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Minerals Management Service
Royalty Management Program
Rules and Procedures Staff
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Gentlemen:

On September 23, 1996, the Minerals Management Service (MMS) published in the Federal Register a notice of proposed rulemaking entitled "Amendments to Gas Valuation Regulations for Indian Leases." The MMS requested that comments on the notice be submitted on or before November 22, 1996. Please accept the following as the formal comments of the Southern Ute Indian Tribe (Tribe) regarding the proposed amendments to the regulations found at 30 CFR Parts 202 and 206.

General Comments

As a participant in the development of the proposed amendments, the Tribe supports the general concepts recommended by the Indian Gas Valuation Negotiated Rulemaking Committee. Many of the key elements of the amendments were the result of thoughtful dialogue and reasonable compromise. The Tribe believes that the amendments accomplish the overall objectives of the committee, specifically those of simplification, certainty and fairness coupled with the recognition of the federal trust responsibility to maximize Indian revenues in accordance with the lease terms.

The Tribe commends the MMS on its decision to institute Indian gas valuation regulations that are separate from those which govern the valuation of federal lease production. Indian leased lands and federal public lands are sufficiently different to warrant separate treatment and regulation. The concept of separate regulations was supported by many in the Indian community

during the development of the 1988 valuation regulations. Furthermore, with the passage of the Royalty Simplification and Fairness Act affecting federal, but not Indian leases, the Tribe believes that separate regulatory treatment is now even more crucial.

Because the Tribe's leases are within the San Juan Basin, the comments submitted here will be mostly confined to those amendments which will impact Indian leases within an index zone. It should be stated, however, that should the San Juan Basin ever be disqualified as a valid index zone, the very foundation of these amendments would be unsound and the regulations would require significant revision.

202.550(a)(2)

The MMS has requested specific comment as to whether individual allottees' consent is required to reduce the royalty rate if a lessee demonstrates an economic hardship. The standard allottee lease form in paragraph 3(g) states that "...no regulation hereafter approved shall effect a change in the rate of royalty or annual rental herein specified without the written consent of the parties to this lease..." and in paragraph 13 the standard lease states "...every benefit hereof shall inure to, the heirs, executors, administrators, successors of, or assigns of the respective parties hereto." Given the lease language, the MMS probably should not grant a royalty rate reduction to a lessee on an allotted lease without the lessors' consent.

202.550(b)

The Tribe supports the payment of royalty on entitled volumes rather than actual takes. The standard Indian lease form requires that the lessee pay royalty monthly on the volumes "produced and saved" and contemplates the payment of royalty on an entitlements basis.

206.172(b)(2)(ii)

The Tribe agrees with the long-standing position of the MMS that royalty is due at a minimum on all the components of a lessee's gross proceeds, including certain amounts received by the lessee to settle a gas sales contract dispute with a purchaser of the lessor's royalty gas. These amendments should include a provision that supports the continued collection of royalty on the lessees' gross proceeds.

206.172(b)(3)

The Tribe supports the notion that gas sold under dedicated contracts be valued at the higher of gross proceeds or the index formula price.

206.172(d)(1)

The index based formula, which can be described as the average of the average of the highest publication prices, is the result of extended discussion within the committee. The Tribe believes that, while this final formula was not that on which the committee originally reached consensus, it does reflect the spirit of compromise and accomplishes the committee's goals.

The formula is based on information which is readily available to the public in a timely manner. It is a simple calculation of averages and, unlike the existing regulations, does not require significant commitment of industry staff time to accomplish correctly nor MMS/Tribal audit staff time to verify. Also unlike the existing regulations which speak of median value, it properly recognizes the meaning of Indian lease language related to the payment of royalty based on the *highest* price paid or offered for a major portion of field production.

206.172(d)(2) through (6)

The committee recommendations resulted from its conclusion that the published index price ranges are in fact reflective of market value and that they are not manipulated in any way to wrongly benefit any person or party. The committee further concluded that, as currently determined, the published indices are sufficiently valid as a basis for a major regulation. It is imperative that the MMS continually validate the published index prices and that technical conferences be held without hesitation if the MMS suspects that any published index price may no longer reflect market value.

206.172(e)

The Tribe believes that a safety net comparison of values is absolutely essential for the protection of the Indian lessor and for the validation of the published index price ranges. The once-a-year calculation of a safety net price is a small concession by Indian lessees to accomplish certainty and to foster general confidence in the validity of the published index prices. The calculation of the safety net price does not require a detailed "tracing" of molecules produced from all Indian leases to all distant sales points. The safety net calculation is designed to accomplish the committee's goals, specifically that of closure, in the simplest manner possible.

The proposed regulation permits only one year for the MMS to verify a lessee's safety net calculation. Because of the importance of the safety net to Indian lessors, the Tribe recommends that the MMS establish formal procedures and staff resources to verify the safety net calculations within the one year period allowed by the proposed regulation.

206.173

The proper performance of dual accounting has been for most Indian lessees, at the very least, extremely difficult. For many, the task has been nearly impossible largely because of the unavailability of the information necessary to account for comparison. Yet the calculation is required by the standard Indian lease language. The Tribe supports the alternative methodology for dual accounting as an option available to Indian lessees. The Tribe disagrees, however, with the use of weighted average BTU content for the lease and believes that, for the purposes of the alternative dual accounting method, the use of individual well BTU values would result in a more accurate calculation. The final method described in the proposed amendments, however, was the committee recommendation offered in the spirit of compromise and should satisfy the lease requirement that dual accounting be performed.

206.174(g)(2)

The MMS has requested specific comments as to whether or not there should be a minimum value for gas plant products when a lessee chooses the actual dual accounting methodology. The amendments specify that this minimum value will be the *average minimum price* reported in commercial price bulletins less an estimated transportation cost. The standard Indian lease requires that royalty be paid on the *highest price* paid or offered for all hydrocarbon substances produced from the lease. The Tribe believes that the amendments take too broad a leap to get from the lease's *highest price* to the regulation's *average minimum.* To better satisfy the lease requirement, the amendments should, instead, require that the minimum value for gas plant products be based on the highest price or at the very least the average of the highest prices found in commercial price bulletins.

206.175

The collection of BTU data by well on the Form MMS-3160, Monthly Report of Operations, is an essential component for the verification of the dual accounting calculation when the lessee chooses the alternative methodology. The Tribe supports this data collection effort.

206.178(a)(1)(i)

In those instances when a lessee must report a separate actual transportation allowance deduction, the Tribe supports the requirement that the lessee submit to the MMS the contracts or cost information on which that deduction is based. The information contained in those contracts or cost reports will permit the timely verification of the deduction and satisfies the committee's goal related to closure.

206.179

The Tribe agrees that extraordinary cost deductions have no place in the regulations governing the calculation of Indian royalty.

Conclusion

The Southern Ute Indian Tribe supports the promulgation of this much needed regulation. It will result in long-awaited substantial benefits to both industry and Indian lessors. In this era of industry down-sizing and organizational restructuring within the federal government, it should be recognized that more efficient methods of conducting business must be explored and implemented. Simplification in the name of efficiency, however, should also result in recognizable benefits to Indian tribes and allottees. The Southern Ute Indian Tribe believes that these amendments, taken as a whole, achieve that goal.

Regards,

Leonard C. Burch, Chairman
Southern Ute Indian Tribal Council