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23	MPDAV&.ORD 11/19/1997	LTR Jicarilla Apache	Same Enclosure with pg 5-c different

Project File No. 96-0480

RVD reviewed the payor responses to the 1995 Armstrong order on dual accounting to determine which payors had or had not performed dual accounting. RVD then calculated additional royalties due based on Major Portion prices for those payors who stated that they had performed major portion. RVD determined that those payors who had stated in response to the Armstrong order that they had performed dual accounting paid royalties on prices less that the major portion price for those months tested.

RVD also determined the estimated royalties due for each payor and for the major portion issues using the following calculations:

RVD calculated the royalties due for Mobil lease 609-000089-0 and determined the percentage factor for royalty underpayments (1.505%). This factor was then multiplied by the royalties paid for gas for each payor to determine an estimate of royalties due. Based on this estimate RVD calculated additional royalties due for major portion for the Jicarilla's. The estimated royalties due are $71,338,497.69.

RVD calculated the MMBtu price paid by in value payors to the Major Portion 103 price. RVD then multiplied the price difference if negative by the royalty volumes reported. Based on this estimate RVD calculated additional royalties due for major portion for the Jicarilla's of $55,289136.73..

2

Project File No. 97-0480

RVD reviewed the following settlement agreements to determine whether to bill major portion prices and dual accounting for the Jicarilla Apache Tribe:

Conoco Inc. January 14, 1993

Conoco Inc. February 1, 1994

Conoco Inc. July 1, 1995

Jerome P. McHugh & Associates, Nassau Resources Inc. December 1, 1994

Columbus Energy Corp. December 15, 1995

The agreements cover all royalty payments and time periods for the above payors, except for leases 609-000042-0, 609-00077-0, 609-000078-0, 609-000161-0, for Conoco which are not included in the agreement.

RVD has also requested a settlement agreement for Mobil Inc. from the Dallas Compliance Division but we have not received the copy for review.

Project File No. 97-0480

RVD reviewed the Jicarillla Severance and Priveledge Tax Manual to determine the appropriate amounts to include for Tax Reimbursements on ajor Portion Prices. RVD also reviewed the El Paso and Northwest RIK contracts and determined that the contracts called for maximum lawful prices plus reimbursements for taxes. RVD confirmed the tax rates and times periods for each rate with the Jicarilla Apache Tribe.

Project File No. 97-0480

RVD performed several types of verifications to determine that the RIK sales represented a major portion of production when compared to the total sales volumes for the reservation.

Data Retrieval

During September 1996, AFS data as reported on the Report of Sales and Royalty Remittance (Form MMS-2014), was extracted from the AFS database, processed and downloaded to a Microsoft Access table on the RVD Local Area Network. The criteria for extracting this data were: (1) all AFS data reported under Fund Code 550 (the fund code for the Reservation); (2) the product codes 03 (residue gas) and 04 (unprocessed gas); and (3) the transaction codes 01 (royalty) and 11 (transportation allowance).

Data Processing

Once extracted from the AFS database, the information was processed by a program that removed adjustments to previously submitted information. This program first sorted the database by lease, product code, revenue source, selling arrangement, sales year, sales month, royalty quantity, and royalty value. The program then identified all negative (adjusted) royalty quantities and values and searched for a matching positive line. If a match was found, both the positive and negative lines were removed. Next, those negative lines without a matching positive (indicative of misreporting) were written to an error file and removed from further processing.

The next operation performed on the data was to determine major portion prices. We calculated $/MMBtu prices by adjusting for the quality of the gas.

A problem encountered in the data was that some records did not have a reported gas quality or an incorrect Btu content that was not within a reasonable range. Options included removing those records, using the quality last reported for the lease, or assuming a quality. After analyzing this problem, we decided that given our limited resources, the best option was to calculate a gas quality from the data available. We determined the 1996 average quality reported on the Monthly Report of Operations (Form MMS 3160) for all Jicarilla leases and calculated the range reported on all Jicarilla leases. We used the average Btu reported on the Form MMS 3160 for each lease for all 04 lines submitted that did not report a quality or reported a quality outside of the average range. We used the average Btu reported on the Form MMS-2014 for all 03 lines submitted that did not report a quality or reported a quality outside of the average range.

AFS Analysis of Major Portion

Upon completion of processing, the database for the Reservation contained 47,463 records. In addition, MMS did not require the purchaser's of RIK production to report those sales on the Form MMS-2014. In an effort to verify that the RIK data is the major portion price RVD created an off-line MMS-2014 and manually added the RIK sales data to the price array for February 1988. MMS extracted AFS database lines February 1988 and arrayed lines by $/Mcf from the highest price to lowest price. RVD then determined the amount of RIK production sold from the Jicarilla purchase statements by month and determined an average $/Mcf price. RVD calculated that price at which 50 percent (by volume) plus 1 Mcf of the gas (starting from the bottom) is sold (Attachment 6).

RVD downloaded all royalty payments for Fund Code 550 (Jicarilla Tribe). We then summarized the payments for February 1988 by payor. Using data from settlement statements, we added the total RIK volumes purchased by El Paso and Northwest for February 1988 and determined the total sales for the Reservation. RVD then divided total RIK sales by the total sales for the reservation to determine the percentage of Reservation gas which was sold as RIK. Our review indicated that for February 1988 sales month, 66 percent of the royalty production on the Reservation was sold as RIK, therefore, RVD concluded that the major portion price based on RIK data represents approximately 66 percent of the sales volume for February 1988 sales month, when compared to the sales volume reported by in-value payors on Form MMS 2014. (Attachment 5).

The attachments in this file show the data used and the schedules created in performing this analysis.

MMS-RVD-OG
Mail Stop 3152

CERTIFIED MAIL--
RETURN RECEIPT REQUESTED

Name
Company
Address
City, State, Zip

Dear Name

In carrying out the trust responsibility of the United States in the administration of Indian oil and gas leases, the Minerals Management Service (MMS) has long recognized the primacy of the lease terms. As a royalty payor on Jicarilla Apache Indian Tribe (Jicarilla Apache) leases, you are obligated to comply with Section (c) **Rental and royalty**, of the Indian lease terms, which states, in part:

> During the period of supervision, "value" for the purposes hereof may, in the discretion of the Secretary, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the oil and gas supervisor.

This requirement, commonly called major portion analyses, is also embodied in the oil and gas valuation regulations found at 30 CFR 206 (1987) and in the amended valuation regulations at 30 CFR §§ 206.152 and 206.153 (1995). Title 25 CFR 211 (Indian tribal) and 212 (Indian allotted) (1987) also recognize this requirement.

MMS has performed major portion analyses for natural gas production from Jicarilla Apache leases for the period **January 1984 through (June?)December 1995**. We have used gas sales data reported by the Jicarilla Apache Tribe under their Royalty-in-Kind program to determine major portion prices for the Jicarilla Apache Indian Reservation (Reservation) by production month. We have determined that the Jicarilla Apache sold the majority of their RIK production based on the Maximum Lawful Price (MLP) as set by the Natural Gas Policy Act (NGPA). Enclosure _ provides a list of NGPA prices by NGPA category. Enclosure __ provides a list of your accounting identification (AID) numbers for the Reservation. If you are not currently responsible for payment of royalties for the lease numbers in Enclosure __, please identify the responsible party and the date the lease(s) were assigned to the other company.

