Abilene
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Houston
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Los Angeles
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Mississippi

New Mexico
New Orleans
Ohio
Oklahoma City
Oklahoma-Tulsa
Permian Basin
Rocky Mountain
San Antonio
San Francisco
San Joaquin
San Juan Basin
Wichita Falls

April 26, 1999

Mr. David S. Guzy
Chief, Rules and Publications Staff
Minerals Management Service
Royalty Management Program
P.O. Box 25165, MS 3021
Denver, CO 80225

Comments on Revising an Existing Information Collection
Report of Sales and Royalty Remittance (MMS – 2014)
64 FR 8835 (February 23, 1999)

Dear Mr. Guzy:

The Council of Petroleum Accountants Societies (COPAS) appreciates the opportunity to comment on MMS' proposed revisions to the Report of Sales and Royalty Remittance, MMS Form 2014. COPAS members have extensive experience in working with this report and have a mutual interest to share the benefits of reducing the volume of lines, minimizing errors, simplifying reporting and lowering costs. Therefore, we believe our comments will be beneficial in improving RMP processes for both the MMS and industry.

General Comments

COPAS commends the MMS for its efforts to revise reporting requirements and to re-examine the reporting process. Industry is appreciative of MMS' receptiveness to its ideas and the results are very evident in the Federal Register Notice. Although many items are addressed in our comments, COPAS is most concerned with the valuation code, the API well number, and agreement level reporting. We continue to look forward towards achieving common goals with the MMS.

Specific Comments

Reporting Concepts:

COPAS National Office P.O. Box 1190 Denison, TX 75021-1190
Phone: (903) 463-5463 FAX: (903) 463-5473

PIF

COPAS agrees the Payor Information Form should be eliminated. The MMS is requested to explain how it will determine when a party is responsible for the royalty payment in the absence of the PIF.

Product Valuation

Of all of the proposals, the requirement to report separate lines for different types of sales is one of COPAS' biggest concerns. Many of the companies aggregate their volumes in pools and then sell or exchange their product under multiple contracts that fit into the many different categories of contracts listed by the MMS. This is not necessarily limited to large integrated oil and gas companies selling to their affiliates. Some of the smaller reporting companies also conduct activities subject to the valuation code. The accounting systems do not have this information and are not equiped to produce the detail that the MMS is expecting. In order to comply with the proposed reporting requirement, industry would have to perform arbitrary allocations of the pool volumes to the different contracts. To give you an idea of how burdensome this would be, one company had an example that would require them to analyze 146 sales from one pool and then allocate volumes to different contract categories and apply the weighted average price from each category. In addition, the reporting requirement will have a significant increase on the number of lines sent to the MMS. Another company has reviewed the impact of the change and estimates the number of lines reported will increase by 30%. This increase is just on the reporting of the initial sales. Within the first six months of a pool sale, adjustments normally occur that will produce prior period adjustments and will further multiply the number of lines reported to the MMS. In one example, a company's pool had four different contract categories. When an adjustment is made, four more lines will be created. Assuming the initial sale and one prior period adjustment for 100 leases, the valuation code will cause an increase in lines from 200 to 800 lines. Much of the discussion focused on gas but the valuation code is also burdensome to oil reporting given gravity bank adjustments and BS&W.

In addition, further analysis would be required to breakdown transportation and processing costs between the different contracts. This information is not tracked in the pool. Again, this information is not captured in the accounting system and would require additional analysis. There is also some concern that the valuation codes also apply to the identification of transportation and processing allowance deductions. COPAS requests MMS to clarify if the valuation codes will apply to allowance deductions (arm's length versus non-arm's length transportation).

COPAS noted several other issues that do not appear to be addressed in the proposal. For example, some valuation situations do not have a unique code to identify the valuation method. Examples are Dual Accounting and Majority Pricing. Would these situations require identification as arm's length versus non-arm's length? Another problem is where the operator is paying on behalf of other working interest owners but does not know if the contract is long term, spot, arm's length or non arm's length.

The proposal conflicts with the stated objectives of reducing the volume of lines, reducing errors, simplifying reporting and lowering costs to both industry and the MMS. The proposal will create an accounting nightmare. In addition, the categories defined by the perception of today's contracts will likely change as the market changes. This could lead to more reporting complexities. Both large and small producers will be adversely affected by this requirement and believe the benefit to the MMS is extremely limited. However, COPAS is willing to sit down with the MMS, review our concerns and look at alternatives to this requirement. In the absence of any alternatives, COPAS recommends the elimination of this data element.

Reporting Adjustments

Payors that submit a large number of lines support this initiative because it will significantly reduce the number of lines and reduce the edit errors requiring correction. It is recommended that any edits performed by the MMS should be performed only after the netted line is consolidated with the original entry. Payors with smaller reports believe that reporting net adjustments should be an optional requirement.

Transportation and Processing

COPAS supports reporting transportation and processing allowances on the same line as the royalty. We agree this will greatly reduce the number of lines reported by industry.

An issue that needs to be addressed by the MMS is royalty in kind leases where the transportation charge is a recovery. The MMS needs to address if the recovery should be reported on separate lines and any other coding requirements such as a unique payment method code.

Data Elements:

Indian Report Indicator

It is proposed that if the indicator is left blank, then the report is assumed to be Federal. This may be inconsistent with EDI applications that require the field to be marked.

