TRANSFERRING A PORTION OF ONE PROGRAM TO ANOTHER ENTITY WHILE RETAINING MANY FUNCTIONS, SOME DUPLICATIVE, AT THE FEDERAL LEVEL.

IPAMS' RECOMMENDATIONS

IDEALLY, IPAMS SUPPORTS THE TOTAL TRANSFER OF THE FEDERAL MINERAL AND SURFACE ESTATE TO THE STATES. IN THE LONG TERM, WE BELIEVE THAT THIS WOULD LEAD TO THE OVERALL REDUCTION OF GOVERNMENT AND ECONOMIC PROSPERITY FOR THE ROCKY MOUNTAIN REGION. IPAMS BELIEVES THAT THE STATES ARE BETTER EQUIPPED TO CHART THE COURSE OF THEIR ECONOMIC AND ENVIRONMENTAL FUTURES THAN THE FEDERAL GOVERNMENT IN WASHINGTON, D.C. THE DEPARTMENT OF INTERIOR SHOULD EXAMINE OR IMPLEMENT IMPROVEMENTS IN EXISTING REPORTING, VALUATION, AUDIT PROCEDURES. THERE ARE NUMEROUS WAYS IN WHICH THE MMS CAN SAVE MONEY.

ALL OF THESE ISSUES HAVE BEEN DISCUSSED AND ANALYZED FOR MANY YEARS. SEVERAL OF THESE AREAS WERE EXAMINED BY THE MMS NATIONAL PERFORMANCE REVIEW ROYALTY MANAGEMENT PROGRAM REINVENTION LABORATORY REPORT IN 1993. SHORT OF A TOTAL TRANSFER, THE MMS COULD CERTAINLY REDUCE THE FEDERAL BUDGET BY IMPLEMENTING THE FOLLOWING RECOMMENDATIONS:

* ELIMINATE THE PAYOR INFORMATION FORM (PIF) 4025. THIS FORM SERVES NO REAL FUNCTION AND COSTS THE MMS AND THE INDUSTRY MONEY.

* ELIMINATE AUDITS FOR LOW VOLUME WELLS WHICH PRODUCE LESS THEN 200 MCFD. THE FEDERAL GOVERNMENT SHOULD FOCUS ON EFFORTS WHICH RESULT IN THE GREATEST RETURN WITH THE LEAST INVESTMENT.

* INCREASE TRAINING FOR CURRENT MMS STAFF. WHILE MANY MMS EMPLOYEES ARE KNOWLEDGEABLE ABOUT THE INDUSTRY, MANY ARE NOT. IPAMS IS AWARE OF INSTANCES IN WHICH MMS AUDITORS HAD TO BE TRAINED ON INDUSTRY FUNDAMENTALS BY THE COMPANIES THEY WERE AUDITING. THIS DRAINS VALUABLE RESOURCES FROM A COMPANY AND IS SIMPLY INEXCUSABLE.

* COMBINE THE MMS AND THE BLM INTO A SINGLE FEDERAL MINERALS AGENCY. THIS WOULD ELIMINATE DUPLICATIVE WORK, ENABLE THE FEDERAL GOVERNMENT TO MANAGE AND EXPLOIT ITS MINERALS FOR MAXIMUM RECOVERY, AND ALLOW INDUSTRY A "USER FRIENDLY" GOVERNMENT AGENCY.

* TAKE FEDERAL ROYALTY IN KIND. IF THE FEDERAL GOVERNMENT IS TRULY SINCERE ABOUT REINVENTING GOVERNMENT, IT SHOULD TAKE ROYALTY IN KIND. THE MMS CURRENTLY HAS A PILOT PROGRAM IN EFFECT FOR OFFSHORE NATURAL GAS PRODUCTION. THE MMS SHOULD TAKE THIS PROGRAM ONSHORE.

IN 1993, THE MMS COLLECTED APPROXIMATELY $1.1 BILLION IN FEDERAL ONSHORE ROYALTIES COMPARED TO $3.1 BILLION FROM OFFSHORE PRODUCTION. ACCORDING TO MMS FIGURES, THE RMP SPENDS APPROXIMATELY FIVE TIMES AS MUCH ADMINISTERING THE ONSHORE PROGRAM AS IT DOES THE OFFSHORE PROGRAM.

THE MMS COULD AGGREGATE ITS ROYALTY VOLUMES IN VARIOUS ONSHORE PRODUCING BASINS AND PLACE THOSE VOLUMES OUT FOR BID TO INDUSTRY MARKETERS. A NATURAL GAS MARKETING COMPANY WOULD PAY HANDSOMELY FOR SUCH VOLUMES. THE MMS WOULD RECEIVE MORE MONEY FOR THE GAS. IT WOULD ELIMINATE THE NECESSITY OF VALUATION REPORTING, VALUATION DISCREPANCIES, VERIFICATION, AND EXTENSIVE APPEALS AND LITIGATION EXPENSES ASSOCIATED WITH VALUATION ISSUES. COMPANIES WOULD STILL REPORT THEIR VOLUMES AND THEY WOULD BE ABLE TO ACQUIRE THIS INFORMATION FROM THE OPERATOR OF A PROPERTY, THEREBY ELIMINATING ADDITIONAL REPORTING BY THE INDUSTRY.

* LASTLY, IPAMS RECOMMENDS THAT THE DEPARTMENT OF INTERIOR AND THE CONGRESS ENCOURAGE THE FEDERAL ROYALTY RECIPIENT STATES TO DEVELOP THEIR OWN PROPOSAL. WE BELIEVE THAT THE STATES ARE COMMITTED TO WORKING WITH INDUSTRY IN AN EFFORT TO REACH AN ACCEPTABLE SOLUTION FOR ALL PARTIES. THESE EFFORTS COULD RESULT IN LOWER COSTS FOR INDUSTRY AND STATES; UNIFORMITY BETWEEN STATE AND FEDERAL LAND SYSTEMS; AND ELIMINATION OF DUAL ROYALTY AND SEVERANCE TAX REPORTING.

BUREAU OF LAND MANAGEMENT PROPOSALS
INDUSTRY PAYMENT FOR PRE-LEASING NEPA ANALYSIS

THE DEPARTMENT PROPOSES TO IMPOSE THE COSTS OF PRE-LEASING NEPA ANALYSIS ON THE OIL AND GAS INDUSTRY. THE DEPARTMENT'S PROPOSAL FORECASTS THAT SUCH A MOVE WOULD SAVE $6 MILLION AND 30 FULL-TIME EMPLOYEES OVER A FIVE-YEAR PERIOD.

SUCH A PROPOSAL DEMONSTRATES DOI'S LACK OF KNOWLEDGE OF THE OIL AND GAS INDUSTRY. THE RESPONSIBILITY OF COMPLYING WITH NEPA IS IMPOSED ON THE AGENCY, 42 U.S.C. SECTION 4332. CURRENTLY, FOR POST-LEASING SITE-SPECIFIC SURFACE DISTURBING ACTIVITIES, OIL AND GAS COMPANIES PAY FOR THE REQUIRED NEPA ENVIRONMENTAL DOCUMENTATION.

INDUSTRY PAYS FOR ENVIRONMENTAL ASSESSMENTS AND ENVIRONMENTAL IMPACT STATEMENTS FOR DRILLING OF WELLS. THESE DOCUMENTS ANALYZE THE IMPACTS WHICH SURFACE DISTURBING ACTIVITIES HAVE ON THE LANDSCAPE AND DEVELOP MITIGATION MEASURES TO PROTECT THE ENVIRONMENT. INDUSTRY ALSO PAYS FOR ENVIRONMENTAL IMPACT STATEMENTS FOR INFILL OR DEVELOPMENT DRILLING PROGRAMS. TYPICALLY, THE BLM, WHICH IS RESPONSIBLE FOR THE NEPA COMPLIANCE, SAYS IT CAN DO THE DOCUMENTATION FOR INDUSTRY PROJECTS BUT NOT FOR THREE YEARS. MEANWHILE, THE COMPANY'S LEASE IS RUNNING AND THE ONLY ALTERNATIVE THEN IS TO CONTRACT WITH A THIRD PARTY TO DO THE NEPA DOCUMENTATION.

THE DEPARTMENT DOES NOT HAVE A POLICY WHICH CUTS ACROSS PROGRAM LINES REQUIRING ALL USERS OF THE PUBLIC LANDS TO BEAR THE COST OF NEPA PLANNING COSTS. FOR EXAMPLE, MINERS, CATTLEMEN, RECREATIONAL USERS, AND TIMBER HARVESTERS ARE NOT CHARGED FOR NEPA ANALYSIS AT THE PROGRAMMATIC LEVEL. WHY HAS THE OIL AND GAS PROGRAM HAS BEEN SINGLED OUT TO PAY FOR ADDITIONAL ENVIRONMENTAL DOCUMENTATION? IN ADDITION TO POST-LEASING ENVIRONMENTAL COSTS, THE INDUSTRY ALSO PAYS FOR STUDIES AND SURVEYS OF ARCHAEOLOGICAL AND HISTORICAL RESOURCES, RAPTORS, SAGE GROUSE, ELK, MULE DEER, ANTELOPE, AND THREATENED AND ENDANGERED SPECIES.

HOW WOULD THE BLM DETERMINE WHICH COMPANIES PAY FOR PRE-LEASING COMPLIANCE? INCREASED COMPLIANCE COSTS WOULD DISCRIMINATE AGAINST SMALL INDEPENDENT PRODUCERS. IN ADDITION, CAN A COMPANY PAY FOR NEPA COMPLIANCE DOCUMENTATION WHEN THE COMPANY DOES NOT YET OWN THE LEASE WHICH IS SUPPOSED TO BE ANALYZED.

COST RECOVERY FOR ENERGY/MINERALS ADMINISTRATION

THE DEPARTMENT ESTIMATES THAT BY MORE AGGRESSIVELY SEEKING COST RECOVERY FOR THE ADMINISTRATIVE COSTS OF IMPLEMENTING THE MINERALS PROGRAM, IT CAN SAVE $3 MILLION OVER A FIVE-YEAR PERIOD. THE DEPARTMENT ALSO ANTICIPATES THAT 15 FULL-TIME EMPLOYEES WOULD BE NEEDED TO ADMINISTER A MORE AGGRESSIVE COST RECOVERY PROGRAM. IPAMS FINDS IT VERY DIFFICULT TO BELIEVE THAT THE DOI WILL ACTUALLY ACHIEVE A NET SAVINGS UNDER THIS PROPOSAL.

TRANSFER OF INSPECTION AND ENFORCEMENT AUTHORITY TO THE STATES

BLM PROPOSES TO TRANSFER ITS MANDATED INSPECTION RESPONSIBILITIES ON FEDERAL LEASES TO THE INDIVIDUAL STATES. MANDATED INSPECTION REQUIREMENTS ARE THOSE DICTATED BY THE FEDERAL OIL AND GAS ROYALTY MANAGEMENT ACT (FOGRMA). FOR EXAMPLE, 30 U.S.C. SECTION 1711 REQUIRES THE SECRETARY OF THE INTERIOR TO ENSURE THAT EACH PRODUCING LEASE SITE IS INSPECTED ONCE A YEAR. THE DEPARTMENT OF

INTERIOR ANTICIPATES SUCH A TRANSFER TO SAVE $9 MILLION AND 99 FULL-TIME EMPLOYEES OVER A FIVE-YEAR PERIOD.

IPAMS IS NOT ADVERSE TO SUCH A PROPOSAL, BUT QUESTIONS THE LEGITIMACY OF THE COST SAVINGS ESTIMATE. FOGRMA, ENACTED IN JANUARY OF 1983, ALREADY AUTHORIZES THE DEPARTMENT OF THE INTERIOR TO ENTER INTO COOPERATIVE AGREEMENTS WITH STATES AND INDIAN TRIBES AND TO DELEGATE TASKS IMPOSED BY FOGRMA TO STATES AND INDIAN TRIBES. 30 U.S.C. SECTION 1732 AND 1735. DESPITE THIS AUTHORITY WHICH HAS EXISTED FOR A DOZEN YEARS, WE ARE AWARE OF FEW INSTANCES IN WHICH STATES HAVE SOUGHT COOPERATIVE AGREEMENTS OR DELEGATIONS OF AUTHORITY TO CONDUCT THE INSPECTION AND ENFORCEMENT OF FEDERAL LEASE SITES.

FOR EXAMPLE, THE COLORADO OIL AND GAS CONSERVATION COMMISSION AND THE BUREAU OF LAND MANAGEMENT RECENTLY ENTERED INTO A MEMORANDUM OF UNDERSTANDING (MOU) WHICH DIVIDES INSPECTION RESPONSIBILITIES WITHIN THE STATE TO CONCENTRATE FEDERAL RESOURCES ON THE WEST SLOPE WHERE MOST OF THE FEDERAL LANDS ARE LOCATED, WHILE THE COGCC ASSUMES RESPONSIBILITY FOR FEDERAL LANDS IN THE EASTERN PART OF THE STATE. IPAMS ENDORSES A SENSIBLE, PRACTICAL APPROACH SUCH AS THIS.

IPAMS UNDERSTANDS THAT THE BLM DOES NOT INTEND TO TRANSFER TO THE STATES ITS NON-FOGRMA INSPECTION RESPONSIBILITIES SUCH AS INSPECTIONS NECESSARY TO INSURE COMPLIANCE WITH DRILLING PLANS. SINCE THE REGULATIONS ALREADY AUTHORIZE DELEGATION OF BLM'S FULL INSPECTION AUTHORITY (43 CFR SECTION 3191.1-1, 3190.0-5(a), IT SEEMS CURIOUS THAT ONLY FOGRMA-MANDATED SITE SECURITY INSPECTIONS ARE PROPOSED TO BE DELEGATED TO THE STATES. IPAMS ASSUMES THAT, AS IS NOW THE CASE, STATE INSPECTORS WILL BE CERTIFIED BY BLM SO THAT ALL INSPECTIONS ARE HELD TO THE SAME STANDARDS.

THE EXISTING AUTHORITY FOR DELEGATION OF INSPECTION RESPONSIBILITIES TO THE STATES REQUIRES REIMBURSEMENT TO THE

STATES FOR THEIR COSTS (43 CFR SECTION 3190.2-2), SHARING OF ALL PENALTIES COLLECTED, AND COSTS OF TRAINING INSPECTORS. IPAMS WANTS TO KNOW WHETHER THESE COSTS WERE FACTORED INTO THE COST SAVINGS ESTIMATE FOR THE INSPECTION AND ENFORCEMENT DELEGATION ELEMENT OF THE REGO II PROPOSAL.

RECOMMENDATIONS AND COMMENTS ON BLM PROPOSALS

IPAMS RECOMMENDS THAT THE DEPARTMENT OF INTERIOR ABANDON THE BLM PROPOSALS IN THE REGO II DOCUMENT. THE OIL AND GAS INDUSTRY ALREADY PAYS ITS OWN WAY AND PAYS FOR SIGNIFICANT ENVIRONMENTAL COMPLIANCE COSTS. IPAMS OPPOSES BURDENING THE INDUSTRY ONCE AGAIN TO PAY FOR ENVIRONMENTAL COSTS FOR WHICH THE BLM IS RESPONSIBLE.