Please compare these values to the values you reported to MMS on Form MMS-2014. Please identify and document with copies of contracts or lease settlement statements, any differences you feel are not valid. You must pay additional royalties for those gas sales that are less than the MLP value. Please be aware of the following when paying the additional royalties:

- Follow the procedures outlined in 30 CFR § 218.51 (1996).
- If you are not currently a royalty payor to MMS or if you have questions on the completion of the Form MMS-2014, please contact your Reports Branch representative at (303) 231-3287.
- **You must use adjustment reason code 49 when you report your additional royalties on Form MMS-2014.** This adjustment reason code must be used for both the reversal line and the re-entry line.
- Late payment charges under 30 CFR § 218.102 (1996) will be computed and billed to you upon receipt of payment of the additional royalties due.

MMS will compare these major portion values to your Form MMS-2014 information approximately 60 days from the date of this letter. We will send you an official order to pay additional royalties for those instances where your royalty value is still less than these major portion values.

MMS is also conducting a review of dual accounting on Indian leases. MMS (has previously?) issued an order to company (Comp) to provide a declaration of policy on dual accounting. On your ____, 19__ response, you stated that the company (did or?) did not perform dual accounting on the Indian leases for which Comp is a royalty payor. Based on the review of a sample lease under section 3(c) entitled "Rental and Royalty", we determined that the lease terms require dual accounting. Our review shows that, Comp did not perform dual accounting calculations in determining royalties due on the lease and, as a result, additional royalties may be due.

Dual accounting requirements are specified by Indian lease terms, Federal regulations, and MMS' instructions. Federal regulations at 25 CFR §§ 211.13 (1996) and 212.16 (1996) state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that <u>royalty will be computed on</u>

the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.152 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.153 (1996). Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency. Royalty on gas produced from an Indian lease and ultimately processed (either by the lessee or any purchaser) must be computed by applying the dual accounting requirements specified by the lease. Indian royalty is to be calculated and paid based on the method yielding the higher value. However, royalty is never to be based on a value which is less than the gross proceeds received by the lessee. (After March 31, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.156 through 206.159 (1996))).

By "Dear Payor" letter dated September 30, 1988 (Enclosure __), MMS emphasized the requirement with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1996).

Therefore, in order to comply with regulations and lease terms, within __ days of receipt of this letter, Comp is ordered to perform the following:

1. For each Indian lease for which the dual accounting requirement is specified in the lease terms, Comp is hereby directed to recalculate royalties following the dual accounting requirements from January 1984 through December (June?) 1995. For those months listed on Enclosure __, MMS has calculated majority prices for leases within the Reservation Comp must use the higher of the MMBtu prices listed on Enclosure __ or the gross proceeds MMBtu price received for wellhead and the residue gas values in the dual accounting calculations.

   If Comp is unable to obtain the necessary information to perform dual accounting as required by the lease terms, Comp is directed to apply the theoretical dual accounting as explained in the MMS' "Dear Payor" letter dated July 27, 1992 (Enclosure __). MMS has provided a worksheet for theoretical dual accounting calculations and a diskette with the Excel worksheet on it in order to assist Comp in completing dual accounting calculations (Enclosure __). If needed, MMS can provide assistance in completing these calculations.

2. Compare royalties due as calculated in step (1) to royalties previously paid for each month and pay any additional royalties due. All such redeterminations are to be documented in the format shown in Enclosure __.

Your payments should be made in accordance with the regulations at 30 CFR § 218.51 (1996), and accompanied by an appropriately completed green Form MMS-2014 (Enclosure __). A copy of your payment and the green Form MMS-2014 should be sent to the address shown below.

Appropriate late payment charges pursuant to 30 CFR § 218.102 (1996) will be computed and billed to Comp upon receipt of payment of any additional royalties due.

All documentation supporting your compliance with this order should be retained until MMS completes its follow-up compliance testing. After the period covered by this order, Comp should continue to value production for royalty purposes in accordance with regulations and guidelines discussed in this order. If MMS determines that the required accounting has not been performed, or the future royalty payments do not comply with this order, the violation may be considered willful.

Section 109 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), promulgated in 30 CFR § 241.51 (1996), authorizes MMS to assess civil penalties for failure or refusal to comply with the requirements of FOGRMA or any statute, regulation, rule, order, lease, or permit. Consequently, your failure to comply with the terms of this order may be considered a violation pursuant to 30 CFR § 241.51 (1996) and could subject you to appropriate penalties as provided therein.

You have the right to appeal in accordance with the provisions of 30 CFR 290 (1996). Any appeal taken will be to the Deputy Commissioner of Indian Affairs and must be filed within 30 days from the receipt of this order at the following address:

Ms. Deborah Gibbs Tschudy
Chief, Royalty Valuation Division
Minerals Management Service
P.O. Box 25165, Mail Stop 3152
Denver, Colorado 80225-0165

Any notice of appeal must be accompanied by written statement of reasons, as you deem adequate to justify reversal or modification of this directive. Within 90 days from receipt of this order, the appellant will be permitted to file additional statement of reasons or written briefs.

With the exception of the time fixed for filing a notice of appeal, the time for filing any document in connection with an appeal may be extended. Extensions for filing the statement of reasons will not be permitted unless requested in writing by the appellant (within the 30-day period allowed for filing the appeal) with justification showing good cause for the time extension and delivered to Deborah Gibbs Tschudy at the above address.

In accordance with the provisions of 30 CFR § 243.2 (1996), compliance with this order will be suspended by reason of an appeal having been taken.

If you have any comments or questions concerning this request, contact Joseph Cornellisson at (303) 275-7239.

Sincerely,

Deborah Gibbs Tschudy
Chief, Royalty Valuation Division

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MMS-RVD-OG
Mail Stop 3152

CERTIFIED MAIL--
RETURN RECEIPT REQUESTED

Name
Company
Address
City, State, Zip

Dear Name

In carrying out the trust responsibility of the United States in the administration of Indian oil and gas leases, the Minerals Management Service (MMS) has long recognized the primacy of the lease terms. As a royalty payor on Jicarilla Apache Indian Tribe (Jicarilla Apache) leases, you are obligated to comply with Section 3(c) **Rental and royalty**, of the Indian lease terms. More specifically, the regulations state that major portion analysis for oil and gas and dual accounting for gas (accounting for comparison) must be performed in determine the value of production for royalty purposes. (Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.)

For major portion, Federal Regulations (25 CFR §§ 211.13 (1996)) state:

> During the period of supervision, "value" for the purposes hereof may, in the discretion of the Secretary, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the supervisor.

This requirement is also embodied in the gas valuation regulations found at 30 CFR §§ 206.172 and 206.173 (1996).

Dual accounting requirements are specified Federal regulations found at 25 CFR §§ 211.13

(1996) and 212.16 (1996) state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.172 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.173 (1996). Royalty on gas produced from an Indian lease and ultimately processed (either by the lessee or any purchaser) must be computed by applying the dual accounting requirements specified by the lease and paid based on the method yielding the higher value. However, royalty is never to be based on a value which is less than the gross proceeds received by the lessee. (After March 31, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.156 through 206.159 (1996))).

