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CONFIDENTIAL

TELECOPIER (FAX) COVER SHEET

TO:	David S Guzy Chief, Rules and Procedures Staff Minerals Management Service	**DATE:**	November 3, 1997
FROM:	Lawrence J. Dreyfuss Vice President and General Counsel	**FAX NO.**	(303) 231-3194
NO. OF PAGES:	5		

COMMENTS: Also submitted by e-mail pursuant to NOPR. Thank you.

PLEASE CONTACT MANOOSH PENROSE AT (713) 646-4389 IF ANY PROBLEMS OCCUR IN RECEIVING THIS FAX. SENDER'S TELECOPIER NO. IS (713) 646-4216.

PLEASE DELIVER THIS FAX IMMEDIATELY UPON RECEIPT.

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Lawrence J. Dreyfuss
Vice President
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November 3, 1997

VIA FACSIMILE
(202) 231-3194

Mr. David S. Guzy
Chief, Rules and Procedures Staff
Minerals Management Service
Royalty Management Program
P. O. Box 25165
Denver, CO 80225-0165

Re: Proposed Rules
Department of the Interior, Minerals Management Service, 30 CFR Parts 206 and 208
"Establishing Oil Value For Royalty Due on Federal Leases and on Sale on Federal Royalty Oil," NOPR, 62 Fed. Reg. 49460 (September 22, 1997); NOPR, 62 Fed. Reg. 3742 (January 24, 1997)
(Our File L1030)

Dear Mr. Guzy:

I appreciate the opportunity to provide the following comments regarding the proposed rule for establishing oil value for royalty due on federal leases and on sale of federal royalty oil. This letter will supplement the comments of Scurlock Permian Corporation ("SPC") dated April 17, 1997.

SPC has its headquarters in Houston, Texas. SPC is a gatherer and marketer of crude oil in the United States. SPC employs over 900 people with operations in 15 states. SPC operates more than 2,400 miles of active crude oil gathering lines and pipelines. SPC also operates a fleet of more than 300 tractor-trailers to gather crude oil. SPC also has crude oil tankage at 154 onshore terminal locations plus 12 marine terminals.

Neither SPC nor any of its affiliates, including its parent Ashland Inc., owns or leases significant crude oil producing properties. SPC holds no federal lease interests and no operating interest in any crude oil producing field. SPC is a third-party purchaser of crude oil utilizing outright purchase contracts (and division orders) and buy/sell exchanges.

Production Subject to Call

An objective of the MMS is to obtain fair market value for the crude produced from federal leases. Our understanding is that the MMS is concerned that it is not obtaining fair market value for its royalty crude oil from some federal leases. This concern of the MMS apparently arose out of oil royalties paid by major oil companies which act as lease operator, but retain a "call" on, or option to purchase, some or all of the production. As outlined in the following paragraphs, SPC suggests that the proposed MMS regulations contemplate criteria that first turn on whether the crude oil involved is produced by a lease operator that is selling or otherwise transferring the federal lease oil to an affiliated refinery ("controlled crude"), as opposed to whether the operator has an affiliate which has retained a call on some or all of the production.

As to federal crude oil sold or transferred by the lease operator to an affiliate refinery, the valuation could be subject to either (1) an agreed price or price formula between the lease operator and the MMS as to controlled crude, (2) a NYMEX formula less costs including reasonable marketing, trade differentials and actual transportation, or preferably (3) MMS requests oil on a royalty-in-kind basis whereby MMS could sell its oil to a third-party purchaser such as SPC on a spot or term contract. A NYMEX formula in item (2) above should be a formula that aligns the calendar month of production with the corresponding NYMEX contract month for that production month.

Oil Sold by Producer to Non-Affiliated Refiner

As to federal royalty crude oil that is not sold or transferred to an affiliated refinery after the oil is produced by the lease operator, regardless of whether or not the crude oil is subject to a call, the royalty payments should be settled by one of the following methods: (1) the gross proceeds received by the lease operator, provided that the price per barrel paid on federal royalty is the same price received by the lease operator on its share of production (or on the share of production owned by the lessee for whom the lease operator is acting as agent), or preferably (2) the MMS's election to take its royalty share in kind, in which case the oil can be purchased by a third-party purchaser such as SPC on either a spot or term contract.

Independent Oil Purchaser and Marketer

SPC, as an active lease oil purchaser, provides a market for oil produced by independent crude oil producers. SPC also conducts a portion of its business by offering buy/sell exchange contracts to creditworthy independent producers and major oil companies. These exchange contracts provide a service and efficiency to the domestic crude oil business by repositioning oil inventories to locations where buyers and sellers need oil volumes and wish to locate inventory at lower cost than, and in lieu of, straight transportation service only.