THE DOI SHOULD ENGAGE IN AND DEVELOP POLICIES WHICH PROMOTE THE DEVELOPMENT AND UTILIZATION OF THE NATION'S NATURAL RESOURCES. POLICIES WHICH ENCOURAGE THE DEVELOPMENT OF OIL AND NATURAL GAS WILL BENEFIT THE FEDERAL GOVERNMENT, AMERICAN TAXPAYER, AND LEAD TO THE ECONOMIC STRENGTH OF THE COUNTRY. IF THE DOI IS UNWILLING TO PURSUE THESE INITIATIVES, THEN PERHAPS THE STATES ARE A BETTER ENTITY FROM WHICH TO OWN OR MANAGE THE FEDERAL MINERALS.

WE WOULD URGE THIS COMMITTEE TO UNDERTAKE EFFORTS WHICH AIM AT REDUCING THE OVERZEALOUS ENVIRONMENTAL EXPENSES WHICH PERPETUATE THE DEPARTMENT OF INTERIOR AND REQUIRE INDEPENDENT PRODUCERS TO SPEND UNNECESSARY DOLLARS FOR PERCEIVED ENVIRONMENTAL PROBLEMS. IT IS NO WONDER THAT EXPLORING FOR AND PRODUCING OIL AND GAS IN THE ROCKY MOUNTAIN STATES IS THE MOST DIFFICULT IN THE COUNTRY. IPAMS SPECIFICALLY RECOMMENDS THE FOLLOWING:

* RETURN A PORTION OF OIL AND GAS REVENUES TO THE OIL AND GAS PROGRAM. THIS WOULD INCLUDE FUNDING FOR LEASING, ENVIRONMENTAL COMPLIANCE, AND OPERATIONS PERSONNEL WHICH DEAL DIRECTLY WITH OIL AND GAS ISSUES.

* ELIMINATE THE BLM DISTRICT LEVEL OFFICES. THE DISTRICT LEVEL DOES NOT SERVE A PRACTICAL FUNCTION. IPAMS RECOMMENDS FOCUSING THE BLM'S EFFORTS AT ON-THE-GROUND MANAGEMENT THROUGH EMPHASIS AT THE RESOURCE AREA OFFICES.

* CONTINUE THE BLM'S CURRENT SYSTEM OF CONDUCTING LEASING ANALYSIS. THIS IS A REASONABLE SYSTEM WHICH ALLOWS THE BLM TO EXAMINE ALL LAND USES CONCURRENTLY AND PLAN LAND MANAGEMENT DIRECTION FOR A 15 TO 20 YEAR PERIOD.

* ADOPT THE FEDERAL ROYALTY INCENTIVE RECOMMENDATIONS DETAILED IN THE <u>BUREAU OF LAND MANAGEMENT ONSHORE OIL AND GAS PERFORMANCE REVIEW, FINAL REPORT, APRIL 27, 1995</u>. THESE RECOMMENDATIONS INCLUDE: ROYALTY RATE REDUCTION FOR HIGH COST PRODUCTION; ROYALTY RATE REDUCTION FOR ENHANCED RECOVERY PROJECTS; ROYALTY RELIEF FOR HORIZONTAL AND DIRECTIONAL WELLS; ROYALTY RELIEF FOR WILDCAT AND DEEP WELLS; ELIMINATE MINIMUM ROYALTY REQUIREMENT FOR STRIPPER WELLS; AND REVISE POLICY ON DEVELOPMENT CONTRACTS.

<u>CONCLUDING STATEMENT</u>

IPAMS APPRECIATES THE OPPORTUNITY TO PROVIDE THIS HONORABLE COMMITTEE WITH COMMENTS. WE ARE ALWAYS AVAILABLE TO PROVIDE YOU WITH ADDITIONAL COMMENTS OR ANSWER FURTHER QUESTIONS.

Statement of

J. LARRY NICHOLS
President, Devon Energy Corporation

on behalf of

THE DOMESTIC PETROLEUM COUNCIL

and

THE INDEPENDENT PETROLEUM ASSOCIATION OF AMERICA

on

Alternatives for Streamlining Management of Onshore
Federal Oil and Gas Activities

before the

ENERGY AND MINERAL RESOURCES SUBCOMMITTEE
OF THE
HOUSE COMMITTEE ON RESOURCES

Washington, D.C.

June 8, 1995

STATEMENT OF J. LARRY NICHOLS
ON
ALTERNATIVES FOR STREAMLINING MANAGEMENT OF
ONSHORE FEDERAL OIL AND GAS ACTIVITIES
BEFORE THE
ENERGY AND MINERAL RESOURCES SUBCOMMITTEE
HOUSE RESOURCES COMMITTEE
JUNE 8, 1995

Mr. Chairman and members of the subcommittee, I am Larry Nichols. I am President of Devon Energy Corporation ("Devon") headquartered in Oklahoma City, Oklahoma and of the Domestic Petroleum Council ("DPC"). My testimony today is given not only on behalf of Devon and DPC but also on behalf of the Independent Petroleum Association of America ("IPAA"), whose Public Lands Committee I chair.

The DPC is a national trade association which represents 20 of the largest independent oil and gas companies, while IPAA represents approximately 5,500 independent oil and gas producers, many of whom are small businessmen and women. Independents produce over 65% of the natural gas and almost 50% of the crude oil produced in the lower 48 states. The subject of today's oversight hearing is of great importance to independent oil and gas producers, since nearly 30% of all of the independents' production comes from the federal lands.

Earlier this year, the Administration unveiled its "reinventing government" proposals ("REGO II") for the Minerals Management Service ("MMS") and the Bureau of Land Management ("BLM"), the two Interior Department agencies responsible for the management of oil and gas activities on federal and Indian lands. At about the same time, BLM released its Onshore Oil and Gas Performance Review, a report intended to lay the foundation for improving the onshore oil and gas program. We are not prepared to take a position on the Administration's developing MMS "devolution" proposal, but from what we have seen, it appears not to be a devolution, but rather a convolution, of the agency. The Administration's proposals for streamlining BLM's management of oil and gas activities contain many commendable ideas but also some that are, frankly, of concern to us. What I would like to do today is first summarize why it appears to us that the Administration has chosen the wrong path to streamline the MMS royalty collection function, then comment briefly on the BLM proposals and finally highlight alternatives which we believe will result in major improvements in the management of the federal onshore oil and gas estate.

Before I begin my discussion of these onshore issues, let me just say that while we may not yet have a firm position on the onshore REGO II proposals, our members are nearly unanimous in their view that transferring the MMS offshore function intact to some other agency is not a good idea. The minuscule savings ($2 million per year) that would result from this proposal don't seem worth the risk of compromising the effectiveness of the MMS by diluting its importance within the management of some other Interior Department agency.

I. The Reinventing Government ("REGO II") Proposal for the MMS

We had assumed that the Administration's "devolution" proposal involved transferring the entire MMS royalty management program to the states, including the authority to achieve the purposes of the program in the most efficient, cost-effective manner. We were surprised to learn that the Administration's proposal would transfer only MMS's "ministerial" royalty collection functions. The authority to establish policies to reduce the cost of the program and make it more efficient would be retained by the Interior Department, where some other agency would continue to develop royalty management policy, make value determinations, promulgate rules, enforce lease terms and royalty obligations and adjudicate disputes. The Interior Department believes these functions cannot constitutionally be delegated to the states because they involve the exercise of executive power and must therefore be performed by employees of the executive branch of the federal government. The Administration proposal thus simply shifts much more of the cost of running the program to the states without empowering them to make the policy decisions that might result in significant cost reductions.

It is inconceivable to us that the states will want to assume the role the Administration would have them play. Currently, 25% of the cost associated with administering onshore federal mineral leases is deducted from the states' 50% share of revenues from those leases. The Administration would increase the states' share of the cost by 100% from 25% to 50%. This cost shift to the states -- $20 million annually -- appears to account for a large part of the $107 million of savings the Administration hopes to achieve over the first five years from "devolving" the MMS. For a state like New Mexico where Devon has substantial gas production from federal leases, the loss of revenue under this proposal would be significant. The Interior Department estimates that even with the substantial, unproven cost savings that it assumes will be achieved by the state's assumption of the royalty collection role, the state of New Mexico would lose over $4.5 million annually. There is simply no incentive for the states to embrace the Administration proposal if it is going to impose economic losses of that magnitude.

In addition to our concern that the states are not likely to assume the royalty collection role the Administration proposes for them, we have a number of other concerns and questions about the "devolution" proposal. Chief among our concerns is that the proposal will increase our costs. It is conceivable that after spending millions of dollars to develop sophisticated royalty payment systems to meet current federal regulations, we may be forced to modify those systems or develop new ones. Also, to comply with the reporting requirements of numerous states and Indian Tribes, as opposed to those of just the MMS, we may be forced to hire additional staff. These and other concerns are detailed in Attachment 1 to my statement.

II. BLM's REGO II and Performance Review Proposals

In its REGO II proposal, the Department of the Interior is proposing to transfer BLM's oil and gas inspection operations to states and Indian tribes. BLM's Onshore Oil and Gas Performance Review proposes that enforcement responsibilities be transferred by memorandum of understanding to the states as well. It is not unusual for Devon to have inspectors for the Environmental Protection Agency, the BLM and the New Mexico state agency at the same field sites on the same day. Eliminating this duplication would result in savings to both the governmental agencies and the producers. We support these proposals.

We commend BLM for the royalty reduction incentives it is proposing in its Performance Review. The royalty rate reductions proposed by BLM should encourage development of more high-risk, high-cost projects and allow for the continued production of marginally economic stripper wells. The government will earn increased revenues on oil and gas production volumes which would not otherwise occur without the royalty incentives. We also think BLM's "ecocredits" proposal -- royalty relief or other credits for voluntarily exceeding environmental requirements -- is a good idea.

While BLM's royalty incentives proposal would encourage development of the federal oil and gas resource, a companion proposal would discourage development by adding to our costs. BLM is proposing to collect $9 million in additional fees and charges from producers over four years beginning in 1997 for administrative costs associated with pre-lease and post-lease activities. This additional levy on the oil and gas industry is not warranted. The industry pays in lease rentals and bonus bids more than enough to cover the cost of the entire oil and gas program. A more appropriate initiative would be to curtail the scope of pre-leasing National Environmental Policy Act ("NEPA") compliance, a subject that is currently being reviewed by the Senate Energy and Natural Resources Committee.

III. Alternatives for Streamlining and Improving Management of Onshore Oil and Gas Activities

In managing our federal oil and gas resources, we should strive to achieve as major goals the simple virtues of certainty, clarity, simplicity and reasonableness. We have a number of recommendations to offer which would further these goals, while reducing MMS's and BLM's management costs and our cost of compliance. I will highlight just a few of our recommendations in the time remaining.

A. Eliminate Unnecessary and Redundant Reporting to Federal and State Agencies and Streamline the Royalty Management Audit Program

A great deal of information is required to be reported to both Federal and state agencies or multiple times to the same federal agency. Information on well completions, applications for permits to drill and authorizations to transport is reported to both state and federal agencies. We suggest making a single government agency responsible for gathering and maintaining these reports. If this proves impractical, then it would seem to us that the agencies at a minimum should standardize the forms that are filed with each agency.

Under current audit programs, it is possible for a lessee to be required to provide the same information to a number of MMS auditors or state and Tribal auditors. For example, an operator of a unit may be requested to supply the same document to several different auditors. A number of duplicate and triplicate audits would be eliminated if audits were conducted at a unit level. Since most federal production onshore is part of a communitized or unitized agreement, developing a unit audit strategy would drastically reduce the audit resources needed for onshore review. Moreover, audits would also be completed more timely.

B. Simplify and Streamline Royalty Reporting

I won't burden the subcommittee with all of the ways in which MMS's reporting requirements could be simplified and streamlined. Attachment 2 to my statement lists a number of ways this could be done. Implementation of these changes would result in cost savings to both the MMS and the producer.

There are no doubt a variety of other ways to simplify the reporting burden. We recommend that MMS undertake a review of the various forms it requires producers to complete and ask (1) whether the data required by the form is necessary and (2) if so, is there a simpler method of obtaining it?

C. Simplify Product Valuation

Approximately $68 million are spent annually to administer the MMS Royalty Management Program. The most difficult, uncertain, unclear and costly aspect of administration is royalty valuation, the determination of the value of a lessee's production to which the federal royalty rate should be applied. With the advent of open access and deregulation, many marketing changes have occurred. Gas is often aggregated, pooled, transferred and stored before it reaches the final sales point. Transactions are numerous and complicated. A simplification of royalty valuation would eliminate unnecessary costs by industry and the MMS.

One way the MMS could give clarity and certainty to royalty valuation and eliminate administrative legal expenses by both the MMS and the producer would be to eliminate the "marketable condition" clause and to establish a clear point for determining the deductibility of various expenses.

D. Solicit Meaningful Input from Industry in the Formulation of New Policies and Regulations

Once policies are established, it is hard for the producer to work with compliance personnel on practical solutions to address problems arising in the course of policy interpretation and implementation. When producers are included in the formulation of policy, potential implementation and interpretation problems can be anticipated and dealt with in advance.

The process used in constructing the Federal Gas Valuation Negotiated Rulemaking proposal was an attempt to include industry in the policy formulation process. We are encouraged by the inclusion of the industry in that process and are anxious to see the resulting proposals.

E. Develop an Onshore Royalty-in-Kind Program

We recommend that MMS develop an onshore royalty-in-kind ("RIK") program similar to MMS's offshore pilot program. After six months of operation, the offshore pilot program has received widespread praise and support from both industry and the MMS. Since only the production volume need be accounted for, there is little administrative cost incurred by the federal government. Value is established by contractual arrangement with a purchaser. If the MMS were to establish a similar program onshore, the $68 million annual budget for the MMS Royalty Management Program could be significantly reduced.

F. Provide Certainty, Clarity and Fairness in Regulating the Responsibilities of the Lessor and Lessee

Two statutory corrections should be made that would provide greater certainty, clarity and fairness in the relationship between the federal government and the producer. The MMS recognizes no time limitation for compelling lessees to keep and provide production information for federal lease audits and recognizes no time limitations in attempting to collect royalties. This results from the fact that there are multiple, conflicting statutes of limitation which apply to the federal government's claims for underpayments of royalty and no clear statutory rules governing when the applicable statute begins to run. Enactment of legislation which clarifies when the limitation begins and ends would encourage MMS to assert its claims in a more effective and efficient manner, would provide fairness to lessees and would reduce the cost of keeping records.

The MMS requires lessees to pay interest and penalties on underpayments of royalty, but unlike the IRS, the MMS is not required to pay interest on overpayments. To avoid interest and penalty charges, this system encourages producers to overpay royalties, for which they have no right to interest. We believe legislation that affords the producer a reciprocal right to interest is long overdue.