Major Portion

MMS has performed major portion analyses for natural gas production from Jicarilla Apache leases for the period **January 1984 through June 1995**. We have used gas sales data reported by the Jicarilla Apache Tribe under their Royalty-in-Kind (RIK) program to determine major portion prices for the Jicarilla Apache Indian Reservation (Reservation) by production month. We have determined that the Jicarilla Apache sold the majority of their RIK production based on the Maximum Lawful Price (MLP) as set by the Natural Gas Policy Act (NGPA) in the following categories:

102 new natural gas	104 old flowing gas
103 new onshore production.	108 stripper gas
104 old gas	109 other gas

Enclosure MP provides a list of NGPA prices by NGPA category. Enclosure AID provides a list of your accounting identification (AID) numbers for the Reservation. If you are not currently responsible for payment of royalties for the lease numbers in Enclosure LN, please identify the responsible party and the date the lease(s) were assigned to the other company.

Dual Accounting

MMS is also conducting a review of dual accounting on Indian leases. MMS (has previously?) issued an order to company (*Short company name*) to provide a declaration of policy on dual accounting. On your ____, 19__ response, you stated that the company (did or?) did not perform dual accounting on the Indian leases for which *Short company name* is a royalty payor. Based on the review of a sample lease under section 3(c) entitled "Rental and Royalty", we determined that the lease terms require dual accounting. Our review shows that, *Short company name* did not perform dual accounting calculations in determining royalties due on the lease and, as a result, additional royalties may be due.

By "Dear Payor" letter dated September 30, 1988 (Enclosure __), MMS emphasized the requirement with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1996).

<u>Order to Perform</u>

Therefore, in order to comply with regulations and lease terms, **within __ days of receipt** of this letter, *Short company name* is ordered to perform the following:

1. Please compare the values shown on Enclosure MP to the values *Short company name* reported to MMS on Form MMS-2014 and recalculate any royalties due from **January 1984 through June 1995**. Please identify and document with copies of contracts or lease settlement statements, any differences you feel are not valid. *Short company name* must pay additional royalties for those gas sales that are less than the prices shown on Enclosure MP. MMS will compare these major portion values to your Form MMS-2014 information approximately 60 days from the date of this letter.

2. For each Indian lease for which the dual accounting requirement is specified in the lease terms, *Short company name* is hereby directed to recalculate royalties following the dual accounting requirements from **January 1984 through June 1995**. For those months listed on Enclosure __, MMS has compiled majority prices for leases within the Reservation, *Short company name* must use the higher of the MMBtu prices listed on Enclosure MP or the gross proceeds MMBtu price received for wellhead and the residue gas values in the dual accounting calculations.

   If *Short company name* is unable to obtain the necessary information to perform dual accounting as required by the lease terms, *Short company name* is directed to apply the theoretical dual accounting as explained in the MMS' "Dear Payor" letter dated July 27, 1992 (Enclosure __). MMS has provided a worksheet for theoretical dual accounting calculations and a diskette with the Excel worksheet on it in order to assist *Short company name* in completing dual accounting calculations (Enclosure __). If needed, MMS can provide assistance in completing these calculations.

3. Compare royalties due as calculated in step (2) to royalties previously paid for each month and pay any additional royalties due. All such redeterminations are to be

documented in the format shown in Enclosure __.

Payment Instructions

Please be aware of the following when paying the additional royalties pertaining to major portion:

- Your payments should be made in accordance with the regulations at 30 CFR § 218.51 (1996), and accompanied by an appropriately completed green Form MMS-2014 (Enclosure __). You will be in compliance with the order only if your payment is enclosed with a properly completed green Form MMS-2014 and mailed to:

Minerals Management Service
Royalty Valuation Division
P.O. Box 5810 T.A.
Denver, Colorado 80127-5810

- If you are not currently a royalty payor to MMS or if you have questions on the completion of the Form MMS-2014, please contact your Reports Branch representative at (303) 231-3287.

- For additional major portion royalties, you must use adjustment reason code 49 when you report your additional royalties on Form MMS-2014. This adjustment reason code must be used for both the reversal line and the re-entry line.

- For additional dual accounting royalties, you must use adjustment code 41 when you report your additional royalties on Form MMS-2014. This adjustment reason code must be used for both the reversal line and the re-entry line.

- Appropriate late payment charges pursuant to 30 CFR § 218.102 (1996) will be computed and billed to *Short company name* upon receipt of payment of any additional royalties due.

All documentation supporting your compliance with this order should be retained until MMS completes its follow-up compliance testing. After the period covered by this order, *Short company name* should continue to value production for royalty purposes in accordance with regulations and guidelines discussed in this order. If MMS determines that the required accounting has not been performed, or the future royalty payments do not comply with this order, the violation may be considered willful.

Section 109 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), promulgated in 30 CFR § 241.51 (1996), authorizes MMS to assess civil penalties for failure or refusal to comply with the requirements of FOGRMA or any statute, regulation, rule, order, lease, or permit. Consequently, your failure to comply with the terms of this order may be considered a violation pursuant to 30 CFR § 241.51 (1996) and could subject you to appropriate penalties as provided therein.

Appeal Rights

You have the right to appeal in accordance with the provisions of 30 CFR 290 (1996). Any appeal taken will be to the Deputy Commissioner of Indian Affairs and must be filed within 30 days from the receipt of this order at the following address:

Ms. Deborah Gibbs Tschudy
Chief, Royalty Valuation Division
Minerals Management Service
P.O. Box 25165, Mail Stop 3152
Denver, Colorado 80225-0165

Any notice of appeal must be accompanied by written statement of reasons, as you deem adequate to justify reversal or modification of this directive. Within 90 days from receipt of this order, the appellant will be permitted to file additional statement of reasons or written briefs.

With the exception of the time fixed for filing a notice of appeal, the time for filing any document in connection with an appeal may be extended. Extensions for filing the statement of reasons will not be permitted unless requested in writing by the appellant (within the 30-day period allowed for filing the appeal) with justification showing good cause for the time extension and delivered to Deborah Gibbs Tschudy at the above address.

In accordance with the provisions of 30 CFR § 243.2 (1996), compliance with this order will be suspended by reason of an appeal having been taken.

If you have any comments or questions concerning this request, contact Joseph Cornellisson at (303) 275-7239.

Sincerely,

Deborah Gibbs Tschudy
Chief, Royalty Valuation Division

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August 15, 1997

DRAFT - FOR REVIEW ONLY - NOT TO BE RELEASED

September 8, 1997

MMS-RVD-OG
Mail Stop 3152

CERTIFIED MAIL--
RETURN RECEIPT REQUESTED

Name
Company
Address
City, State, Zip

Dear Name

In carrying out the trust responsibility of the United States in the administration of Indian oil and gas leases, the Minerals Management Service (MMS) has long recognized the primacy of the lease terms. As a royalty payor on Jicarilla Apache Indian Tribe (Jicarilla Apache) leases, you are obligated to comply with Section 3(c) **Rental and royalty**, of the Indian lease terms. More specifically, the regulations state that major portion analysis for oil and gas and dual accounting for gas (accounting for comparison) must be performed in determine the value of production for royalty purposes. (Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.)

For major portion, Federal Regulations (25 CFR §§ 211.13 (1996)) state:

> During the period of supervision, "value" for the purposes of the lease may, in the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the supervisor.

This requirement is also embodied in the gas valuation regulations found at 30 CFR §§ 206.172 and 206.173 (1996).