Payor Assigned Document Number

COPAS recommends the MMS use this field as a reference on communications with payors where a reporting item is questioned. The current six digit field was changed from alpha-numeric to numeric a few years ago. COPAS requests an explanation of why the field has been expanded to eight digits and changed to alpha-numeric.

<u>Reserved for Payor's Use</u>

Most companies use this field to reference a property name. Again, this information is useful to industry and should be used in communication with payors where a reporting item is questioned or when payment files are provided by the MMS to payors.

<u>MMS Lease Number</u>

There is some confusion as to why both the lease number and the agreement number are required for a unit or communitization agreement. MMS is requested to provide more explanation as to the reasons for requiring both data elements for this situation.

<u>API Well Number</u>

This is another area of COPAS' greatest concerns. This data element is not maintained by industry in their accounting systems. In addition, industry captures sales data on a lease level basis but sales are not allocated by well. Therefore, MMS is requested to eliminate this data element.

<u>MMS Agreement Number</u>

The industry is concerned that the number may be unavailable at the time of reporting. If the agreement number is the same number used by the BLM, what number will be used if it has not been assigned by the BLM? Will the MMS expect the payor to contact the BLM or will the MMS be responsible for getting the agreement number?

<u>Product Code</u>

MMS is requested to provide a definition for the coalbed methane product code. The current terminology is not clear and industry is uncertain of its ability to identify this product without knowing the criteria for identification.

<u>API Gravity</u>

COPAS recommends eliminating this data element because it is being furnished on the production reports. Therefore, reporting this information is redundant.

<u>Valuation Code</u>

COPAS recommends eliminating this code. Please reference the comments above on Product Valuation.

Transaction Code

MMS is requested to review the existing transaction codes and delete codes that are no longer used or allowed.

Adjustment Reason Code

Reference the comment above on the Transaction Code. The codes should be reviewed in light of net adjustment reporting. In addition, the MMS may need to consider additional codes for adjustments due to audit and AFS/PAAS exceptions.

MMBtu Sales Volume

COPAS requests the MMS to clarify what volume should be reported on POP contracts (residue or wellhead).

Royalty Rate

COPAS recommends the data element be eliminated because the BLM or MMS Offshore should have the information in their systems. Therefore, reporting this information would be redundant for industry.

Unit Price

COPAS recommends the data element be eliminated but replaced with the Sales Value. The MMS could then calculate a Unit Price.

Payment Method

Payment method code 4 (royalty-in-kind) should be deleted.

Report Control Block:

MMS is requested to expand the Control Block to provide the capability to report any bills that are included with the 2014 report.

Agreement Level Reporting:

Within industry there is some debate about this proposal. Industry sees benefit to reducing the number of lines reported to MMS but also sees other problems created by the proposal. COPAS has several concerns about how the MMS will handle agreement level reporting on Indian leases. For example, the proposal does not address reporting procedures for handling dual accounting, recoupment of overpayments, reporting on mixed agreement units involving Federal and Indian leases, or where payments are made to Indian Tribes or allottees on a different valuation basis.

Another concern is the allocation process used by MMS to each lease in the agreement. If the MMS allocates volumes and values to all leases in the agreement, it appears the allocation will result in a portion of the funds being allocated to another lessor's lease obligation. If one party does not pay or underpays their royalty, it appears that all unit owners will be seen as underpaying their royalties. In this case, the funds should be applied only to those leases that the lessor has a lease settlement obligation.

When AFS / PAAS discrepancies are generated, it will be difficult and time consuming for the payors to determine the party responsible for underpayment without knowing MMS' royalty allocation. In turn, this may put some lessors at risk of loosing the lease. It is perceived that industry will continue generating tract level data to analyze any AFS / PAAS discrepancies.

Finally, it is unclear on what is meant in the proposal, "does not support designee / designor requirements of RSFA". Because the statement seems to indicate the proposal does not comply with the law, please provide further explanation and clarification.

Report Format and Presentation:

COPAS prefers the landscape version because it is the format that has been used for several years.

Paperless Reporting:

Industry's experience is that electronic reporting is most beneficial in the areas of providing the information more timely and accurately to the MMS. By eliminating MMS' keying of the data, the information is more readily available to MMS in their system and errors are greatly reduced. Electronic reporting does not impact the amount of time spent by payors to gather, interpret and input data to a form. Instead, the payor's time is impacted more by the additional reporting requirements that are not part of the normal lease payment process.

Reporting Burden:

COPAS believes the new valuation code requirement will significantly increase the number of lines reported on the 2014 and the time spent analyzing and allocating volumes, values and deductions among the different contract categories. The proposal will significantly increase the burden on industry. Further, the estimates to complete one line of the 2014 appear to be underestimated. When the burden is recalculated to consider the underestimate and the valuation code, the total reporting burden for industry will drastically increase the current stated estimate. In addition, the savings on eliminating the PIF may be overstated as the payor is required to assemble the data for the royalty report.

Summary

COPAS appreciates the effort and thought that MMS has put into the proposal. Overall, the proposal is positive and moving in the right direction. We look forward to MMS' response on the comments submitted by industry. COPAS understands MMS' objectives and is willing to meet with the MMS to address the concerns as outlined above and further explore additional alternatives.

Conclusion

COPAS appreciates the opportunity to provide comments to the proposed 2014 revisions. If you have any questions regarding these comments, please call me at 405-552-4721.

Sincerely,

G. H. Wade

Gary Wade
Chairman, COPAS Federal Affairs Subcommittee

CC:
Sandy Launchbaugh
Mary Stonecipher
John Clark