G. Grant Federal Oil and Gas Lessees Access to New Mexico's Potash Area

In looking for ways to improve its existing oil and gas program, the BLM apparently overlooked a major opportunity it has in southeast New Mexico to bring millions of dollars to the treasury, slow the decline of domestic oil production and add hundreds of jobs to that region of the country. Within a 500,000-acre area, known as the potash area of southeastern New Mexico, there is one of the most promising oil and gas fields in the lower 48 states. I am personally familiar with the area, because Devon holds oil and gas leases within it and has been unable to obtain the drilling permits it needs to develop its leases.

The BLM has virtually kept the area off limits to oil and gas exploration and development due to unsubstantiated concerns about the safety of the potash mines in the area. Studies demonstrate that by providing an extensive buffer around mine workings, then drilling only a small fraction of the potential allowable wells in the area, the total economic impact could range from $2-4 billion, with net royalties to the federal treasury exceeding

$200 million, most of which would be flowing to the Treasury within five to seven years. The savings BLM hopes to achieve through its REGO II initiative pale in comparison to the revenues the government would realize from development of this area.

We believe BLM has sufficient scientific and geological data to grant immediate access to the 300,000 acres within that portion of the area where mining is not eminent. We also believe that BLM's further scientific study of the real extent of the safety issue will allow it to grant limited oil and gas development in that portion of the area where mining is planned. There is too much to be gained for the BLM not to give the highest priority to permitting oil and gas development in this area.

IV. Conclusion

It seems to me that the Administration's MMS and BLM initiatives suffer from a kind of schizophrenia. On one hand they reflect a desire to respond to current pressures to provide a greater role for the states in the management of the 632 million acres of federal land which comprise about 30 percent of the land area of the western states and Alaska. On the other hand, they reflect a reluctance to really give the states a meaningful role because of the federal agencies' desire to retain full federal control over surface management of these federal lands and the revenue flowing from them, based on the Federal Government's role as proprietor of these lands and the policy of the Federal Land Policy and Management Act of 1976 (43 U.S.C. § 1701(a)(1)) that "the public lands [shall] be retained in Federal ownership, unless as a result of the land use planning procedure provided for in this Act, it is determined that disposal of a particular parcel will serve the national interest." Until these conflicting concerns are resolved, I believe that the optimum course is for the MMS and BLM to move forward now with the program changes I have endorsed today, while the various Administration and Congressional approaches to "reinventing government" receive the further refinement and careful evaluation they require.

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DEVOLUTION OF MINERALS MANAGEMENT SERVICE TO STATES AND INDIAN TRIBES: CONCERNS AND QUESTIONS

- **This is potentially an unfunded mandate.**

For the states not to lose money under this proposal, they must reduce by 50% the present cost to administer the royalty management programs. The current cost to collect royalty and to run the associated support activities for onshore federal leases is $54.4 million. The Interior Department assumes that the states and Indian tribes will be able to run the program for $39 million per year less than the Minerals Management Service ("MMS") is running it. A reduction of that magnitude can only be achieved if many of the royalty valuation and collection functions are eliminated. If the royalty collection function is assigned to the states and the states are not given adequate federal funding to carry out the task, industry and states may be forced to pay for the cost overrun.

- **There are minimal cost savings associated with the Department's proposal.**

Transferring functions from one agency to another is a cost shift, not a cost savings. This cost shift to the states -- $20 million annually -- accounts for a large part of the $21 million per year the Department estimates will be saved by this proposal. With the federal government facing a three billion dollar deficit, $21 million is a *de minimus* savings, particularly when it involves tampering with the federal government's second largest revenue source.

- **This is a task assignment with no empowerment.**

In this proposal, the federal government makes the rules, directs the states to govern the rules, penalizes the states if the rules are not complied with, and gives no authority to the states to enforce the rules. It is unrealistic to expect the states to agree to such an arrangement.

- **There will be various interpretations of federal regulations.**

As the MMS has evolved, industry administrative costs have increased to comply with more and more policies and procedures. As 67 collection agencies evolve under this proposal, industry's administrative costs will increase even more to comply with 67 agencies' procedures and interpretations.

- **Shifting management has a destabilizing effect on investment decisions.**

The MMS is the only federal agency that is sharply focused on oil and gas exploration and production and has developed administrative and technical expertise in that field. Movement to another agency that has multiple interests or to multiple states could be detrimental to the future of oil and gas development programs. MMS was created in 1982 following a recommendation of the Commission on Fiscal Accountability to the effect that consolidating minerals revenue collection and offshore minerals management in a single agency would result in better management of the nation's minerals.

- **This will increase industry's reporting costs.**

Companies will have to increase staff to comply with the reporting requirements of numerous states and tribes, as opposed to those of just the MMS. Leases and units that cross state lines will have to be maintained in every working interest owner's system and the percentages applicable to each state.

- **Many of the current policies would be difficult to administer at a state level.**
In making correcting entries, the backout entries may occur in one state and the replacement entries in another. Cross-lease netting would be impossible.

- **The Department has not developed a forum through which all affected parties can provide input.**
The Department did not consult with any producers prior to announcing the proposal. If Phase II of the Vice President's Reinvention of Government was for agencies to contact their customers and determine what regulations were unnecessary and too burdensome, why didn't the Department contact its customers and ask for input with respect to this proposal? Independent producers are the single most affected industry segment.

- **There will be more litigation costs.**
With so many entities interpreting the regulations, there will be many more appeals and issues settled in court. states do not have to assume costs associated with appeals of federal royalty audits and have no incentive to provide a cost justification for their position. The federal government will incur increased legal costs when conflicting interpretations exist among the states and tribes in interpreting federal regulations and policies.

- **The federal government cannot transfer its trust responsibility of the Indian tribes.**
If the tribes' royalty management program proves deficient after three years of operation and the federal government must take back that function, how does the Department plan to pay for reassuming that responsibility? It is unclear why the Department thought that the Indian tribes that currently receive 100 percent of royalty collected would want to begin to collect the royalty themselves. It is a cost that they do not currently incur.

- **No consideration was given to industry costs of modifying and developing new royalty payment systems.**
Industry has spent millions of dollars to develop sophisticated royalty payment systems to meet the current federal regulations. This proposal contains no cost analysis for new industry royalty payment systems.

Attachment 1

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METHODS TO SIMPLIFY AND STREAMLINE ROYALTY REPORTING TO THE MINERALS MANAGEMENT SERVICE

- **Eliminate unnecessary forms**

  The MMS budget for forms verification in FY95 is $4.6 million. There are essentially four types of forms: production, royalty, allowance and payor information. The Payor Information Form (PIF) and the allowance forms (oil transportation, gas transportation, gas processing) are unnecessary, since the data reported on these forms is duplicated on other Federal forms. Elimination of the PIF and allowance forms would eliminate a whole department of the MMS and would also be an administrative cost savings to industry.

- **Modify the level of reporting that is required**

  Lease production is summed to a unit level but allocated and reported to the MMS at a lease level, so that the MMS can sum the leases to a unit level and reallocate to a lease level to determine if every lessee allocated and paid correctly. The volume of production doesn't change, but the allocation does. Lessees must go through the backout and replacement process to correct the allocation. The MMS doesn't collect any additional royalty through this cumbersome process, but does collect a few dollars in reporting fees. This process could be simplified by shifting reporting to the highest level of common ownership. Since most Federal production onshore production is part of a unit, the reporting requirement would be at the unit level. To allow royalty reporting a unit level would reduce the number of reported lines and would reduce the number of correcting entries. Both the MMS and the reporting entity would benefit from administrative cost savings.

- **Eliminate reversal and replacement reporting**

  Current MMS regulations require that all corrections be reported as a reversal of the previously reported volume and value. For large independents who have thousands of monthly transactions and do not have multi-million dollar systems, this method can require 50% of an accountant's time. In the daily transactions of business, no other entity requires transactions to be backed out and re-booked. We recommend allowing the royalty payor make adjustment on a net basis by simply paying the net difference in the two entries, instead of reversing the reported entries.

- **Eliminate selling arrangement reporting**

  Initially, the selling arrangement consisted essentially of long-term gas sales contracts, but as a result of the changes occurring in the gas market, there are now a multiplicity of selling arrangements. One company estimates that elimination of this reporting function would reduce reporting lines by at least 50%

Attachment 2

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WRITTEN STATEMENT

OF

ROCKY MOUNTAIN OIL AND GAS ASSOCIATION

SUBMITTED TO THE

HOUSE COMMITTEE ON RESOURCES

SUBCOMMITTEE ON ENERGY AND MINERALS

HEARING ON

BLM OIL AND GAS PERFORMANCE REVIEW

AND

DOI REINVENTION PROPOSALS

JUNE 8, 1995

INTRODUCTION

The Rocky Mountain Oil and Gas Association (RMOGA) appreciates this opportunity to provide the House Resources Committee's Subcommittee on Energy and Minerals with our views on the Bureau of Land Management's Onshore Oil and Gas Performance Review and Department of Interior's Reinvention Proposals. RMOGA is a trade association with hundreds of members, both large and small, who account for over 90 percent of the oil and gas exploration, development and transportation activities in the Rocky Mountain Region.

BACKGROUND

The recent decline of the domestic oil and gas industry has been well documented. Industry has lost nearly 1/2 million jobs in the last decade. Since 1979, more than 200,000 marginal wells have been abandoned and drilling (both exploratory and development) has declined 50 percent since 1983. In addition, industry is faced with ever-increasing regulatory and compliance costs connected with exploring for and developing oil and gas resources on public lands. In an attempt to control the cost of doing business, industry has vigorously cut expenses, streamlined its operations, and made technological advances.

We concur it is vitally important for the Federal government to employ similar measures to streamline agency structures, regulations and procedures to reduce costs and improve efficiency. However, such changes must be made with utmost care and consideration for the program responsibilities with which the Federal government is charged. Even minor changes can have broad, negative impacts. Therefore, it is incumbent upon the Federal agencies and Congress to implement innovative changes which will improve the oil and gas program without shifting the financial burden for program management to the oil and gas industry or to state taxpayers.

The Bureau of Land Management (BLM) adopted a logical process for determining how best to accomplish these objectives by initiating the Onshore Oil and Gas Performance Review (BPR). The BPR process allowed affected parties to provide BLM with issues, concerns and recommendations on how to improve the oil and gas program. By consulting with industry, BLM has been able to discern exactly where beneficial changes may be made. That is not to say there is total consensus regarding the proposed actions derived by the BLM; this is clearly not the case. Nonetheless, interested parties have an opportunity to discuss their concerns with the BLM before any program changes are implemented.

The BPR process has attempted to avoid surprises such as the REGO II proposals, i.e., the proposed abolition of the Minerals Management Service (MMS) and the "Reinvention" of BLM. The Federal government should take lessons learned in the BPR and apply them to REGO II. Industry is more than willing to work with the Federal government to determine how best to streamline processes and cut costs. We have only to be given the opportunity to participate.

BLM PERFORMANCE REVIEW

On April 28, 1995, officials from the Department of Interior, BLM and MMS met with industry members in Denver to present the Final BPR Report which includes Policy Options now being considered by BLM and DOI for implementation. This testimony provides background for understanding industry§ reaction to the BPR Policy Options as well as our recommendations for issue resolution. RMOGA believes elements of the BPR will provide assistance in solving industry problems related to exploration, development and production activities on public lands.

Following is a discussion about each of the BLM BPR Teams, their charge and their current recommendations/policy options.

INCENTIVES

The Incentives Team was charged with developing and recommending incentives for industry operating on Federal lands. This team perhaps offers the greatest opportunity for improving the condition of the oil and gas industry in the Rocky Mountain Region. RMOGA commends BLM for considering policy options that will help sustain a healthy domestic oil and gas industry. Incentives discussed below are based on the premise that while the Federal government cannot control price, it can alter the cost of production either though tax incentives [which require legislation], removal of regulatory disincentives, or specific to this discussion, royalty reduction. In RMOGA's opinion this portion of NPR creates a win/win scenario. There are benefits that will help Federal and state governments, the oil and gas industry, the environmental community, and the general public.

The BPR Incentive Team objectives are aimed at increasing gas production and reducing the decline in oil production while improving performance in environmental protection and contribute to improving the health of ecosystems. Actions which BLM recommends be accomplished immediately through issuance of Policy Guidance include:

- 1 year Royalty Relief for Enhanced Oil Recovery Projects
- 1 year Royalty Relief for Wildcat and High Cost Drilling
- Pilot an Environmental Compliance Self-Certification Program
- Reinstate Policy on Approval of Development Contracts
- Hold Local Industry and Interagency Technology Transfer Forums
- Broaden Use of Bioremediation for Small Spills

Two additional Priority Action items which will require regulatory changes are streamlining of the Unitization Application Process and the elimination of duplication with states on Communitization Applications. Several additional proposals will be further evaluated, such as a royalty rate reduction for high water cut wells, elimination of minimum royalty for stripper wells, and Ecocredits for voluntary environmental enhancement.

RMOGA would like to discuss what we consider to be the highest industry priorities and our reaction to BLM's stated Policy Options.

Policy Option - Royalty Relief for High Cost and Marginal Wells

Of the high-cost oil production, perhaps the most benefit for RMOGA members would be derived from royalty reduction for high water cut wells. High water cut wells producing in excess of 95% water with oil production totaling less than 25 barrels of oil per day are known throughout the industry to have the highest expenses per barrel of oil equivalent. Reducing the royalty burden on these properties will help offset these additional costs making them more economical to drill and maintain.

Additional reserves can also be realized by improving the economic viability of development projects through secondary and tertiary methods such as water flooding, steam flooding, polymer injection and other costly but effective enhanced recovery mechanisms. In addition to secondary and tertiary recovery methods, the application of enhancements such as 3-D seismic, hydraulic fracturing, high technology production facilities and other approaches to increase production should be considered for royalty rate reduction. These high tech approaches will add reserves, extend the productive life of marginal properties, prevent premature abandonment and significantly increase Federal and state revenues. Optimizing existing wells does not require new wells to be drilled so surface disturbance is minimized and there is little, if any, environmental impact.

Royalty relief for high cost wells becomes critical as producing properties reach marginal condition. According to the National Petroleum Council's July 1994 Study of Marginal Wells, about 85% of the Nation's 600,000 producing wells are defined as marginal.

Recommendation:

a) Expand the current BLM "stripper" royalty reduction rule to become a "marginal" royalty reduction rule using the NPC definition of marginal property. We also recommend wells falling within this definition receive a sliding scale royalty reduction. This would include wells having an average daily production of 15 barrels of oil equivalent per day [BOEPD] or less with injection wells included, wells having an average daily production of 25 barrels BOEPD or less per well with water production accounting for more than 95% or more of the total production with injection wells included, and wells that produce heavy oil with an API gravity of less than 25 degrees.

b) The incremental production resulting from implementation of approved tertiary recovery projects should receive a 50% royalty reduction. Examples are: Miscible or immiscible gas injection, steam injection, surfactant injection, fireflooding, polymer injection, inert gas injection and horizontal drilling.

c) The incremental production resulting from well stimulation activities should receive a 50% royalty rate reduction. Examples are: fracture treatments, chemical stimulation, horizontal sidetracking of existing wellbores and perforation of new intervals or horizons in existing wellbores.

d) Wells producing sour oil and gas which do not qualify as "marginal" but are costly to produce (processing and regulatory compliance), and, which obtain a lower market price at the wellhead, should receive a 25% royalty rate reduction.