Dual accounting requirements are specified Federal regulations found at 25 CFR §§ 211.13 (1996) state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that <u>royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater</u> [Emphasis added.]

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.172 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.173 (1996). Royalty on gas produced from an Indian lease and ultimately processed (either by the lessee or any purchaser) must be computed by applying the dual accounting requirements specified by the lease and paid based on the method yielding the higher value. However, royalty is never to be based on a value which is less than the gross proceeds received by the lessee. (After March 31, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.176 through 206.179 (1996))).

<u>Major Portion</u>

MMS has performed major portion analyses for natural gas production from Jicarilla Apache leases for the period **January 1984 through June 1995**. We have used gas sales data reported by the Jicarilla Apache Tribe under their Royalty-in-Kind (RIK) program to determine major portion prices for the Jicarilla Apache Indian Reservation (Reservation) by production month. We have determined that the Jicarilla Apache sold the majority of their RIK production based on the Maximum Lawful Price (MLP) as set by the Natural Gas Policy Act (NGPA) in the following categories:

102 new natural gas	103 new onshore production
104 flowing gas	104 replacement gas
105 Existing intrastate	106 Alternate MLP
107 tight gas	108 stripper gas
109 other gas	

Enclosure <u>MP</u> provides a list of NGPA prices by NGPA category through 1989. After 1989, the major portion price is shown. Enclosure <u>AID</u> provides a list of your accounting identification

(AID) numbers for the Reservation. If you are not responsible for payment of royalties for the lease numbers in Enclosure LN between January 1984 and June 1995, please identify the responsible party and the date your responsibility ended.

Dual Accounting

MMS is also conducting a review of dual accounting on Indian leases. MMS (has previously?) issued an order to (*Short company name*) to provide a declaration of policy on dual accounting. On your______19__ response, you stated that the company (did or?) did not perform dual accounting on the Indian leases for which *Short company name* is a royalty payor. Based on the review of a sample lease under section 3(c) entitled "Rental and Royalty", we determined that the lease terms require dual accounting. Our review shows that, *Short company name* did not perform dual accounting calculations in determining royalties due on the lease and, as a result, additional royalties may be due.

By "Dear Payor" letter dated September 30, 1988 (Enclosure __), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1996).

Order to Perform (Need example enclosure)

Therefore, in order to comply with regulations and lease terms, **within 90 days of receipt** of this letter, *Short company name* is ordered to perform the following:

1. Please compare the values shown on Enclosure MP to the values *Short company name* reported to MMS on Form MMS-2014 from **January 1984 through June 1995**. From January 1984 through December 1988, ~~please recalculate royalties due on~~ use the higher of your gross proceeds or the NGPA price plus tax reimbursements in the following calculation. After January 1, 1989 please compare your gas sales price with the major portion price shown on Enclosure MP and ~~recalculate any royalties due on~~ use the higher of your gross proceeds price or the major portion price shown in the following calculations. Please identify and document with copies of contracts or lease settlement statements, any differences you feel are not valid.

2. Using the higher of the gross proceeds or major portion price please calculate a dual accounting value (processed gas plus liquids value) and an unprocessed (well head) value.

   In the dual accounting calculation, the processed gas value includes residue gas values and natural gas liquids less a processing allowance. (A processing allowance can only be claimed if a processing allowance form has been previously filed with MMS.) Liquids values used in the calculation must be the higher of actual gross proceeds price or the Mt. Belvieu, Texas average spot price as shown in Enclosure NGL

If *Short company name* is unable to obtain the necessary information to perform dual accounting as required by the lease terms, *Short company name* is directed to apply the theoretical dual accounting as explained in the MMS' "Dear Payor" letter dated July 27, 1992 (Enclosure __). MMS has provided a worksheet for theoretical dual accounting calculations and a diskette with the Excel worksheet on it in order to assist *Short company name* in completing dual accounting calculations (Enclosure __). If needed, MMS can provide assistance in completing these calculations.

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Please be aware of the following when paying the additional royalties pertaining to major portion and dual accounting:

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  Albuquerque, NM 87103

- A copy of your payment and the green Form MMS-2014 should be mailed to:

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  P.O. Box 5810
  Denver, Colorado 80127-5810

- If you have questions on the completion of the Form MMS-2014, please contact your Reports Branch representative at (800) 525-0309 or (303) 231-3288. If you are not currently a royalty payor to MMS please contact Joseph Cornellisson at (303) 275-7239 for further instructions.

- For additional royalties, you must use adjustment reason code 49 when you report your additional royalties on Form MMS-2014. This adjustment reason code must be used for both the reversal line and the re-entry line.

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All documentation supporting your compliance with this order should be retained until MMS completes its follow-up compliance testing. After the period covered by this order, *Short company name* should continue to value production for royalty purposes in accordance with regulations and guidelines discussed in this order. ~~If MMS determines that the required accounting has not been performed, or the future royalty payments do not comply with this order, the violation may be considered willful.~~

Section 109 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), promulgated in 30 CFR § 241.51 (1996), authorizes MMS to assess civil penalties for failure or refusal to comply with the requirements of FOGRMA or any statute, regulation, rule, order, lease, or permit. Consequently, your failure to comply with the terms of this order may be considered a violation pursuant to 30 CFR § 241.51 (1996) and could subject you to appropriate penalties as provided therein.

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You have the right to appeal in accordance with the provisions of 30 CFR 290 (1996). Any appeal taken will be to the Deputy Commissioner of Indian Affairs and must be filed within 30 days from the receipt of this order at the following address:

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Minerals Management Service
P.O. Box 25165, Mail Stop 3152
Denver, Colorado 80225-0165

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With the exception of the time fixed for filing a notice of appeal, the time for filing any document in connection with an appeal may be extended. Extensions for filing the statement of reasons will not be permitted unless requested in writing by the appellant (within the 30-day period allowed for filing the appeal) with justification showing good cause for the time extension and delivered to Deborah Gibbs Tschudy at the above address.

In accordance with the provisions of 30 CFR § 243.2 (1996), compliance with this order will be suspended by reason of an appeal having been taken.

If you have any comments or questions concerning this request, contact Joseph Cornellisson at (303) 275-7239.

Sincerely,

Deborah Gibbs Tschudy
Chief, Royalty Valuation Division

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August 28, 1997

(6)

DRAFT (DID NOT PERFORM) - FOR REVIEW ONLY - NOT TO BE RELEASED

September 11, 1997

MMS-RVD-OG
Mail Stop 3152

CERTIFIED MAIL--
RETURN RECEIPT REQUESTED

Name
Company
Address
City, State, Zip

Dear Name

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For major portion, Federal Regulations (25 CFR § 211.13 (1996)) state:

> During the period of supervision, "value" for the purposes of the lease may, in the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the supervisor.

This requirement is also embodied in the gas valuation regulations found at 30 CFR §§ 206.172 and 206.173 (1996).

Dual accounting requirements are specified by Indian lease terms and Federal regulations found at 25 CFR § 211.13 (1996) which state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.172 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.173 (1996). Royalty on gas produced from an Indian lease and ultimately processed (either by the lessee or any purchaser) must be computed by applying the dual accounting requirements specified by the lease and paid based on the method yielding the higher value. However, royalty is never to be based on a value which is less than the gross proceeds received by the lessee. (After March 31, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.176 through 206.179 (1996))).