Crude Oil Buy/Sell Exchanges

SPC provides exchanges as a service competitive with transportation and not in any way to assist any producer to avoid any royalty obligation to which the lease operator may be subject. Exchanges offered by SPC provide a valuable service to crude oil buyers and sellers. The components of this service include purchasing and receipt of crude at the lease, in-field gathering by pipelines or trucks owned by SPC (or by others in some cases), scheduling movements on other pipelines, owning, carrying and maintaining a large crude oil inventory, and arranging sales at delivery points. SPC provides this service by taking title to the crude oil and placing its assets at risk for price movements, potential loss or spill of pipeline crude oil and motor vehicle maintenance, potential breakdown, injury and spillage.

SPC employs over 600 truck drivers, gaugers and other field personnel and about 200 office personnel. As mentioned above SPC maintains a large capital investment in pipelines, trucks, equipment, tankage and real estate and, in addition, SPC must carry at considerable cost a very large investment in crude oil inventory to provide for and facilitate these exchanges. Generally these exchanges are effectuated by SPC's transferring oil in and out of its inventory at appropriate locations, saving on actual physical transportation costs which are passed on to customers in the form of lower gathering and handling rates, and avoiding transportation delays and risks attendant thereto.

The MMS should recognize the validity and economic benefit to the crude oil industry derived from crude oil exchanges provided by a third-party purchasers and marketers such as SPC. SPC is very concerned that its exchange business, which is very beneficial to the oil industry, will be inadvertently damaged or destroyed as a result of this dispute between the MMS and the owners of controlled crude or calls on production who retain crude for use in their own or affiliated refineries.

SPC is willing to provide its services (1) to majors and creditworthy independents who need exchanges on federal lease crude at fair market values on either (a) agreed-upon postings or (b) NYMEX-related prices with deduction for costs incurred and gathering and handling fees earned by SPC, (2) to the MMS as a marketing agent for MMS federal royalty oil, and/or (3) to the MMS as a purchaser of federal lease crude oil at the lease upon an agreed fair market value or reference price applicable at the lease level which is comparable to prices paid by SPC to others.

The "Alberta Model"

In addition, it is our understanding that the MMS has looked to the system for marketing the Crown's royalty oil in Alberta, Canada as a model for valuing oil at the lease and royalty-in-kind regulation. We feel there are significant differences which must be considered before applying the so-called "Alberta model" to federal royalty oil production and marketing in the United States. If marketing agents were to be appointed by the MMS to market federal royalty crude, significantly more agents would be needed to market the diverse sources and types of crudes produced domestically, and greater compensation would be required than is provided in the Alberta marketing agent's commission of five cents (Canadian) per barrel (about 3.5 cents U.S.), for the following reasons:

1) Most of the approximately two million barrels per day of crude oil production in Alberta is derived from public lands. This large volume of production is placed in the hands of only three marketers (two of which are also producers), resulting in significant economies of scale unavailable to the domestic producer or the midstream marketer such as SPC.

2) The Crown's oil is produced and marketed in a more limited environment, including a much simpler distribution network than is required domestically. There are only about ten significant feeder pipelines in Alberta, and even fewer major trunk lines; truck transport of oil is a smaller percentage. The cost of crude oil movement and storage domestically is higher, reflecting the diversity and number of sources and consumers of oil, and the complex distribution web necessary to serve them.

3) Production and marketing of the Crown's oil are handled entirely by the Alberta Department of Energy (DOE), such that industry's reporting and remittance are also much more streamlined than in the United States. The Alberta DOE is the sole payee of royalties on the Crown's oil in the province. In the United States there may be many individuals and entities who are royalty payees who must be accounted for and paid, which requires additional administrative expense.

4) Contractual arrangements for marketing of oil in Alberta are much less rigorous and commensurately simpler and less costly to administer than in the United States.

5) Valuation of the Crown's oil is determined in a simple manner based on posted prices negotiated by the producer, reflecting a market-center posting adjusted as reasonable for location and quality (e.g., tariffs, feeder pipeline equalizations and similar charges, fees and differentials). This system in the United States is now under attack for reasons which the Alberta government has already faced and apparently found unpersuasive.

Accordingly, relative to their marketing and producing counterparts in the United States, Alberta's marketers of the Crown's oil are advantaged by economies of scale, streamlined reporting and remittance requirements, and simpler delivery arrangements necessary to aggregate the production and position it at major markets. As a result the commission negotiated by the Alberta DOE with its three marketing agents may not be adequate compensation to perform the same function in the United States as legal duties, lease variables and volumes on discreet sales arrangements are not equivalent.

Thank you for your consideration.

Very truly yours,

SCURLOCK PERMIAN CORPORATION

Lawrence J Dreyfuss

Lawrence J. Dreyfuss

cc: Ben Dillion, IPAA
Eric Fox, Ashland Inc.

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