Policy Option for Royalty Holiday for Wildcat Wells

The definition normally used for "wildcat well" defines it as a new well located in excess of one mile from existing production. This definition is too narrow and does not reflect the real criteria that should be evaluated, which is whether a company is taking a risk to find "new" production.

Recommendation:

For this rule to be optimally successful in encouraging new production, the definition needs to be broadened to include drilling to a previously unproduced horizon. Under this definition one could deepen an existing wellbore, find a new horizon, and still fall within the true meaning of wildcat well. This will also minimize environmental impacts.

Policy Option to Revise Policy on Development Contracts

Companies most likely to explore previously unexplored public lands with potential for oil and gas are unable to conduct such operations because they are approaching their acreage limitation. The development contract is a concept, authorized by statute, whereby the lessee agrees to commit to the exploration of the area on a schedule as prescribed by the Federal government's development contract. BLM imposed a moratorium on development contracts as a result of criticism by the General Accounting Office. While the moratorium is no longer in effect, BLM has not developed any subsequent policy on the use of development contracts.

Recommendation:

RMOGA members are in favor of development contracts as an exploration tool. Development contracts provide the Federal government with a company's commitment to explore high risk areas, with no cost to the government, but with the opportunity for significant benefit to the nation. Both large and small operators believe the benefits of development contracts are clear and far reaching. Therefore, RMOGA strongly endorses the resumption of the use of development contracts on Federal lands.

Policy Option to Simplify Production Pooling (Communitization)

Simplification of the communitization process as proposed entails eliminating the need for industry to submit a separate agreement package to pool Federal interests. This proposal requires modification of existing regulations.

Recommendation:

RMOGA fully supports this Policy Option.

Policy Option to Streamline the Unitization Process

Unitization benefits both the public and industry and is intended to promote the most efficient development of an oil and gas reservoir, while minimizing both the number of wells drilled and environmental disturbance. Simplification of the process would reduce administrative uncertainties, provide flexibility to operators, and establish clear benefits in return for development. Changes in the unitization process requires regulatory modification.

Recommendation:

RMOGA fully endorses this Policy Option.

Policy Option to Institute Ecocredits

Under the concept of "ecocredits", BLM would offer credits against lease rentals, lease bonuses, or royalty payments for voluntarily exceeding environmental requirements, or undertaking or cooperating in ecosystem enhancement projects (e.g., habitat restoration) identified in land use plans. Additional analysis is required to develop the proposals into implementable actions. Two proposals, the "Best Operating Proactive Program (BOPP) and the "Ecosystem Enhancement Program" (EEP) have been identified for further development.

Recommendation:

This concept originated with BLM and has a great deal of promise. As articulated in the BLM's Final BPR Report, however, it is too narrow. Ecocredits should be designed to cover reimbursement to companies for the added costs incurred for archeological surveys, T&E species inventories and project environmental impact statements (EIS). This should be BLM's responsibility. Unfortunately, if project proponents desire timely project approval, they are left with no choice but to fund these studies themselves. This has a negative impact on project economics and is a significant <u>disincentive</u>. This trend must be reversed.

Policy Option to Utilize Bioremediation

BLM would develop a national policy to recommend using bioremediation as a treatment method to reduce clean-up costs and prevent future liabilities.

Recommendation:

RMOGA supports development of such a national policy.

Policy Option for Environmental Compliance/Self Certification

BLM would establish a pilot program to allow industry to self certify environmental compliance. One or two operators with a good compliance record would volunteer for this program.

Recommendation:

RMOGA supports the concept of self-certification but needs more details.

REGULATORY REVIEW

Regulatory reform is the best way for the Federal government to improve the onshore oil and gas program while streamlining its own processes. Eliminating waste and duplication may also be achieved with a significant cost savings to the government and to industry. A recent American Petroleum Institute (API) study of pending EPA rules found that compliance with these new environmental regulatory proposals could cost the exploration and production sectors of the oil and gas industry about $14 billion over the next five years. API also estimates a loss of over 19,000 industry related jobs and a loss of another 35,000 jobs in the communities where industry employees live and in the businesses that supply our industry.

The BLM Regulatory Review Team has not yet presented Policy Options for industry review or consideration. Because regulatory reform presents an important opportunity for significant cost savings, RMOGA believes it is important to summarize some of the recommendations presented by our Regulatory Review Team to BLM.

Risk Assessment/Cost Benefit Analyses

Too often, regulations are imposed on an industry or activity without any assessment of the risks posed by that industry or activity on wildlife, plants or other sensitive resources on public land. Moreover, the cost of compliance often outweighs any benefit that may be derived. RMOGA supports broad-based regulatory reform that would require Federal agencies to conduct both risk assessment and cost benefit analysis before imposing new regulatory requirements. This principle should apply to any Federal agency that can issue regulations to address environmental concerns or impacts.

Instruction Memorandum

It is vital that BLM seek industry input before issuing instruction memoranda (IM) which may significantly revise how BLM manages the oil and gas program or the manner in which industry conducts oil and gas activities on Federal lands.

Streamlining and Elimination of Waste and Duplication

BLM and other Federal agencies should aggressively seek ways to reduce or eliminate unnecessary or duplicative regulatory requirements. The following recommendations were made by RMOGA to the BLM's Regulatory Review Team:

<u>General</u>

- Standardize and consolidate duplicative reporting forms required by Federal and state agencies.

- Use automation to reduce paperwork. Expedite BLM's Automated Fluid Mineral System (AFMSS). Examine AFMSS linkage with the Forest Service Data General database to facilitate EISs, environmental assessments (EA), applications for permits to drill (APD) postings and lease sales. Expedite linkage with the Automated Lease Management Record System (ALMRS) to facilitate automation of all data (e.g., wildlife habitat, T&E habitat, wetlands, land ownership). Allow public access where information is not confidential.

- Improve procedural consistency among BLM offices without losing flexibility.

- Create and/or facilitate data sharing, consolidation of data and training throughout Federal, state and local agencies wherever possible.

- Eliminate conflicting Federal requirements.

<u>Permitting/Operations</u>

- Revise cultural resource requirements to reduce time and cost required for compliance with Section 106 of the National Historic Preservation Act (NHPA). BLM should use its current data base to reduce the number of required surveys.

- Eliminate or reduce redundant Federal/state regulations and permitting approvals. Foster Memoranda of Understanding (MOUs) with interested states to delegate downhole responsibility.
- Eliminate on-site inspections and 30 day APD processing for <u>nonsensitive</u> locations.

- Use EAs and CEs (Categorical Exclusion) more frequently on activities that have minimal impact on the environment (e.g., geophysical permits to drill along existing roads).

- Implement broader use of field-wide surface use plans to facilitate development. Eliminate sundry notice requirements for activities consistent with the surface use plan and record of decision.

- Shorten the time frame for drilling applications and plans to conform to changes recommended by RMOGA to Onshore Order No. 1.

- Eliminate sundry notice approvals for routine operations such as casing repairs, and institute a time frame requirement (15 days) for approval. Accept faxed sundries, etc.

Reporting/Compliance

- Revise regulations to require submission of only one copy of well logs, core data, DSTs, and geologic reports.

- Implement the waste tracking/inventory system previously proposed by industry during discussions on Onshore Order #1.

- Revise and facilitate the current Inspection and Enforcement (I & E) program. The BLM spends too much time on minor violations such as incorrect well signs when the focus should be on major violations.

- Extend the shut-in period that a well can be allowed to remain non-producing from the current one-year period before any action by the producer is triggered.

IOGCC Public Lands Project

In addition to BPR efforts to streamline Federal regulations and procedures, the Interstate Oil and Gas Compact Commission (IOGCC) has begun a "Public Lands Project" to seek ways to reduce regulatory duplication among state and Federal government agencies. The project covers the states of California, Colorado, New Mexico and Wyoming and is made up of representatives from the state conservation commission, industry, environmental groups and the Federal government.

This group is now developing consolidated reporting forms for APDs, sundry notices and completion reports. Instead of using different forms for different states and for the state and Federal government, operators would report on one form that could apply to all public lands states.

CALIFORNIA OUTREACH AND INTERAGENCY COORDINATION

RMOGA supports all the policy options proposed by the California Process Review Team.

NEPA/PLANNING

The NEPA/Planning Team Charter identified two key objectives for the Phase I review: 1) identify salient issues along with a recommended course of action and 2) recommend priorities along with solutions. The Final NEPA/Planning Report indicates the review was comment driven. However, the NEPA/Planning Team appears to be severely predisposed against the current oil and gas program and multiple-use in general.

In comments submitted to the Team last December, RMOGA expressed alarm that the Team's issue statements were biased against oil and gas activities on public lands. We recommended that BLM focus on a balanced consideration of relevant issues. Unfortunately, many biased and unfounded issue statements have been given legitimacy merely by virtue of their being included in the report. For example, an element of Issue 1, *Agency Approach to Oil and Gas Management*, states "resource values, other than threatened and endangered species and cultural resources, do not receive equal consideration with oil and gas". This is certainly not the perception of the oil and gas industry which believes oil and gas resources are not being given equal consideration with other resource values.

It is clearly documented that new oil and gas leases are being subjected to increasingly restrictive lease stipulations to protect newly designated areas of critical environmental concern (ACEC), constantly expanding wildlife winter range areas, semi-primitive recreation areas (both roaded and unroaded), unstable soils and steep slopes, to name a few, under the auspices of new resource management plans. Consequently, a more balanced issue statement reflecting all viewpoints might read, "whether oil and gas is given appropriate consideration with other resource values".

We acknowledge that some of RMOGA's issues and comments were addressed in the NEPA Team's Final Report, such as the need to justify lease stipulations, to improve post-land management plan monitoring, and the need for a "model" resource management plan to help streamline the planning process. However, many of these issues are buried in Action Plans whose overall emphasis we cannot fully support. Generally, BLM's Action Plans reflect a desire to cater to a small, but vocal, segment of the public which customarily opposes all economic uses of public lands. This ignores BLM's statutory mandate to manage public lands in accordance with multiple-use principles.

Of the five Action Plans developed, two have been identified for immediate implementation.

- Establish and Maintain a Common Resource Database
- Southwest Wyoming Resource Evaluation

Following is a discussion of the five Action Plans identified by the NEPA/Planning Team.

Policy Option to Establish and Maintain a Common Resource Database

On a positive note, BLM is proposing to establish a coordinated, comprehensive and dynamic resource database to aid in decision-making during resource management planning. BLM currently lacks a comprehensive database; therefore, standards for data collection must be established to ensure consistency in data collection and display. Establishment of the database will help eliminate redundant resource studies (which have been a significant problem for industry operators on public lands). Industry information regarding future exploration and development plans will be solicited.

Recommendation:

RMOGA fully supports compilation of a computerized, up-to-date, comprehensive resource database. Collection and maintenance of extensive resource information will aid BLM in preparation of resource management plans, implementation and monitoring of plans as well as in its resource program management. Funding this effort should be a BLM priority.

RMOGA would caution, however, that only very limited industry information regarding future exploration and development plans will be available. Due to the competitive nature of the oil and gas business, companies are unable to divulge proprietary information regarding future exploration targets. It is also extremely difficult for companies to tell BLM what their future development plans may be because these plans are dependent upon a variety of factors, such as demand, pricing, geographical and reservoir information, results of exploration efforts and new environmental compliance requirements.

Policy Option to Utilize the Southwest Wyoming Resource Evaluation

BLM is proposing to "test" the Performance Review recommendations under field conditions, using the BLM's Southwest Wyoming Evaluation currently underway.

Recommendation:

In light of the fact that we do not support several of the BLM's policy options, particularly with regard to controversy and limitations on environmentally sound exploration and development activities, we unequivocally oppose the use of the Southwest Wyoming Evaluation as a test case for BLM's Performance Review recommendations. BLM states such a test would help refine its ecosystem management planning techniques, evaluate mitigation techniques and improve the quality of post-lease monitoring. However, southwest Wyoming is not the ideal candidate for such a test because it is 95 percent under lease and the oil and gas activities are primarily focused on development. Industry has already experienced permit delays in the area and cannot accommodate any additional delays.

Policy Option to Conduct Additional Studies and Analyses

The Team identified several studies that will purportedly provide information to improve the onshore minerals program and provide better customer service to both industry and other publics. Many of the additional studies coupled with the increase in public involvement recommended in the report will only serve to further increase financial burdens on taxpayer funded government programs and to industry as well as to increase permitting delays without any corresponding improvement in the quality of Federal land management decisions.

Areas of primary concern with elements of this Policy Option are discussed below.

Environmental Controversy

BLM's inordinate sensitivity to controversy is cause for great concern. The BLM intends to analyze the "magnitude" of environmental controversies and their relationship to on-the-ground oil and gas potential and other resource values. For example, actions identified include:

- Identify all areas that have controversial oil and gas leasing and development activities.
- Determine what proportion of lease tracts offered and drilling permits (APD) processed during the past 10 years provoked environmental controversies.
- Determine what proportion of the available public land base contains areas of high environmental concern.
- Compare acreage of tracts successfully offered without controversy with acreage and tracts that provoked appeals or litigation.
- Compare number of APDs processed and issued with the number of APDs subject to administrative appeals or litigation.

Recommendation:

Federal land management decisions must be based upon the best available resource and scientific information rather than the emotional rhetoric caused by controversy. If controversy is to be the touchstone for making decisions, many extremely important prospective areas could be placed off-limits to oil and gas activities. BLM personnel are trained professionals who are educated and experienced in scientific realities associated with what is possible and reasonable in terms of mitigation and actual effects to sensitive resource values. BLM must not abrogate this expertise for fear of public criticism or challenges.

We strongly object to utilizing "degree of controversy" as a standard by which oil and gas decisions will be measured and decided. Exploration for and development of oil and gas resources in this country provides goods, services and jobs. As such, it is an important component of our national and regional economy and must not be arbitrarily diminished in importance. Controversy must not be the criterion of the decision-making process because it is far too simple to create and manipulate. By allowing the degree of controversy to dominate the decision-making process, BLM abandons science in favor of certain public sentiment.

Public Input

BLM proposes to examine the adequacy of the public input process in deciding whether to grant stipulation waivers, exceptions or modifications (WEMs). BLM would also investigate the practicability of an open process for public participation in on-the-ground actions, e.g., on-site inspections for APDs.

Recommendation:

Public involvement in the WEM process is statutorily limited to those decisions which could constitute a significant management change or one which could result in significant impact to the resource being protected. Expanded public involvement is unwarranted when WEM criteria are included in RMP documents which have already received substantial public review, or if BLM determines WEM decisions will not result in significant impacts to the resource being protected. It is important for BLM, as the land management agency, not to abdicate its authority to make technical land use decisions which would further delay the process. Industry is routinely faced with many project delays due in large part to the numerous opportunities for public input that currently exist. Additional delays, such as those which could result from unnecessary public involvement, must be avoided.

Further, expanded public involvement in the resolution of on-the-ground activities will not improve the quality of project related decisions. Decisions associated with placement of the well pad, reserve pit, access road, and production facilities, for example, are normally made in conjunction with technical and scientific requirements. Involvement of an untrained member of the public in such technically oriented procedures would likely lead to even more controversy, which would create additional delays where there are presently none.