Major Portion

MMS has performed major portion analyses for natural gas production from Jicarilla Apache leases for the period **January 1984 through June 1995**. We have used gas sales data reported by the Jicarilla Apache Tribe under their Royalty-in-Kind (RIK) program to determine major portion prices for the Jicarilla Apache Indian Reservation (Reservation) by production month. We have determined that the Jicarilla Apache sold the majority of their RIK production based on the Maximum Lawful Price (MLP) as set by the Natural Gas Policy Act (NGPA) in the following categories:

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Enclosure MP provides a list of NGPA prices plus tax reimbursements by NGPA category through 1989. After 1989, the major portion price is shown by NGPA category. Enclosure AID

provides a list of your accounting identification (AID) numbers for the Reservation, the wells pertaining to each lease, and the NGPA category for the wells. If you are not responsible for payment of royalties for the lease numbers in Enclosure AID between January 1984 and June 1995, please identify the responsible party and the date your responsibility ended.

Dual Accounting

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Order to Perform

Therefore, in order to comply with regulations and lease terms, **within 90 days of receipt** of this letter, *Short company name* is ordered to perform the following:

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August 28, 1997

DRAFT (DID NOT PERFORM) - FOR REVIEW ONLY - NOT TO BE RELEASED

September 11, 1997

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August 28, 1997

DRAFT (DID PERFORM) - FOR REVIEW ONLY - NOT TO BE RELEASED

September 11, 1997

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   In the dual accounting calculation, the processed gas value includes residue gas values and natural gas liquids less a processing allowance. (A processing allowance can only be claimed if a processing allowance form has been previously filed with MMS.) We have reviewed comparable contract prices and found that Mt. Belvieu, Texas average spot prices provide a reasonable comparable value. Therefore, liquids values used in the calculation must be the higher of actual gross proceeds price or the Mt. Belvieu, Texas average spot price as shown in Enclosure NGL.

If *Short company name* is unable to obtain the necessary information to perform dual accounting as required by the lease terms, *Short company name* is directed to apply the theoretical dual accounting as explained in the MMS' "Dear Payor" letter dated July 27, 1992 (Enclosure __). MMS has provided a worksheet for theoretical dual accounting calculations and a diskette with the Excel worksheet on it in order to assist *Short company name* in completing dual accounting calculations (Enclosure __). If needed, MMS can provide assistance in completing these calculations.

3. Compare royalties due as calculated in step (2) to royalties previously paid for each month and pay any additional royalties due. All such redeterminations are to be documented in the format shown in Enclosure __.

Payment Instructions

Please be aware of the following when paying the additional royalties pertaining to major portion and dual accounting:

- Your payments should be made in accordance with the regulations at 30 CFR § 218.51 (1996), and accompanied by an appropriately completed green Form MMS-2014 (Enclosure __). You will be in compliance with the order only if your payment and a copy of a properly completed green Form MMS-2014 is mailed to:

Jicarilla Apache Tribe
P.O. Box 2053
Albuquerque, NM 87103

- The completed original green Form MMS-2014 and a copy of your payment should be mailed to:

Minerals Management Service
Royalty Valuation Division
P.O. Box 5810
Denver, Colorado 80127-5810

- If you have questions on the completion of the Form MMS-2014, please contact your Reports

Branch representative at (800) 525-0309 or (303) 231-3288. If you are not currently a royalty payor to MMS please contact Joseph Cornellisson at (303) 275-7239 for further instructions.

- For additional royalties, you must use adjustment reason code 49 when you report your additional royalties on Form MMS-2014. This adjustment reason code must be used for both the reversal line and the re-entry line.
- Appropriate late payment charges pursuant to 30 CFR § 218.102 (1996) will be computed and billed to *Short company name* upon receipt of payment of any additional royalties due.

All documentation supporting your compliance with this order should be retained until MMS completes its follow-up compliance testing. After the period covered by this order, *Short company name* should continue to value production for royalty purposes in accordance with regulations and guidelines discussed in this order. If MMS determines that the required accounting does not comply with this order, the violation may be considered willful.

Section 109 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), promulgated in 30 CFR § 241.51 (1996), authorizes MMS to assess civil penalties for failure or refusal to comply with the requirements of FOGRMA or any statute, regulation, rule, order, lease, or permit. Consequently, your failure to comply with the terms of this order may be considered a violation pursuant to 30 CFR § 241.51 (1996) and could subject you to appropriate penalties as provided therein.

Appeal Rights

You have the right to appeal in accordance with the provisions of 30 CFR 290 (1996). Any appeal taken will be to the Deputy Commissioner of Indian Affairs and must be filed within 30 days from the receipt of this order at the following address:

Ms. Deborah Gibbs Tschudy
Chief, Royalty Valuation Division
Minerals Management Service
P.O. Box 25165, Mail Stop 3152
Denver, Colorado 80225-0165

Any notice of appeal must be accompanied by written statement of reasons, as you deem adequate to justify reversal or modification of this directive. Within 90 days from receipt of this order, the appellant will be permitted to file additional statement of reasons or written briefs.

With the exception of the time fixed for filing a notice of appeal, the time for filing any document in connection with an appeal may be extended. Extensions for filing the statement of reasons will not be permitted unless requested in writing by the appellant (within the 30-day period allowed for filing the appeal) with justification showing good cause for the time extension and delivered to Deborah Gibbs Tschudy at the above address.

In accordance with the provisions of 30 CFR § 243.2 (1996), compliance with this order will be suspended by reason of an appeal having been taken.

If you have any comments or questions concerning this request, contact Joseph Cornellisson at (303) 275-7239.

Sincerely,

Deborah Gibbs Tschudy
Chief, Royalty Valuation Division

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August 28, 1997

October 3, 1997

MMS-RVD-OG
Mail Stop 3152

CERTIFIED MAIL--
RETURN RECEIPT REQUESTED

Name
Company
Address
City, State, Zip

Dear Name

To comply with MMS regulations and lease terms of the Jicarilla Apache Indian Tribe, you (company) must perform major portion calculations and dual accounting (accounting for comparison) analysis as described below. These requirements are identified in Section 3(c) **Rental and royalty**, of the Tribal leases. (If your lease terms disagree with the regulations, follow the terms of your lease.)

Order to Perform

To comply with the regulations and lease terms, **within 90 days of receipt** of this letter, your you (company) are ordered to perform the following dual accounting and major portion calculations. Please follow the steps below to determine the value of the production for royalty purposes:

1. Calculate the **unprocessed gas value** for the period January 1984 through June 1995.

   a) The value of our gross proceeds if your gas is sold at the wellhead under an arm's-length contract (30 CFR 206.172 (1996)).

   b) The value determined under the the gas valuation benchmarks if your gas is sold at the wellhead under a non-arm's-length contract or a no sale situation (30 CFR 206.172 (1996)).

   c) The value based on the major portion price shown on Enclosure 1.

2. Calculate the **processed gas value** for the period January 1984 through June 1995:

a) If your gas is processed under an <u>arm's-length contract</u>, the processed value is your gross proceeds for the combined value of

- the residue gas,
- the gas plant products, and
- the condensate recovered downstream of the point of royalty settlement without resorting to processing,
- less a transportation and processing allowance. (A processing allowance can only be claimed if a processing allowance form has been previously filed with MMS.)

b) If your gs is processed under a <u>non-arm's-length contract</u>, the processed value is the combined value determined by the gas valuation benchmarks under 30 CFR 206.173 (1996) for

- the residue gas,
- the gas plant products, and
- the condensate recovered downstream of the point of royalty settlement without resorting to processing,
- less a transportation and processing allowance. (A processing allowance can only be claimed if a processing allowance form has been previously filed with MMS.)