Policy Option to Establish a Multi-disciplinary BLM/Forest Service Review Team

BLM is proposing to establish an interagency review team to review the adequacy of RMPs, Forest Plans and NEPA documents. Other issues to be reviewed include length of time required to complete NEPA/planning documents, level of environmental documentation needed to make a decision, and the efficiency and cost of preparing an environmental assessment (EA) v. environmental impact statement (EIS).

Recommendation:

We support BLM's intent to examine the possibility of reducing the time required to prepare NEPA/planning documents. The process should be streamlined while retaining the analytical integrity needed to make defensible resource decisions. We also support review of what level of environmental documentation is required in a given situation. Science, not public controversy, should be the driving factor in determining whether an EIS is necessary. Whether an undertaking would have a significant impact on the human environment is the legal standard of whether or not to prepare an EIS or EA.

We do not endorse another review of the adequacy of BLM's RMPs or the Forest Service's LRMPs. Both agencies have already recently concluded such reviews. New studies would be redundant and a waste of time and money.

Policy Option for Bureau-wide Policy Review and Guidance

BLM proposes to change existing Bureau-wide policies and guidance to give greater flexibility to resource area managers to consider lease deferrals, no-lease decisions, and withdrawal of lands from leasing based upon "ecological" conditions. New policy would also ensure planning documents are goal oriented, utilizing a screening process which would identify areas with moderate-to-high potential for oil and gas resources. The agency could then limit its decisions to those areas. Policy guidance allowing the imposition of additional stipulations on existing leases is also proposed. On the positive side, a quality control program would be established to ensure decisions are justified by objective NEPA analysis.

Imposition of Additional Stipulations

Policy guidance has also been proposed which would allow application of additional restrictive stipulations to existing leases which are unstipulated or were issued prior to implementation of a RMP or FLPMA. The report states this policy option "*responds to concerns that existing lease rights need to be protected and pre-FLPMA leases and other leases need to be updated to meet current environmental concerns*". Historically, BLM policy has been consistent with statutory limitations on the imposition of new stipulations on leases which have already been issued. Moreover, conditions of approval for APDs are also subject to limitations according to BLM policy established just three years ago.

Recommendation:

BLM policy on authority to impose additional requirements on an unstipulated existing lease was addressed in Washington Office Instruction Memorandum (IM) No. 92-67, which directs:

> *"Any relocation greater than 200 meters, timing restriction greater than 60 days, or mitigation which would render a proposed operation uneconomic or technically infeasible is not considered to be consistent with a lessee's rights and cannot be required absent a lease stipulation, unless it is determined that such mitigation is required to prevent unnecessary and undue degradation of public lands or resources. The clear evidence and convincing need for such mitigation must be documented in a site-specific EA or EIS, if necessary, on the APD."*

An excerpt from the Bureau's Decision on the recently completed Big Piney/LaBarge Coordinated Activity Plan (CAP) in Wyoming further defines BLM policy:

"The BLM Wyoming State Director, or his representative, utilizing appropriate COAs, can exceed the 60-day and 200-meter rule for site-specific actions, such as an APD, where there is site-specific environmental analysis and clear and convincing evidence in the documentation showing undue and unnecessary degradation would result if protective restrictions were not applied. This takes into consideration that due and necessary degradation are acceptable." [emphasis added]

The mitigation identified by the BLM is precisely that which could be required by a permit condition of approval (COA) to avoid unnecessary and undue degradation. However, if the COA is determined to be excessive, the same would be true of similarly restrictive mitigation measures, such as a suspension of operations and production.

Limitations on BLM's authority to change the conditions of an existing lease are necessary. Recognition of valid existing rights is a crucial element of the oil and gas program. Unlimited BLM authority to change lease conditions mid-stream would create unacceptable uncertainty for the oil and gas industry. It would make it next to impossible for companies to make rational decisions regarding commitment of exploration or development capital. Therefore, we strongly recommend that the BLM retain its existing policy which was developed very carefully and with public input.

Goal Oriented Planning

BLM's proposal to adopt "goal oriented" planning would limit leasing and development opportunities to non-controversial areas and to areas which contain moderate to high potential for oil and gas resources. The report's focus on finding ways to rationalize no leasing in controversial areas and to limit activities to only those areas with moderate to high potential for oil and gas which are not controversial will even more dramatically slash land availability for oil and gas activities.

Recommendation:

The "goal oriented" planning proposed by the NEPA/Planning Team does not take into account the need for an extended land base to accommodate the development of prospects. Nor does it acknowledge that oil and gas activities are relatively short-term in the overall scheme of things. Arbitrarily setting aside controversial areas with potential for oil and gas must not be an option because it could preclude discovery of signficant oil and gas reserves. We do not believe the Team has considered whether the benefits of such limitations outweigh the potential loss in exploration and development opportunities and their associated loss of state and Federal revenues.

As the agency responsible for managing the onshore oil and gas program, it is incumbent upon the BLM to ensure maximum opportunities for environmentally sound exploration and development activities to occur on public lands. We strongly recommend BLM abandon this goal oriented planning policy option in favor of existing guidance, which mandates multiple use management.

Policy Option for Training and Staff Efficiency

BLM proposes to improve efficiency and effectiveness through increased cross-training (both interdisciplinary and within the oil and gas program area). Awareness training for non-mineral personnel to provide a fundamental understanding of processes and operational aspects of oil and gas resources and the industry would also be provided along with a comprehensive, government-wide fluid mineral training program.

Recommendation:

RMOGA supports any effort to improve the understanding of the Federal oil and gas program of non-mineral personnel as well as mineral personnel. However, we also believe in addition to cross-training, the BLM must ensure it RETAINS its current fluid minerals expertise. Federal onshore oil and gas program expertise has been severely diluted through the buy-out program and transfers to other programs. This continued loss of expertise must cease if BLM is to continue as manager of the onshore energy and minerals program.

NEPA/Planning Conclusion

It would seem the NEPA/Planning Team is catering to the demands of environmental groups who aim to curtail oil and gas exploration and development on virtually all public lands. We urge the DOI and BLM to develop a rational approach to streamlining and making the NEPA/Planning and leasing and permitting processes more efficient. That was the stated intent of the performance review in the first place. Most of the policy options described in this report will not accomplish that goal; they will only serve to further burden an already overburdened domestic oil and gas industry.

BONDING/UNFUNDED LIABILITY

The BLM justifies inclusion of its bonding program in the Performance Review, in part, as a response to the July 1993 report prepared by the House Natural Resources Committee *"Deep Pockets: Taxpayer Liability for Environmental Contamination"*. The executive summary states:

> "The Federal government for over a century has encouraged, promoted, supported and subsidized activities that have resulted in a **severe environmental crisis**. Although there is no method in place to pay for mitigation of any of these **serious environmental hazards**--many of which pose **significant danger** to wildlife, economic activity, and even human safety--outdated government policies continue to **underwrite creation of even more crises.**" (emphasis added)

The report goes on to say:

> "Hundreds of onshore oil and gas wells on Federal lands may be improperly closed or contaminated with oil and drilling waste"; and,

"... a number of sites contaminated by oil and gas drilling waste have been added to the National Priorities List (NPL) for clean-up under Superfund".

RMOGA takes strong exception to such grossly misleading and inflammatory rhetoric. There is no scientific basis for the report's assertion the DOI's management of public lands, including oil and gas activities, has resulted in "a severe environmental crisis". Although oil and gas wastes may have contributed to the contamination at several sites on Superfund's National Priorities List, their disposal was regulated in accordance with the laws in place at the time. The petroleum industry is responsible for 10% or less of all Superfund site contamination, yet it pays approximately 60% of the Superfund taxes. Nor is there any empirical evidence to support EPA's claim in the report that oil and gas wastes will cause environmental contamination on BLM land. In its own 1987 Congressionally mandated "*Report to Congress*", EPA concluded that exploration and production (E&P) wastes rarely pose a significant environmental threat when managed properly; that existing State and Federal regulations are generally adequate; and, that regulation of E&P wastes as hazardous was unnecessary and impractical.

RMOGA does not perceive the existing Federal liability associated with orphan wells to be unmanageable. By its own admission, the BLM found it difficult to obtain accurate data on the extent of the problem using its own records, and was forced to rely on information gleaned from a poll of its offices. The liability for plugging what BLM estimates to be approximately 300 existing orphan wells represents only about 3% of the annual royalty revenue to the Federal government from onshore oil and gas production. Nor does the mere presence of orphan wells automatically imply that each poses a threat to public health and the environment. RMOGA suggests the BLM Bonding and Unfunded Liability Team has properly focused its review to minimizing future liability.

The BLM Bonding and Unfunded Liability Team offered thirteen recommendations intended to address the Federal government's liability for orphaned wells. Of the thirteen, the Project Leader for the BPR identified six recommendations which meet the criteria for initial implementation. The Team recommendations to be pursued are:

- Revision of assignment forms to clearly clarify the liability relationship between the assignor and assignee;
- Selective bond increases where need has been clearly demonstrated;
- Development of a shut-in well data base;
- Evaluation of risk, potential liabilities and bonding needs at the time of assignment;
- Elimination of duplicative bonding; and,
- Review of the Memorandum of Understanding between the BLM and the Forest Service.

RMOGA generally supports the targeted recommendations as reasonable proposals to minimize future taxpayer liability for plugging, abandonment and reclamation of existing wells. Although there are issues remaining which require further evaluation, clarification and refinement; we are confident the BPR process will continue to afford the oil and gas industry the opportunity for meaningful input.

In addressing how future liability for orphaned wells might be minimized, RMOGA reiterates several concepts previously submitted to the BLM on the bonding/unfunded liability initiative.

Increasing standard minimum bond amounts across-the-board will significantly impact independent operators. Increasing minimum bonds could exacerbate the problem by leading to more wells being shut-in and potentially more wells entering orphan well status. Establishing an orphan well fund into which all operators contribute will not necessarily solve the problem either. These approaches offer no incentive for the proper conduct of future operations. To the contrary, such requirements are likely to encourage default, poor industry practices and lax BLM enforcement activities. Either the fund or other prudent operators will subsidize the actions of noncompliant or insolvent operators. Minimizing the number of future orphan wells can be accomplished through appropriate risk assessment and compliance enforcement.

Case-by-case risk assessment must be a component of any bonding approach the Bureau adopts. The environmental risk posed by the type and location of various oil and gas activities must be evaluated to determine whether increased standard bond amounts are warranted. Likewise, the financial risk posed by an operator based on past compliance history, proof of financial assurance and years of operation must be determined case-by-case.

RMOGA strongly opposes imposition of joint and several liability. Such a scheme can be extremely inequitable. It places liability on past owners/operators who have no control over current operating practices and, again, offers no incentive for current owners/operators to comply with BLM rules and regulations. An operator could potentially be held liable for lease operations in perpetuity under such a scheme. Lastly, Superfund's joint and several liability scheme has led to protracted third-party litigation and has consumed the cleanup process. The BLM must not impose a liability scheme which has historically proven to be unworkable and inequitable. RMOGA supports a proportional liability scheme based on working interest owner percentages and recommends the allocation of past and future liability be handled at the time ownership transfers are negotiated.

The apportionment of liability is generally handled contractually by the parties involved in the ownership transfer. The affected parties have a vested interest in assuring liability is properly placed and responsibility for past and future operating practices is clearly identified. RMOGA has previously proposed an ownership transfer approval process in which a checklist is used by BLM personnel to determine whether all the liability issues of concern to the Federal government (compensatory royalties, bonding, plugging and abandonment, etc.) have been addressed and responsibilities clearly assigned in the contract. Another approach RMOGA has advanced in previous comments to the BLM Team is an ownership transfer approval process based on audit certifications between the parties involved. We do not, however, support audit procedure mandates. Again, the affected parties are most interested in clearly identifying responsibility for past and future liabilities. RMOGA does not want a BLM ownership transfer approval process to impose delays in closing transactions.

Following are specific comments on each of the policy options considered by the BLM Bonding and Unfunded Liability Team.

Policy Option #1 - Joint and Several Liability

This policy option would apply the concept of joint and several liability for compliance with all lease obligations regardless of the percentage of past or existing interest ownership. For reasons stated above RMOGA opposes a joint and several liability scheme as unworkable and inequitable. Past and future liability for environmental harm, unpaid royalties as well as plugging, abandonment and reclamation should be addressed at the time ownership is transferred.

Policy Option #2 - Joint and Several Liability

This option proposes pursuit of the party failing to comply with requirements of lease terms when 100% of record title has been assigned. BLM will first pursue the party who failed to comply. If the assignee had nothing to do with the failure to comply, the assignee will not be involved in the collection of damages by BLM. This proposal does not impose joint and several liability as the concept is traditionally applied. While it would appear rational to pursue the party truly responsible for failure to comply with a lease term, as summarized in the final report, considerable clarification of this option is needed. If the responsible party is no longer available or financially solvent, how does the BLM propose to proceed?

Policy Option #3 - Revise Assignment Forms

This option proposes to clearly assign liability between the assignor and assignee, and to use the Bureau of Indian Affairs (BIA) revised assignment form as a model. As stated above, we support the notion of dealing with past and future liabilities contractually at the time of ownership transfers. Unfamiliar with the revised BIA form, however, we cannot evaluate its adequacy in addressing liability issues.

Policy Option #4 - Increase Minimum Bond Amounts

The proposal to increase individual and statewide bonds across-the-board while maintaining the existing nationwide bond will not limit the Federal government's potential liability for orphan wells but will, as discussed above, only aggravate the problem.

Policy Option # 5 - Selective Increase in Bond Amounts

Option #5 was not identified by the BPR Project Leader as one to be pursued. Although not taken quite far enough, option #5 is similar to an industry suggestion to use Wyoming's recently revised bonding requirements as a model for the BLM. In summary, the Wyoming Oil and Gas Conservation Commission first defined and categorized various types of idle wells (shut-in, temporarily abandoned, dormant, permanently abandoned). In addition to the minimum bond, the state may require increased bond amounts of $2.00 per foot for dormant wells. Dormant wells are defined as those which are not producing, monitoring, injecting, permanently abandoned, shut-in or temporarily abandoned. In lieu of additional bonding, an operator may file a detailed plan of operation outlining actions to remove wells from dormant status within two years. This approach provides incentives for operators to either plug and abandon wells or return them to beneficial use.

The BLM recommendation suggests that after two years in approved temporarily abandoned status, operators agree to either plug wells on an acceptable schedule and increase the bond in place by $2.00 per foot or agree to pay a $100 per well, nonrefundable yearly fee into a BLM managed account for purposes of offsetting the cost of abandoning orphan wells. RMOGA encourages the BLM to continue to evaluate the feasibility of combining a revised policy option #5 with option #6 to address selectively increased bond amounts.

Policy Option #6 - Selective Increase in Bond Amount

Option #6 proposes a selective increase in bond amounts where a need to do so has been clearly demonstrated. Although RMOGA agrees bond amounts should be increased only where warranted, as written, this proposal could result in arbitrary application. Criteria for increasing bond amounts need to be defined. RMOGA offers its assistance in developing criteria for selectively increasing bond amounts which possibly combines elements of options #5 and #6.

Policy Option #7 - Federal Well Database

Implementation of option #7 to develop a database for tracking the status of all Federal wells should be the BLM's top priority. It is imperative the extent of the problem be defined before the BLM's bonding requirements are completely revamped. Development and maintenance of a data base which tracks the status of wells on Federal lands would well serve the government in quantifying and managing its true potential liability.

Policy Option #8 - At Risk Assessments

In this option, the BLM proposes the reassessment of potential liabilities of "at risk assignments" as an appropriate time to reconsider the amount of risk posed by the particular situation. Although RMOGA supports the concept of conducting risk assessment at the time of assignments, option #8 needs to be more definitive. What are "at-risk assignments"? RMOGA prefers this recommendation be revised to more closely track our suggestions on assignment of liability at the time of ownership transfers as discussed above in our General Comments.

Policy Option #9 - Alternative Funding Source for Orphan Wells

Although not targeted, the Bureau recommendation proposes a one-time authorization from Congress to establish an orphan well fund. RMOGA has previously suggested the pursuit of Congressional authority allowing a portion of the existing Water Reclamation Fund monies to be used for plugging, abandonment and reclamation of orphan wells.

It is our understanding 80% of the Federal government's share of the annual onshore mineral revenues is earmarked for the Water Reclamation Fund. In 1993, approximately $230 million deposited in the fund represented onshore oil and gas royalty income alone. Currently, however, revenue in the Water Reclamation Fund may only be used for construction and maintenance of dams and power facilities and other water projects as deemed appropriate by the Bureau of Reclamation. Use of the funds for any other purpose would require Congressional approval. Recognizing our recommendation may not meet the BPR criteria for swift implementation, RMOGA believes a portion of the oil and gas revenue deposited to the existing fund should be appropriated annually for plugging and abandonment of orphan wells. The *"Deep Pockets"* report states there is "no method in place to pay for mitigation of any of these serious environmental hazards". The Water Reclamation Fund is in place and a portion of it should be earmarked to mitigate orphan well liability.

Finally, Congress should require a full accounting of the Federal government's use of oil and gas revenues. Industry pays more than its fair share for the right to operate on Federal lands. Before additional monetary demands are placed on industry, the government should be required to make an accounting of how existing industry-generated funds are used.

Policy Option #10 - Tax Deduction for Abandonment Account

This recommendation proposes a revision of tax policy to permit payments deposited into approved abandonment/reclamation escrow accounts to be deducted as an expense of operations. The funds would remain dedicated to reclamation and would be transferred with the lease upon assignment. RMOGA sees little benefit to industry in this option. The upfront escrow money would not replace the bond but would be in addition to the bond. Industry should not be expected to pay twice.

Policy Option #11 - Eliminate Duplicate Bonding

RMOGA supports the BLM proposal to eliminate duplicative bonding by state or other Federal agencies on BLM and Forest Service Lands.

Policy Option #12 - Review BLM and Forest Service MOU

RMOGA supports option #12 to conduct a review of the National Memorandum of Understanding between the BLM and Forest Service as long as the BLM does not intend to implement Forest Service oil and gas regulations which are, in our opinion, more onerous than the Bureau's.

Policy Option #13 - Establish an Enforcement Record Affirming End-of-Lease Obligations

This option suggests cases involving relatively small monetary claims should be pursued by the Department of Justice to send a message that oil and gas lessees on public lands are not free to disregard their end-of-lease obligations. It also encourages the Government to aggressively pursue its interests in bankruptcy proceedings so the needs of the United States are addressed in reorganization and liquidation plans prepared by creditors, debtors and trustees. RMOGA does not perceive the Justice Department's involvement in BLM compliance as a streamlining process. The Government should already be meeting its obligations to enforce regulations and to pursue its interests in bankruptcy proceedings.

BLM REINVENTION PROPOSALS

BLM has announced several "reinvention" proposals to transfer various administrative responsibilities for the Federal oil and gas program to industry or states and tribes. Remarkably few details of the reinvention proposal are available, which makes it impossible for industry or the Federal government to discern the full ramifications of these proposals. The reinvention has been described by the Department of Interior as simply suggestions on how to achieve cost savings. However, it should be noted that industry believes the cost savings identified for each element of the proposal are minimal and may be inaccurate. Regardless of the level of cost savings which could be achieved by the BLM, any shift of the financial burden of BLM's program administration to industry, states or tribes is an unacceptable solution.

The Federal oil and gas program has always paid its own way. In fact, the onshore oil and gas program generates far more revenue to the Federal government than is needed to manage it in its entirety. For example, in 1994 the BLM's oil and gas program budget was $53 million. During that same period, the oil and gas industry paid $33 million in lease rentals and $97 million in bonus bids for onshore Federal lands, a total of $130 million. When royalty payments (including minimum and production royalty payments) of $647 million are factored in, the oil and gas industry paid $777 million in 1994, half of which went to Federal government. This does not include taxes.

Undeniably, industry reaps benefits from production activities on Federal lands, but the American public also receives exceptional benefits. Many in government see the energy industry as having "deep pockets" which can bear the brunt of ever-increasing costs associated with operating on Federal lands. It should be noted, however, the cost associated with exploration and development activities on public lands has become increasingly burdensome over the last 10 to 15 years primarily due to expanded restrictions, permitting delays, and many environmental compliance requirements with which the price of oil and gas has not correspondingly kept pace. It would be foolhardy for the BLM to monetarily penalize companies for leasing and conducting exploration and development activities on public lands. To do so could cause all companies, both large and small, to abandon heretofore economic domestic projects on public lands in favor of more lucrative ventures on state or private lands or in foreign countries.

OIL AND GAS PRE-LEASE COMPLIANCE

BLM is proposing to require those "industries benefitting from the leasing actions" to pay for pre-leasing environmental analyses. Apparently, BLM envisions industry-funded leasing documents being prepared on a watershed-by-watershed basis, which could encompass either a small or large area. BLM also indicates pre-leasing activities could be delegated to state and tribal governments. The rationale for this change in program management would be to save $6 million over a four-year period ($1.2 million per year), beginning in FY 1997.

Without an existing Federal oil and gas lease and approved permit, companies have no "compliance" obligations on public lands. Therefore, it is unclear how BLM would decide which companies must pay for leasing analyses. How would BLM apportion analysis costs to lessees? Even if BLM could contrive some type of payment system, few companies would be willing to fund leasing analyses without a guarantee they would acquire the specific leases in which they are interested. Of course, any preferential treatment to the funding company(s) would be contrary to the competitive leasing system adopted in 1987 upon passage of the Federal Onsshore Oil and Gas Leasing Reform Act (FOOGLRA). Has it been considered that such funding requirements would necessarily make Federal lease tracts less attractive, which would drive the lease bids down? Moreover, the additional cost of funding pre-leasing analyses could prove to be the "straw that breaks the camel's back" in that the additional financial burden could be sufficient to make new operations on Federal lands become economically infeasible.

BLM is responsible for managing the land and resources on public lands in accordance with resource management plans (RMP). According to 43 CFR Part 1601.02, the objective of planning is *"to maximize resource values for the public through a rational, consistently applied set of regulations and procedures which promote the concept of multiple use management and ensure participation of the public, state and local governments, Indian tribes and appropriate Federal agencies"*. Land management planning is a statutorily mandated process which requires Federal agencies to guide and control future management actions. This includes doing the analysis and making land use decisions, including oil and gas leasing.

The Federal Land Policy and Management Act (FLPMA) does not contain a provision for delegating planning activities on public lands to non-Federal entities. BLM is bound by law to conduct planning activities for the benefit of all users and resources. Therefore, RMOGA believes it is unrealistic for BLM to expect any industry to pay for RMP preparation.

Recommendation:

RMOGA strongly recommends that BLM retain its current system of conducting leasing analyses as a component of the land management planning process. The oil and gas industry already pays for leasing activities on public lands through lease rentals and bonus bids and BLM would have to retain the ultimate responsibility for the oil and gas leasing analysis. This comprehensive approach is appropriate because it allows BLM to study reasonably foreseeable development of oil and gas for a 15 to 20-year period in conjunction with other resource uses, such as grazing, recreation, and wildlife. As such, environmental consequences and cumulative effects of oil and gas and other resource program actions are fully examined in an environmental impact statement. After the analysis is complete, BLM determines where leases will be issued and with what types of stipulations and conditions, taking into account other resource factors.

COST RECOVERY FOR ENERGY/MINERALS ADMINISTRATION

BLM proposes to recover administrative costs incurred from actions necessary to conduct mineral operations, including the cost of preparing "licenses, fees and approval" of APDs. The estimated savings associated with this proposal is $3 million over four years.

The oil and gas program could potentially generate over <u>$3 billion</u> within the same time frame under the current system. It appears the energy industry is being singled out to pay for routine administrative procedures while other public lands users will not be required to similarly pay for their resource program administration.

In order to obtain timely permits, industry is already compelled to pay for countless resource inventories and surveys, all of which are the legal responsibility of the BLM as the Federal land management agency. For the same reason, companies are often forced to hire BLM-approved third-party contractors to prepare environmental analysis documents and to conduct archeological, botanical, and T&E species surveys in conjunction with geophysical, exploration and development proposals. These additional costs could render new projects, on new or existing leases, economically infeasible.

Recommendation:

Through the BLM Performance Review, RMOGA has recommended adoption of some type of cost sharing or royalty credit to compensate industry for expenditures associated with paying for management functions which are legally the responsibility of the BLM. Industry should not be expected to bear the financial burden of BLM's day-to-day program management expenses when over a <u>quarter billion dollars annually</u> are collected as a result of onshore oil and gas activities on Federal lands. Operating on public lands is already a much more expensive enterprise than operating on private or state lands. Therefore, the Federal government needs to ensure it does not drive the oil and gas industry off public lands and put at risk the significant revenue generated by oil and gas activities.

A more productive way for BLM to reduce management costs and save money would be to look within its own structural organization for ways to streamline. For example, is there a need for a three-tiered management scheme. A buffer between the state and the actual officials responsible for on-the-ground management may be expendable. On-the-ground resource program management could be done using resource teams which work from the district level. These teams could be responsible for program needs on a district-wide basis.

On the other hand, resource areas could report directly to the State Director. Clearly, carefully thought out structural changes would result in significant cost savings to BLM.

RMOGA has recommended as part of the BLM Performance Review, described earlier in this testimony, numerous ways to streamline the onshore oil and program and to eliminate waste and duplication. If adopted, many of these recommendations will result in significant cost savings.

TRANSFER OF I/E RESPONSIBILITIES TO STATE AND TRIBES

The proposal to transfer BLM's inspection and enforcement responsibilities to states and tribes lacks specificity and makes evaluation of the impacts of such an arrangement difficult. Absent details, it is assumed states and tribes would inspect facilities for compliance with BLM requirements. It is surmised BLM proposes to transfer only I & E authority to states and tribes while retaining responsibility for permitting, bonding, penalty assessment etc. Alternatively, I & E responsibility over surface activities could be assigned to one regulatory entity and I & E responsibility for downhole operations to another. Regardless of how BLM's existing authorities are partitioned, multiple agencies would be involved in managing operations conducted on Federal lands, which results in a more burdensome and complicated compliance scheme negating the purpose of "reinvention". Imposing multiple agency authority over a single Federal lease is of dubious benefit.

Existing regulations at 43 CFR 3190 permit states and tribes to enter cooperative agreements with BLM or to assume delegation for I & E functions. Since a mechanism is already in place allowing states and tribes to assume I & E responsibilities, it is inappropriate for BLM to mandate those authorities be transferred. The decision of whether to assume I & E functions should be left to the discretion of states and tribes. BLM estimates transferring I & E responsibilities will result in a cost savings of $9 million over a 5-year period. The Federal government may realize such savings, states and tribes will not necessarily. Requiring states and tribes to assume I & E responsibilities is equivalent to an unfunded Federal mandate.

Recommendation:

RMOGA suggests BLM rely on the existing regulatory mechanism available to states and tribes desiring to assume Federal inspection and enforcement responsibilities. State and tribal participation in the allocation of inspection and enforcement authorities through cooperative agreements with BLM will accommodate unique circumstances where opportunities to consolidate and streamline compliance inspections are evident.

BLM Reinvention Conclusion

The BLM Reinvention proposals were ill-conceived and generated as a reaction to the Administration's efforts to cut costs and streamline government. There are many ways in which to accomplish these objectives. However, it must be done in a thoughtful manner and with careful consideration of what impact such proposals would have on existing programs. In many ways, these proposals conflict with the incentives which have been recommended by the BPR Incentives Team, which are attempts to help rather than hinder the oil and gas industry. These proposals have the potential to adversely affect the oil an gas industry, which according to the previously referenced API study, stands to lose an additional 54,000 jobs in addition to the estimated 1/2 million lost since 1982. If the Administration is sincere in its efforts to streamline and cut costs, we need to go back to the drawing board and spend some time thinking about what really makes sense and not what is expedient.

DEVOLUTION OF MMS

With regard to the proposed devolution of the Minerals Management Service, although RMOGA is not representing the Council of Petroleum Accountants Societies (COPAS) in our testimony today, it should be noted that COPAS has provided technical input to RMOGA in preparation of this testimony.

RMOGA is opposed to the decentralization of the Federal royalty collection and production reporting functions for a number of reasons. Although the Department of Interior's "Proposal to Devolve the Responsibilities of the Minerals Management Service" is replete with assumptions and lacking in specificity, making it difficult to analyze, we do have serious concerns about the concepts outlined in the proposal as we understand them.

Under the Devolution Proposal, the Royalty Management Program (RMP) responsibilities for onshore Federal lands would be transferred to approximately 38 states, 31 of which have Federal oil and/or gas production. The 29 tribes would be encouraged to collect royalty payments due on their lands, while royalty responsibilities for Indian allottees and those tribes electing not to assume the royalty collection function would be transferred to the Bureau of Indian Affairs (BIA) or "another DOI bureau". The Department's opinion that the transfer of royalty collection and production reporting functions to approximately 67 states and tribes will create a more efficient and effective collection operation is one RMOGA does not share.

RMOGA views the proposed devolution of the MMS as a peculiar irony, since MMS was established by the Interior Department when the Linowes Commission, in 1982, concluded the Federal government requires a centralized method of determining oil and gas production from Federal leases and collecting the royalties due from those leases. DOI's proposal even flies in the face of its own 1992 Mineral Royalty Transfer Study, which concluded that very few of the royalty collection and disbursement functions could be transferred without severely compromising the economies of scale realized by the Federal program. Indeed, the Federal government acceded delegating accounting functions to the states would be "a step backward to a previously attempted organizational structure that failed". Moreover, the study concluded fragmentation of the Federal government's centralized and uniform accounting system might compromise all efficiencies and savings achieved during the MMS's 2first decade. We know of nothing that has happened in the past three years to alter those conclusions.