If *Short company name* is unable to obtain the necessary information to perform dual accounting as required by the lease terms, *Short company name* is directed to apply the theoretical dual accounting as explained in the MMS' "Dear Payor" letter dated July 27, 1992 (Enclosure 4). MMS has provided a worksheet for both actual and theoretical dual accounting calculations and a diskette with a Microsoft Excel worksheet in order to assist *Short company name* in completing dual accounting calculations (Enclosure 8). An example of the dual accounting calculations is shown in Enclosure 9. If needed, MMS can provide assistance in completing these calculations.

c) The <u>value of the processed gas</u> is the greater of: the combined value of the processed gas calculated in a or b above, as applicable, or the combined value of:

- the residue gas using the major portion price in Enclosure 1,

- the gas plant products using the Mt. Belvieu, Texas average spot price as shown in Enclosure 7 as the comparable contract price,

- the condensate based on the gross proceeds under the arm's-length contracts,

- less any transportation or processing allowances.

3. To comply with the dual accounting requirement, the value for royalty purposes is the greater of:

    - the unprocessed gas value (determined in Step No. 1),
    - the processed gas value (determined in Step No. 2), or
    - your gross proceeds.

4. To determine the royalty due compare the greater value in Step No. 3 above to the values *Short company name* reported to MMS on Form MMS-2014 from **January 1984 through June 1995** and pay any additional royalty amount due. All such redeterminations are to be documented in the format shown in Enclosure 10. Please identify and document with copies of contracts or lease settlement statements, any differences you feel are not valid.

Payment Instructions

When paying the additional royalties pertaining to major portion and dual accounting:

- You must pay under 30 CFR § 218.51 (1996). You payment must include properly completed green Form MMS-2014 (Enclosure 11). To comply with the order you must mail your payment and a copy of Form MMS-2014 to:

Jicarilla Apache Tribe
P.O. Box 2053
Albuquerque, NM 87103

- Mail the completed original green Form MMS-2014 and a copy of your payment to:

Minerals Management Service
Royalty Valuation Division
P.O. Box 5810
Denver, Colorado 80127-5810

- Please use adjustment reason code 49 when you report your additional royalties on Form MMS-2014. This adjustment reason code must be used for both the reversal line and the re-entry line.

We will compute and bill late payment charges as authorized under 30 CFR § 218.102 (1996) when we receive your additional royalties. If you have questions on the completion of the Form MMS-2014, please contact your Reports Branch representative at (800) 525-0309 or (303) 231-3288. If you are not currently a royalty payor to MMS please contact Joseph Cornellisson at (303) 275-7239 for further instructions.

Retain all documentation supporting your compliance with this order until MMS completes its follow-up compliance testing. Section 109 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), issued under 30 CFR § 241.51 (1996), authorizes MMS to assess civil penalties for failure or refusal to comply with the requirements of FOGRMA or any statute, regulation, rule, order, lease, or permit. If you don't comply with this order you will violate 30 CFR § 241.51 (1996) which could subject you to appropriate penalties.

Appeal Rights

You have the right to appeal in accordance with the provisions of 30 CFR 290 (1996). A copy of the Appeals Procedures and Bonding Requirements is attached (Enclosure 12).

In accordance with the provisions of 30 CFR § 243.2 (1996), compliance with this order will be suspended by reason of an appeal having been taken.

What is Major Portion

For major portion, Federal Regulations (25 CFR § 211.13 (1996)) state:

> During the period of supervision, "value" for the purposes of the lease may, in the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the supervisor.

This requirement is also embodied in the gas valuation regulations found at 30 CFR §§ 206.172 and 206.173 (1996).

Dual accounting requirements are specified by Indian lease terms and Federal regulations found at 25 CFR § 211.13 (1996) which state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product

unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that requires the lessee to compute royalties based on the greater of : (1) the value of the gas prior to processing (as determined under 30 CFR § 206.172 (1996)), or (2) the combined value of the residue gas and gas plant products resulting from processing the gas (as determined under 30 CFR § 206.173 (1996)), plus the value of any condensate recovered downstream of the point of royalty settlement without resorting to processing (30 CFR § 206.52). However, the value of production can never be less than the gross proceeds accruing to the lease. After March 1, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.176 through 206.179 (1996)).

How was the Major Portion price calculated?

MMS has performed major portion analyses for natural gas production from Jicarilla Apache leases for the period **January 1984 through June 1995**. We have used gas sales data reported by the Jicarilla Apache Tribe (Jicarilla Apache) under their Royalty-in-Kind (RIK) program to determine major portion prices for the Jicarilla Apache Indian Reservation (Reservation) by production month. We have determined that the Jicarilla Apache sold the majority of their RIK production based on the Maximum Lawful Price (MLP) as set by the Natural Gas Policy Act (NGPA) in the following categories:

102 New natural gas	103 New onshore production
104 Several Categories	105 Existing intrastate
108 Stripper gas	109 Other gas

Enclosure 1 provides a list of major portion prices. These prices are based on the prices received under the Jicarilla Apache RIK contract by NGPA category by month. Enclosure 2 lists your accounting identification (AID) numbers for the Reservation. If you didn't pay royalties for the lease numbers in Enclosure 2 between January 1984 and June 1995, please state who did and the date your responsibility ended.

NOTE: The following section entitled Dual Accounting pertain to both those payors that stated they did or did not perform dual accounting. The final letter will be modified for each payor

Dual Accounting - did perform

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 3-6), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1996).

MMS has determined that the Jicarilla Apache lease terms require dual accounting (Section 3(c) entitled "Rental and Royalty"). MMS issued an order (September 29, 1995) to (*Short company name*) to provide a declaration of policy on dual accounting. On your response, you stated that the company did perform dual accounting on the Indian leases for which *Short company name* is a royalty payor. A review of sample months show that your dual accounting calculations were based on prices less than major portion prices shown in Enclosure 1. As a result, additional royalties may be due.

Dual Accounting - Did not perform

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 3-6), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1996).

MMS issued an order (September 29, 1995) to (*Short company name*) to provide a declaration of policy on dual accounting. On your response, you stated that the company did not perform dual accounting on the Indian leases for which *Short company name* is a royalty payor. MMS has determined that the Jicarilla Apache lease terms require dual accounting (Section 3© entitled "Rental and Royalty"). As a result, additional royalties may be due.

If you have any comments or questions concerning this request, contact Joseph Cornellisson at (303) 275-7239.

Sincerely,

Deborah Gibbs Tschudy
Chief, Royalty Valuation Division

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List of Enclosure

1.Major Portion Prices

2. AID numbers

3. September 30, 1988 Dear Payor letter

4. July 27, 1992 Dear Payor letter

5. February 2, 1993 Dear Payor letter

6. February 10, 1995 Dear Payor Letter

7. Mt. Belvieu liquids prices

8. EXCEL worksheet for dual accounting

9. Example dual accounting calculation

10. Format for reporting royalty changes

11. MMS 2014 (green)

12. Appeals rights and bonding requirements

8/29/97

METHODOLOGY FOR MAJOR PORTION AND DUAL ACCOUNTING ANALYSIS JICARILLA APACHE TRIBAL LEASES

Purpose

This report provides a background and describes the proposed methodology to be used in the major portion and dual accounting analyses that will be performed by the Royalty Valuation Division (RVD), Minerals Management Service (MMS), concerning natural gas produced from Jicarilla Apache Tribal leases.