Since its inception, the MMS has cultivated the necessary expertise to manage the Federal royalty program. It has a proven record in improved stewardship of the nation's mineral resources. The Service last year was the recipient of Vice President Al Gore's Quality I2mprovement Prototype Award for the second consecutive year. Moreover, the agency has received high marks in the past several years from the Department's Inspector General — one of its harshest critics — for its efforts to encourage voluntary payor/producer compliance, for its financial statements for Fiscal Years '92 and '93, for increasing its efforts to determine and collect royalties associated with renegotiated natural gas contracts, for improving its automated systems and its services for Indian tribes and allottees, and for improving its appeals process.

MMS also continues to explore cost efficiencies through the use of negotiated rulemaking committees, study teams, and the newly formed Royalty Policy Committee, all of whose efforts are geared toward developing policy and procedures that will generate administrative cost savings.

Although we have had our differences with the MMS, RMOGA and COPAS have worked closely with MMS to develop an improved process for the collection and disbursement of Federal rental, bonus and royalty monies. There are still improvements that could and should be made — but made within the context of the existing system. The mineral royalty collection and disbursement functions must be retained in a centralized format. It is extremely difficult to envision a decentralized scheme which could be administered more efficiently or effectively.

RMOGA appreciates the Department's desire to reduce its budget. While the Devolution Proposal might reduce the Department's budget today, it might also reduce future revenues to the Federal government and the states. Devolution would require an expensive outlay of Federal monies and an indeterminate amount of time to convert the current federally-administered program to a state-administered one. The probability exists we would then return to the same point as thirteen years ago, with calls for a centralized method of determining oil and gas production from federal leases and collecting the royalties due.

NO REAL COST SAVINGS

RMOGA supports the government's efforts to reduce costs. However, the decentralization and transfer of the mineral royalty collection and production reporting functions to the states and tribes is not the best way to achieve cost savings. We view the proposal as simply a cost shifting measure — not a cost savings one — that will transfer the costs for the program from the Federal government to the states and state taxpayers, and result in even greater costs to the states, the industry and the Federal government.

The projected cost savings are not realistic. States and tribes will no doubt have to hire and train additional staff and implement systems alterations, including the purchase of new hardware and software. According to the proposal, the states and tribes would also incur other undefined "startup" costs. Although the Federal government is proposing to reimburse the states for their costs, it is proposing to increase the states' net administrative cost sharing to 50%, which will also include the loss of Federal funding for certain audit activities now performed by the states. Now, states are actually assessed less than 25% under a "cost capping" structure in which the lowest of several cost allocation calculations is charged. (Tribes and allottees receive 100% of revenues with no cost sharing allocations. This will continue under the new plan and Federal funds will be provided to the tribes to cover the cost of conversion.)

The increase in net receipts cost sharing to 50% coupled with the loss of Federal funding for performing audit functions will result in a net decrease in revenues to the states. In fact, a comparison of the Devolution Proposal's net impact to states which was prepared by the House Resources Committee staff indicates an overall annual loss to the states of nearly $8 million. Moreover, should the Federal government be required to fund the transfer beyond what is proposed, the estimated cost savings at the Federal level will be compromised and the states' net receipts share will decrease exponentially. How much will it cost each time the Federal government mandates a change, or whenever system upgrades are required by the Federal government?

The benefits of system uniformity and economies of scale now realized under the centralized system could also be severely eroded. RMOGA questions whether, overall, states and tribes can collect and disburse Federal mineral revenues at a lower cost than the Federal government, while performing comparable functions.

RELIANCE ON THE 1993 WYOMING PROPOSAL VULNERABLE

We question the DOI's reliance on the July 1993 "Wyoming Proposal to Implement Federal Royalty Collections Program for the State of Wyoming", which forms the foundation of many of the cost and savings estimates in DOI's proposal. The Wyoming Proposal compared to the federal system a vastly simplified state system that essentially supports data capture, error handling, remittance processing, accounting, and revenue distribution. However, it provides no capability for the comprehensive reference data maintenance, royalty error correction, exception processing, production error correction, sales volume comparisons, allowance tracking, verification, analysis, or reporting currently performed by the MMS (functions required by the states and tribes as well as the DOI Inspector General). Adoption of a system such as that contemplated by the Wyoming Proposal would likely result in decreased ability to perform these obligatory functions since it would necessarily eliminate many of the routines and audits included in the current MMS system which are intended to increase collections and compliance.

MULTIPLE ENTITIES PROBLEMATIC

According to the Department's proposal, at least four entities would perform royalty collection and production accounting functions: the states in which the leases are located, the Indian Tribal lessors, the BIA or another DOI agency, and the DOI agency which assumes responsibility for the offshore royalty collection as well as collection for those states that decline to accept the function. The potential exists for this number to increase substantially, and therein lies the basis of our concerns. Our comments today are directed specifically to the onshore portion of the Devolution Proposal.

"Inherently Federal functions" (those which cannot be delegated) and oversight of onshore royalty collections would be retained by the Federal government but transferred to "another DOI bureau". These functions include policy and regulatory development, valuation interpretations, adjudication of administrative hearings and appeals, issuance of legally enforceable bills or orders and imposition of penalties and sanctions. Functions which may be transferred from the Federal domain are receipt and monitoring of royalty and production reports, matching royalty reports with submitted payments, correction of errors on submitted reports, royalty accounting, most remaining compliance verification and audit functions, and administrative support. Enforcement of lease terms and royalty obligations must, by law, remain with the Federal government. Thus, enforcement orders and bills would be issued by the Federal government and would have to be appealed to the Federal government utilizing supporting materials furnished by the states.

Inconsistent Interpretation and Guidance

Transferring royalty collection and production reporting functions to the states will, in all probability, result in greater inconsistency in the interpretation and issuance of guidance concerning regulation and policy, thereby increasing payor uncertainty as well as the potential for costly, time-consuming litigation. The probability exists that state auditors will be influenced by their perception of their own state's position and laws. Since these positions vary from state to state — as well as from the Federal government's position — conflicting interpretations of the regulations will lead to added controversy.

Furthermore, legal questions could arise concerning the Federal government's ability to defend its position where conflicting interpretations exist among the states which have been delegated the authority to interpret and issue guidance on Federal regulations and policies. This, despite DOI's assurance it can accomplish "ultimate control" through the promulgation of "detailed, procedural requirements that leave no discretion to the individual carrying out the function".

Inconsistent Auditing

RMOGA is concerned states may utilize an inconsistent approach to auditing. Such inconsistency could implicate the Federal government in procedural disputes, increasing costs to the Federal government, the states, and the industry in resolving them. The Federal government will subrogate to individual and inconsistent state control the right to manage audit cycles and the closure of audit periods on a timely basis. In fact, these kinds of problems already exist in instances where the MMS has delegated audit functions to certain states. The fragmentation of centralized, interrelated functions will also increase the prospect of further delays in resolving disputes with the Federal government when, for example, states are collecting data and processing exceptions, but lessees are still required to settle with the Federal government. This could create significant management problems for the Federal government with respect to policy consistency and cost controls.

PROBLEMS WITH TIMETABLE

The proposed two year schedule for implementation of the transfer of royalty responsibilities is also a concern. Delegation of royalty functions to states and tribes will require enactment of enabling legislation to implement the transfer. The U.S. Congress will be required to amend FOGRMA to allow states and tribes to carry out additional delegable activities and to allow use of decentralized accounting systems. According to the Proposal, states and tribes will also be required to pass legislation in order to assume royalty collection functions. The premise of the Devolution Proposal seems to be that by spending large sums of money, the current Federal system — thirteen years and millions of dollars in its refinement — can simply be discarded, and a brand new, decentralized system can be developed which will operate "more efficiently and effectively" — in a mere two years' time! RMOGA doubts this can be accomplished within the time frame established by DOI.

For example, in 1993, the State of Wyoming discussed a timetable of two years for implementation of its Proposal (referenced above). At that time, Wyoming had scheduled implementation of its comprehensive computerized Mineral Tax System by October of 1993. That system took four years to develop, and was not brought on line until the first quarter of 1994 when the state's new reporting requirements were issued. More than a year later, the system is still problematic, inflexible, and does not address certain types of adjustments, such as prior conversions. Moreover, modifications to the system which would alleviate some of the problems are deemed too costly to perform at this time.

In another example, in 1987, the State of New Mexico formed a tri-agency task force to verify the need and to establish objectives for an enhanced automated information system. In 1988, the state initiated development of its state-of-the-art Oil and Gas Administration and Revenue Database (ONGARD) tax and royalty system. The production reporting component was placed on line in late 1994. The tax and royalty component was placed on line only last month.

These processes have been long and laborious efforts for both the states and the industry, and corroborate the likelihood that implementation of such transfer of responsibilities, including the development of a new system to verify production and royalty payments, will not occur in a two year time period.

ALTERNATIVES TO DECENTRALIZATION

We acknowledge the goals of the Administration and this Congress to decrease the size of government and save money. Much has been done the past several years to accomplish those goals. Our members participated in the Royalty Management Advisory Committee, Bureau of Land Management's (BLM) Onshore Oil and Gas Performance Review Incentives and Bonding Teams, the Federal Gas Valuation Negotiated Rulemaking Committee and Indian

Gas Valuation Negotiated Rulemaking Committee, the Allowance Study Team, the MMS Common Reference Data NPR Laboratory Team, the development of the Alternative Dispute Resolution process, and the MMS' pilot gas royalty-in-kind program. Each of these efforts has been a genuine attempt to simplify and streamline the functions of the MMS and to reduce costs for both government and industry. We question whether these existing measures were adequately considered when devolution of the MMS was proposed.

The DOI has projected startup costs at approximately $60 million. Instead, a more appropriate and far less costly solution would be to simplify, streamline, improve, modify and further refine the current Federal system.

We are proposing a number of alternatives in lieu of devolution of the MMS and decentralization of the Federal royalty collection and production reporting system. Our recommendations will result in significant cost savings for the government without materially affecting the accuracy of reporting or the collection of Federal royalties. Our recommendations would maintain the economies of scale and benefits of system uniformity realized under a centralized collection system. The critical data elements necessary to satisfy the Inspector General, the states, and the tribes that production is accurately reported and royalty due is collected would be retained. Overall, these recommendations will result in tremendous administrative cost savings for the Federal government, particularly in the areas of verification and audit — savings which will be shared with the states.

Simplify Valuation

First and foremost, the Federal government must simplify the valuation of oil and gas sales. Of all mineral lessors, the Federal government's requirements for reporting and paying royalties are the most aggressive. While we recognize the states value the revenues generated by the Federal government's gross proceeds philosophy, significant administrative cost savings could be achieved by revising the current valuation requirements without reducing, and in all likelihood thereby increasing, the states' net revenue shares. Moreover, eliminating the need for every dollar to be accounted for every month could provide some flexibility that would achieve cost savings associated with exception processing, interest calculations, and appeals.

Simplifying valuation should be accomplished by establishing a readily available and flexible indicia of value for the sale of oil and gas which is fair, represents local markets, and is not subject to dispute by the government upon audit. Where payments fall within an acceptable range of value, neither the producer nor the government has to trace the product to the wellhead or the end user to determine value. Reporting and paying royalties should return to the basics: volume and price. We understand the Federal government spends in excess of $23 million annually determining and auditing value. If the government and the producer both know how much the royalty payment should be at the time of production, a great deal of this expense could be saved.

Define Gross Proceeds

The Federal government should expedite its effort to define "gross proceeds". Although the Federal Gas Valuation Negotiated Rulemaking Committee was unable to concur on a definition of gross proceeds, it was agreed that it is essential to equitably, timely and clearly define what gross proceeds are in today's changing gas marketing environment. Again, where the producer and government know what the royalty payment should be at the time of production, vast amounts of unnecessary time and expense spent in determining and auditing value would be saved.

Simplify Reporting

Significant savings could be achieved through the simplification of reporting in several areas. Through simplification, the accuracy of reporting will be improved with a sizable cost savings to both industry and the government. The majority of the time and money spent by the MMS and industry is in correcting how information is reported rather than on identifying actual under- or over-reporting of royalties or incorrect production information. With fewer lines to report, requirements would be less complex, resulting in greater accuracy in reporting. Resources would be far better spent ensuring royalties are accurately paid to the appropriate property and recipient.

- Simplify MMS FORM 2014 reporting. The primary causes of reporting error are: 1) the level of detail required; 2) delays associated with processing the Payor Information Form (PIF); and 3) receipt of inadequate information concerning unit finalization from the BLM. We recommend eliminating or simplifying the selling arrangement, transaction, calculation, and revenue source codes to reduce detailed reporting requirements which necessitate review and re-review of data elements, yet result in no additional royalty collection. Moreover, simplifying the computer system structure would reduce costs for both the government and industry.

- Eliminate the filing of additional forms. Millions of dollars are spent each year by the government checking the additional forms required to be filed with the royalty report that are not verified until audit years later. Clear and simple payment practices based on factual sales data would eliminate the need for expensive checks and balances. We concur with the recommendation by the Federal Gas Valuation Negotiated Rulemaking Committee to eliminate transportation and processing allowance forms. Both industry and the Federal government will save time and money if not required to file, process and verify the information contained in these forms. According to the impending rule, the allowances will simply be reported as a line on the MMS FORM 2014.

- Adopt the new definitions for compression and transportation as contained in the Federal Gas Valuation Negotiated Rulemaking Committee Report. The definitions establish a bright line with regard to compression functions which are deductible and clearly differentiate between transportation costs which are deductible, and gathering costs which are not. Clarifying these terms will eliminate uncertainty on the part of the payor and challenge by the government.

- Review the PIF process to determine whether PIF filings could be eliminated. The primary purpose of the PIF is to ensure accuracy of reporting, however, it seems only to ensure a PIF was previously filed for those codes that identify the purchaser, type of sale, etc. MMS could utilize a simplified form identifying the payor for a specific property and obtain the additional information from other sources within the DOI.

- Simplify the MMS FORM 2014 and MMS FORM 3160 by eliminating redundant or unnecessary information. Often, a data element may be perceived as being necessary or useful, but when weighed against the cost to provide and verify the data, it just makes more sense economically to reject the data element.

- Expedite the procedure under which information on units is received from BLM and processed by MMS. This will allow industry to pay royalties on a unit, rather than a lease, basis much sooner and eliminate the need for retroactive adjustments.

- Add a transaction code or adjustment reason code to the MMS FORM 2014 to accommodate prior period adjustments when a change in the government Accounting Identification (AID) number and/or revenue source code (as requested by the MMS/BLM) has occurred. This would minimize circumstances in which payors are billed for late reporting when, in fact, prior period adjustment are actually being reported.

- Allow prior period adjustments to be reported on a "net" basis. The current regulations require adjustments for prior periods to be made by reversing the prior report line and then re-entering the correct line. Allowing industry to report the adjustment on a "net" basis would eliminate the need for the government to review millions of lines which are reported by payors each year and which involve insignificant amounts of money or are simply the correction of a coding error. Net basis reporting would also encourage more Electronic Data Interchange (EDI) reporting and reduce the system maintenance costs necessarily incurred by retaining massive amounts of historical reporting data.