Background

On December 6, 1996, representatives of the Jicarilla Apache Tribe (Tribe) and MMS met to discuss the implementation of major portion pricing for the natural gas produced from the Jicarilla Reservation. From July 1, 1975, to June 30, 1995, the Tribe sold gas under royalty-in-kind (RIK) agreements. Until 1989, gas was bought by either the Northwest Pipeline Corporation (Northwest) or the El Paso Natural Gas Company (El Paso) under long-term contracts. In 1989, the Tribe entered into contract settlements with El Paso and Northwest, thus, allowing the companies to pay market prices rather than the Natural Gas Policy Act (NGPA) ceiling prices.

On May 28, 1997, representatives of the Tribe and MMS met in Dallas, Texas to discuss the implementation of the major portion and dual accounting analysis. MMS presented a proposal to the Tribe that MMS would issue orders to perform major portion based on MLP for each payor's applicable category of gas rather than calculating a bundled median value based on all of the RIK sales data. The Tribe concurred with this approach. The Tribe also concurred that the orders should include dual accounting.

On June 17, 1997, representatives of the Tribe and MMS met to review the contract settlements, sources of data, pricing data, and combined major portion/dual accounting order to perform.

The RVD will use the Auditing and Financial System (AFS) database to determine prices paid by those payors who paid in-value. The prices paid by the payors who paid in-value will be compared to Tribal data and RVD will issue orders to those payors for any under payments plus interest.

Regulatory Criteria

The oil and gas valuation regulations found at 30 CFR 206 (1987), have long required that the "estimated reasonable value" of production be used for the purposes of computing royalties. Due consideration is given to the highest price paid for a part or for a major portion of gas of like quality in the same field, to the price received by the lessee, to posted prices, and to other relevant matters. Title 25 CFR 211 (Indian tribal) and the terms of the Jicarilla leases also specify that the value may, at the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered at the time of production for the major portion of gas and/or natural gasoline and/or all other hydrocarbon substances produced and sold from the field where the leased lands are located.

The amended valuation regulations at 30 CFR §§ 206.172 and 206.173 (1996) address the issue of major portion for Indian lands. Specifically, the regulations provide:

> For any Indian leases which provide that the Secretary may consider the highest price paid or offered for a major portion of production (major portion) in determining value of production for royalty purposes, if data are available to compute a major portion MMS will, where practicable, compare the value determined in accordance with this section with the major portion. The value to be used in determining the value of production for royalty purposes shall be the higher of those two values.

For natural gas, these regulations specify that a major portion price is determined for a particular quality of gas in the same field (or, if necessary, to obtain a reasonable sample from the same area). For this study, the Tribe specified the Reservation boundary as the area. Like-quality gas is gas of similar physical, chemical, and legal characteristics. Legal characteristics are generally the applicable NGPA category or subcategory and the regulated or deregulated status of the gas.
The price associated with the volume that causes the cumulative volume, summed beginning with the volume associated with the highest price (lowest price beginning March 1, 1988) to exceed 50 percent plus 1 Mcf of the total sales volume is deemed to be the major portion price. Approximately two-thirds of the Tribal production was sold under the RIK program at established NGPA pricing or at a contract price established between the purchasers and the Tribe. The Tribal volumes represented well over 50% of the total volumes and therefore the Tribal price was equated to the majority price.

Dual accounting requirements are specified by Indian lease terms, Federal regulations, and MMS instructions. Federal regulations at 25 CFR §§ 211.13 (1996) and 212.16 (1996) state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the

value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.152 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.153 (1996). Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.

Major Portion Methodology

Under the agreement reached between the MMS and Jicarilla representatives, the major portion methodology will identify monthly estimated median values for all gas production in the Jicarilla Reservation utilizing Tribal RIK data for the time period January 1984 through June 1995. The following key issues were agreed to by RVD and the Tribe at the December 6 and June 17 meetings:

- RVD will consider the Reservation as the "area" for calculating the major portion pricing.
- For the purpose of implementing the major portion pricing, RVD will assume that the production volumes equal the sales volumes from the Reservation.
- The price received for the RIK portion of the gas represents 1/8 royalty share. The RVD will extrapolate the 1/8 royalty share to the entire 8/8 production and assume that the value for the 1/8 royalty share is representative of the prices received for the other portion of the gas sold from the Reservation.[1]
- RVD will analyze a sample of Jicarilla settlement statements from Northwest and El Paso and certify that the Tribe received the proper NGPA prices.
- RVD will compare these values (wellhead values) and compare these values to a transportation-reduced price (net price) for the non-RIK volumes obtained from the AFS.
- When calculating the transportation-reduced prices for the non-RIK volumes, RVD will combine product codes 03 (residue gas) and 04 (unprocessed gas) reported by the payors on the Report of Sales and Royalty Remittance (Form MMS-2014).
- The RVD will send issue letters/orders to the non-RIK payors only.

[1]Approximately 2/3 of the 1/8 royalty share was sold under RIK contracts.

The NGPA Category

Beginning in the mid-1980's, changes in the natural gas market have made the consideration of NGPA category when determining like-quality gas far less important. Natural gas began to be sold and marketed under short-term contracts at prices reflective of the natural gas marketplace rather than under long-term contracts at a regulatory mandated or maximum lawful price (MLP). However, since the major portion analysis will include the time period beginning 1984, RVD will identify gas value by NGPA category for periods prior to the 1989 settlements. In the post-settlement period, RVD will identify the settlement price. In the issue letters that RVD will send to the non-RIK payors, we will provide gas value by NGPA category and request that the payor identify the NGPA category of their gas prior to the contract settlement. If the payor does not provide the NGPA category of the gas, RVD will then issue an order to those payors based on a median value of all NGPA categories of gas. In addition, RVD will not send orders to payors where the MLP prices for non-RIK volumes are less than the median price. For the post-settlement period, RVD will issue an order to those payors who have paid less than the contract settlement price.

The January 1985 through December 1988 prices are based on the NGPA price plus tax reimbursements received by the Jicarilla Apache and are shown by NGPA category by month. Starting in January 1989, the major portion prices are based on the prices recieved under the Jicarilla Apache RIK contract and are shown by NGPA category by month.

Definition of Field or Area

The majority of the Reservation is in Rio Arriba County with a small portion extending into Sandoval County. The Reservation lies along the eastern edge of the San Juan Basin, New Mexico. Gas production is from the Pictured Cliffs Formation, Mesaverde Group, Gallup, Tocito, and fractured Mancos Formations, and the Dakota and Dakota-Morrison Formations. The Fruitland Formation produces methane primarily from coals (Fruitland Coal). During the meeting between MMS and the Tribe it was agreed to use the Reservation boundary as the major portion area.