- Change estimated payments from the lease level to the payor level. The current requirement to file and pay estimated payments on the lease level is burdensome on both industry and the government. Changes in the gas market have made lease level estimates unreasonable. Producers move in and out of the market, change markets, and routinely sell and purchase properties necessitating the monthly monitoring and updating of estimated payments to avoid interest assessments. Industry is often penalized with interest assessments because it is difficult, if not impossible in some instances, to maintain estimates correctly on an individual lease basis. Establishing estimates at the payor level would greatly simplify the process and eliminate the need to allocate, monitor and adjust lease-based estimates. This would eliminate a significant administrative burden for the government as well.

Redefine thresholds

Current MMS regulations and systems require an accuracy that would not satisfy a cost/benefit analysis in terms of dollars spent for dollars received. Measuring, tracing and accounting for oil and gas production is not an exact science. Many of the government's system tolerances are so low that in pursuing such small differences, the government spends more money than is actually recovered in additional royalties. We recommend modifying the system tolerances and thresholds so that only those exceptions which are cost beneficial for the government to pursue are generated. Including minor adjustments in current month reporting would streamline the process without materially affecting the accuracy of reporting for current or prior periods.

With regard to AFS/PAAS (Auditing and Financial System/Production Accounting and Auditing System) discrepancies, we recommend requiring overpayments be verified. This would eliminate the need for the MMS to issue invoices for reporting/coding errors. It is an unnecessary administrative burden to ensure reporting errors are corrected in instances where no additional royalty is due.

With respect to penalty and interest invoicing, MMS currently invoices payors for penalties and interest each time an error is made. The processing costs often exceed the revenue recovered. If thresholds were raised or if the amounts due could be combined until they reached a certain threshold, the cost savings would be significant.

Expansion of Royalty-in-Kind Program

The Federal government could realize additional savings by developing a gas royalty-in-kind program for onshore leases similar to the pilot program developed for Outer Continental Shelf leases. Removing the Federal government from the business of determining proper value could certainly result in dramatic administrative savings, particularly in the audit arena.

There are many other cost-saving measures we would like to discuss with the Department. Taken together, all of these modifications to the current process could be attained at a bargain price, compared to the Devolution Proposal. Moreover, they would result in significant administrative savings to the Federal government and, in turn, increase revenues to the states.

FINAL CONCLUSION

RMOGA welcomes the opportunity to meet and discuss our recommendations with members of the Subcommittee at your convenience. We also look forward to the opportunity to discuss our recommendations and to participate in further studies of the current system with the Department of Interior and Minerals Management Service as part of our continuing efforts to reduce administrative costs and burdens for both the government and the industry.

Written Testimony of

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Before the

Energy and Mineral Resources Subcommittee

of the

House Resources Committee

Regarding the Reorganization of the

Minerals Management Service

June 8, 1995

Enserch Exploration, Inc.
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Comments Regarding MMS Devolution

Enserch Exploration, Inc. ("Enserch") of Dallas, Texas has been in the exploration and production business since the early 1900s and drills exploratory and development wells for natural gas and oil, operates producing wells and markets gas and oil. Although operating in many areas of the United States, Enserch has significant reserves on federal onshore and Indian lands.

Enserch supports the efforts of the Administration to "reinvent" federal government agencies in order to reduce costs, gain efficiencies, and streamline processes. However, Enserch does not believe the Interior Department's proposal to devolve the responsibilities of the MMS will achieve these goals. Rather, we view the proposal as merely a cost shifting measure that will significantly increase the costs and burdens on industry, the states and Indian tribes, with no corresponding benefit other than a minimal reduction in the federal budget.

Enserch opposes the MMS devolution proposal for a number of reasons. First, management of federal lands, including oil and gas collection and accounting, is inherently a federal function which should remain at the federal level. Second, a centralized agency such as MMS can be more efficient and economical in collecting royalties than 67 state and Indian agencies. Third, transfer of MMS functions to the states and Indian tribes, would increase the administrative burden on oil and gas producers with no corresponding benefit. Fourth, the proposed transfer of MMS functions is dependant on cooperation by the states and Indian tribes, which may not be receptive to the proposals. Finally, we believe that the solution to MMS's current problems is to streamline the current system and make it fair rather than simply delegating minerals management responsibilities to the states and Indian tribes. Each of these points is discussed in more detail below.

1. The transfer of MMS functions to the states and Indian tribes would increase the administrative burden on oil and gas producers with no corresponding benefit.

Many oil and gas operators, like Enserch Exploration, Inc., have operations on federal lands in numerous states and on different tribal leases. The MMS offers the convenience of "one stop shopping" for these operators. The initial cost for producers to alter their current reporting and paying systems could exceed millions of dollars. Thereafter, the increased costs to producers with operations in numerous states and tribal leases would be substantial. Instead of a single point of contact for all collection processes, producers would have up to 67 contacts. The number of filings would multiply proportionately. Moreover, producers have an established relationship with MMS that they are familiar with. It would be time-consuming and difficult for producers to establish relationships with up to 67 new agencies. While theoretically each state would administer standardized policies regarding collection, auditing, regulatory interpretation, etc., in reality each state would have its own variations in the application of federal guidelines. Thus increased administrative costs and red tape for producers would be inevitable.

The initial effect on producers would be increased administrative burdens and resulting increase in costs. The longer term effects would very likely be decreased exploration and production on federal lands and a decrease in bonuses and royalties payable to the federal government, the states and Indian tribes. Thus, the net effect of these proposals to save the federal government a few million dollars could very well be a substantial decrease in the federal government's third largest source of revenue.

2. Management of federal lands, including oil gas collection and accounting, is inherently a federal function and should remain at the federal level.

Interior Secretary Babbitt was recently quoted as saying, with regard to the MMS proposals, "These cuts will help us get back to the core responsibilities that are at the heart of Interior's mission." These core responsibilities are defined by Secretary Babbitt as "protecting and managing over 500 million acres of federal land, carrying out related scientific research, ensuring an equitable return on resources, and fulfilling trust responsibilities to Native Americans." We are very concerned that Secretary Babbitt does not indicate that a core function of the Department of Interior is to ensure the orderly and timely exploration and development of mineral resources to meet the energy needs of the Nation as mandated by the Outer Continental Shelf Lands Act.

Mineral royalty collection by MMS is the federal government's third largest revenue source after the Internal Revenue Service and the U.S. Customs. Moreover, all fifty states are beneficiaries of the federal government's share of royalties from federal lands. The federal government has a non-delegable fiduciary obligation to maximize those revenues on behalf of every United States citizen.

As noted in the March 27, 1995 Proposal to Devolve the Responsibilities of the Minerals Management Service, a December 16, 1994 opinion by the Associate Solicitor for General Law describes certain functions which are "inherently federal" by nature and cannot be devolved to private citizens, even by legislation. The opinion states:

> It would appear that the same analysis would apply to states and Indian tribes. Functions which involve the exercise of significant executive power by the United States, which under the Constitution is vested in the President, must be performed by employees of the Executive Branch of the Federal Government. These functions have been described as those that require "either the exercise of discretion in applying federal authority or the use of value judgment in making decisions for the Government. The functions include enforcement of federal law and related legal actions; administrative adjudications; exercise of rulemaking authority vested in Federal Officers such as the Secretary of Interior; and the exercise of ultimate control over the acquisition, use, or disposition of United States property including the collection, control or disbursement of appropriate or other federal funds. In this latter instance, ultimate control can be accomplished by promulgating

detailed procedural requirements that leave no discretion to the individual carrying out the function. Under those circumstances the individual who carries out the function need not be a Federal employee.

While the Associate Solicitors' opinion did not address the specifics of the MMS proposal, it would appear that the only responsibilities that can be legally devolved to the states and tribes in connection with federal minerals management are "ministerial" duties which do not involve the exercise of discretion. If these are the only responsibilities that can be devolved, then there is simply no justification for the proposal other than to shift the costs and burdens of the ministerial functions associated with minerals management to the states and Indian tribes. Given all of the problems that will result from MMS devolution, discussed below, we believe the minimal cost savings for the federal government is an insufficient justification for the proposal.

The original reasons the MMS was created were under-collection of royalties (estimates up to several hundred million dollars), lack of an enforcement system, disarray in recordkeeping, poor coordination between field inspectors, accountants and auditors, and poor verification efforts. The original reasons for the creation of the MMS are still valid reasons to keep the functions of MMS centralized at the federal level. The MMS was established by Secretarial Order No. 3071 on January 19, 1982, as a result of the report of the Linowes Commission on Fiscal Accountability of the Nation's Energy Resources. The fundamental conclusion of the Linowes Commission was that "proper fiscal accountability and management of the public's mineral resources necessitates an independent minerals agency devoted solely to minerals management." The conclusion of the Linowes Commission is as valid today as it was in 1982 when the MMS was created. Proper fiscal accountability and management of the federal government's mineral resources require a single independent minerals agency at the federal level devoted solely to minerals management.

Finally, as noted in an April 10, 1995 Oil and Gas Journal editorial, "a tenet of modern management is that no one handles an asset more carefully and profitably than does its owner." The states and Indian tribes may not have a sufficient incentive to collect royalties from lands they do not own. The federal government, as the owner of the mineral resources, has the greatest incentive to efficiently manage these resources.

3. A centralized agency can be more efficient and economical in collecting royalties than the 38 state and 29 Indian agencies.

The transfer of royalty collection functions to the states and Indian tribes would be a cost shift, not a cost savings. Moreover, it is reasonable to assume that the total real costs would increase if royalty collection functions are shifted to the states and tribes. Centralization results in economies of scale and helps keep costs associated with performing these activities as low as possible.

As noted above, only "ministerial" type functions can be delegated to the states and Indian tribes. Under a decentralized system, each of the states and tribes would have to follow detailed federal guidelines regarding policies, reporting standards, formats, deadlines, etc. The real cost to maintain uniformity of federal guidelines within 67 agencies would be significantly greater than the cost to maintain the guidelines within a single federal agency.

The primary issue concerning the MMS proposal is not whether the proposal will save the federal government money. Clearly, the federal government will realize some minimal savings by shifting costs to the states and Indian tribes. However, the critical issue is whether implementation of the MMS proposal will result in a net savings to the citizens of the United States, who must pay taxes to the states and Indian tribes as well as the federal government. The answer, we believe, is that the MMS proposal would result in a net cost increase to taxpayers because these functions can be handled more efficiently at a centralized level.

The New Mexico Oil and Natural Gas Administration and Revenue Database system development time was approximately 7½ years at an estimated cost of $21 - $25 million. It is hard to believe the Interior Department's projection that a new system could be developed to handle royalty payments for the entire federal oil and gas production within 6 - 18 months at a cost of $15 million.

4. The transfer of MMS royalty accounting and collection functions is dependent on cooperation by the states and Indian tribes, which have little incentive to accept such transfer of responsibilities.

This is potentially an unfunded mandate which the states are not required to accept. In order for states to maintain revenue neutrality, they must reduce by 50% the present cost to administer the royalty management programs. Fifteen million of the MMS cost savings would be transferred as costs to the states by increasing the state allocated percentage of royalty management administrative costs from the present 25% to a proposed 50%. Several states have said if they do not get the funds but get the task, they will increase severance tax and fees. The current cost to collect royalty and to manage the associated support activities for onshore federal leases is $54.4 million. The Department's proposal used an estimate of $7 million to run the entire onshore program. We are doubtful that a reduction of $47.4 million, or 87%, can realistically be achieved.

Moreover, under the existing proposal, the states could be penalized for failing to comply with federal requirements. The states do not have a sufficient incentive to agree to an additional penalty burden.

The MMS proposal anticipates that the oil and gas accounting and collection functions will be assumed by tribes willing to undertake the responsibility. However, it is hard to believe the tribes would want to assume responsibility for services now provided by the federal government. Also, as noted in the March 27, 1995 proposal, the Secretary's trust responsibility is not fulfilled by compacting with a tribe. If the tribe's royalty management program is deficient, the federal government still may be liable to the tribe for financial consequences. Accordingly, the proposal notes that "the Department must be prepared to take back royalty management functions from the tribes." It appears that the MMS proposal with respect to the Indian tribes is tenuous at best.

5. The most efficient way to achieve the Interior Department's goal of cost reduction is to streamline the current MMS royalty accounting and collection system and make it more efficient.

Enserch offers the following suggestions to streamline current centralized reporting and payment processes that we believe will result in significant cost savings to both industry and MMS without the uncertainty and startup costs associated with the devolution proposal:

Product Evaluation

In today's natural gas marketing environment, gross proceeds as defined by the MMS is increasingly difficult to ascertain. This is because of the tremendous changes in the natural gas marketing environment that have occurred as a result of open access and deregulation. Consequently, natural gas is now often sold far downstream of the wellhead after it has been aggregated with many other sources, complicating the valuation of natural gas for MMS royalty purposes and the costs associated with ascertaining this value. Accordingly, Enserch recommends revising the current MMS product evaluation regulations along the lines of the recommendations developed by the Federal Gas Valuation and Indian Negotiated Rulemaking Committee.

Interest

Fairness will be achieved by establishing a reciprocal right to interest for both industry and the government by providing for the right to interest on overpayments made to the Secretary of the Interior. The Internal Revenue Service allows interest on overpayments and underpayments and the MMS should do the same.

Statute of Limitations

The rights of industry and MMS under existing statutes are not reciprocal. The limitation period, in order to be fair and reasonable, should be three (3) years applicable to both industry and government, which is the same time limitation period currently allowed under the IRS statutes.

Offsets

Industry should be able to credit overpayments against outstanding obligations as a cost effective and efficient accounting mechanism.

Elimination of Allowance Forms

The Federal Gas Valuation and Indian Negotiated Rulemaking Committee's recommendation relative to the elimination of processing and transportation allowance forms and the definitions of compression and transportation should be implemented. This would bring quick and immediate administrative cost savings to both the MMS and industry with no loss of control.

"Marketable Condition" Rules

The marketable condition rules should be revised to allow lessors to pay the federal government like other royalty owners. Royalty owners understand that if the product is not marketable when it comes out of the ground then it has limited value. They understand that it is the lessee's responsibility to produce the product free of cost to the royalty owner but that royalty owners must bear their proportionate share of the cost to enhance the value of the product in order to make it marketable. The oil and gas industry spends millions of dollars just to satisfy the federal marketable condition rules, and the federal government spends millions of dollars to make sure that industry has complied with the rules. Instead, the federal government should be treated like any other royalty owner when it comes to bearing the costs to make the product marketable.

Reporting Procedures

Millions of dollars in costs each year could be eliminated if the MMS would work with the industry to eliminate or streamline the level of reporting on the MMS Form 2014. The current costs associated with MMS Form 2014 reporting could be significantly reduced with little or no loss on the MMS's ability to monitor and control royalty payments. Specifically, MMS could eliminate or simplify selling arrangement codes, transaction codes, payment method codes, calculation codes, adjustment reason codes, and revenue source codes.

In summary, Enserch Exploration opposes the devolution of the MMS onshore responsibilities to state and Indian tribe agencies as it will continue to be best administered by the federal government and urges the Subcommittee to carefully consider the ramifications of the Interior Department's proposal. Thank you for the opportunity to submit written comments on this proposal.

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ISBN 0-16-047699-2
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