Calculation of Estimated Median Values

Data Processing

The AFS data on Form MMS-2014 will be processed on the MMS computer system. The

criteria for selecting this data is: (1) all AFS data within the Reservation boundary; (2) the product codes of 03 (residue gas) and 04 (unprocessed gas); and (3) the transaction codes of 01 (royalty) and 11 (transportation allowance). The program will sort the data base by lease, revenue source, selling arrangement, sales year, sales month, royalty quantity, and royalty value. The program will then identify all negative (adjusted) royalty quantities and values and search for a matching positive line. If a match is found, both the positive and negative line will be removed. Next, those negative lines without a matching positive (indicative of misreporting) will be removed from further processing.

The last operation is to calculate $/MMBtu gas prices by adjusting for the quality of the gas. The price will be calculated by using the reported royalty quantity and royalty value, and the associated transportation allowance costs will be subtracted from this sum to arrive at a net royalty value.

The Form MMS-2014 lines occasionally do not have a reported Btu content, or the Btu content is not within a reasonable range (900 - 1500), ~~or the payor reports the Btu content as 1000.~~ The MMS will calculate a monthly volume-weighted average Btu values for the Reservation area based on known Btu values contained within the AFS data.

Estimated Median Value Calculation

Upon completion of processing the RIK Tribal data, individual gas sales records covering the time period January 1984 through June 1995 will be sorted by sales year, sales month, and the calculated $/MMBtu net price. A program will then calculate the cumulative volume for each record, resetting the cumulative total when the production month changes. The price associated with the volume that causes the cumulative volume, summed beginning with the volume associated with the highest price (lowest price beginning March 1, 1988) to exceed 50 percent plus 1 Mcf of the total sales volume for the production month will be identified as the estimated (net) median gas value. The estimated (net) median value will then be compared to the net value for the non-RIK volumes.

The issue letters sent to payors will cite the requirement that royalty be based on the higher of the median value or gross proceeds accruing to the lessee as well as the requirement to perform dual accounting.

Dual Accounting Calculation

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.172 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.173 (1996). Royalty on gas produced from an Indian lease and ultimately processed (either by the lessee or any purchaser) must be computed by applying the dual accounting requirements specified by the lease and paid based on the method yielding the higher value. However, royalty is never to be based on a value which is less than the gross proceeds received by the lessee. (After March 31, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.176 through 206.179 (1996))).

Royalty on gas produced from an Indian lease and ultimately processed (either by the lessee or any purchaser must be computed by applying the dual accounting requirements specified by the lease. Value for the wellhead (unprocessed) stream is determined by the Btu method. The net realization method is used to determine the value of the processed stream. Indian royalty is to be calculated and paid based on the method yielding the higher value. However, royalty is never to be based on a value which is less than the gross proceeds received by the lessee.

For the Btu method, the volume of the unprocessed gas is measured at the wellhead and the Btu content is determined. The value of the gas is then calculated by multiplying the volume(adjusted for its Btu content) by the appropriate unit price.

In comparison, the net realization method determines the value of the gas based on the components of the gas. The aggregate of the values is determined and a processing allowance (not to exceed two-thirds of the total NGL value) is subtracted. After March 31, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.156 through 206.159 (1996)).

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10/7/97

METHODOLOGY FOR MAJOR PORTION AND DUAL ACCOUNTING ANALYSIS JICARILLA APACHE TRIBAL LEASES

Purpose

This report provides a background and describes the proposed methodology to be used in the major portion and dual accounting analyses that will be performed by the Royalty Valuation Division (RVD), Minerals Management Service (MMS), concerning natural gas produced from Jicarilla Apache Tribal leases.

Background

On December 6, 1996, representatives of the Jicarilla Apache Tribe (Tribe) and MMS met to discuss the implementation of major portion pricing for the natural gas produced from the Jicarilla Reservation. From July 1, 1975, to June 30, 1995, the Tribe sold gas under royalty-in-kind (RIK) agreements. Until 1989, gas was bought by either the Northwest Pipeline Corporation (Northwest) or the El Paso Natural Gas Company (El Paso) under long-term contracts. In 1989, the Tribe entered into contract settlements with El Paso and Northwest, thus, allowing the companies to pay market prices rather than the Natural Gas Policy Act (NGPA) ceiling prices.

On May 28, 1997, representatives of the Tribe and MMS met in Dallas, Texas to discuss the implementation of the major portion and dual accounting analysis. MMS presented a proposal to the Tribe that MMS would issue orders to perform major portion based on MLP for each payor's applicable category of gas rather than calculating a bundled median value based on all of the RIK sales data. The Tribe concurred with this approach. The Tribe also concurred that the orders should include dual accounting.

On June 17, 1997, representatives of the Tribe and MMS met to review the contract settlements, sources of data, pricing data, and combined major portion/dual accounting order to perform.

The RVD will use the Auditing and Financial System (AFS) database to determine prices paid by those payors who paid in-value. The prices paid by the payors who paid in-value will be compared to Tribal data and RVD will issue orders to those payors for any under payments plus interest.

Regulatory Criteria

The oil and gas valuation regulations found at 30 CFR 206 (1987), have long required that the "estimated reasonable value" of production be used for the purposes of computing royalties. Due consideration is given to the highest price paid for a part or for a major portion of gas of like quality in the same field, to the price received by the lessee, to posted prices, and to other relevant matters. Title 25 CFR 211 (Indian tribal) and the terms of the Jicarilla leases also specify that the value may, at the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered at the time of production for the major portion of gas and/or natural gasoline and/or all other hydrocarbon substances produced and sold from the field where the leased lands are located.

The amended valuation regulations at 30 CFR §§ 206.172 and 206.173 (1996) address the issue of major portion for Indian lands. Specifically, the regulations provide:

> For any Indian leases which provide that the Secretary may consider the highest price paid or offered for a major portion of production (major portion) in determining value of production for royalty purposes, if data are available to compute a major portion MMS will, where practicable, compare the value determined in accordance with this section with the major portion. The value to be used in determining the value of production for royalty purposes shall be the higher of those two values.

For natural gas, these regulations specify that a major portion price is determined for a particular quality of gas in the same field (or, if necessary, to obtain a reasonable sample from the same area). For this study, the Tribe specified the Reservation boundary as the area. Like-quality gas is gas of similar physical, chemical, and legal characteristics. Legal characteristics are generally the applicable NGPA category or subcategory and the regulated or deregulated status of the gas.
The price associated with the volume that causes the cumulative volume, summed beginning with the volume associated with the highest price (lowest price beginning March 1, 1988) to exceed 50 percent plus 1 Mcf of the total sales volume is deemed to be the major portion price. Approximately two-thirds of the Tribal production was sold under the RIK program at established NGPA pricing or at a contract price established between the purchasers and the Tribe. The Tribal volumes represented well over 50% of the total volumes and therefore the Tribal price was equated to the majority price.

Dual accounting requirements are specified by Indian lease terms, Federal regulations, and MMS instructions. Federal regulations at 25 CFR §§ 211.13 (1996) and 212.16 (1996) state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the

value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.152 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.153 (1996). Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.

Major Portion Methodology

Under the agreement reached between the MMS and Jicarilla representatives, the major portion methodology will identify monthly estimated median values for all gas production in the Jicarilla Reservation utilizing Tribal RIK data for the time period January 1984 through June 1995. The following key issues were agreed to by RVD and the Tribe at the December 6 and June 17 meetings:

- RVD will consider the Reservation as the "area" for calculating the major portion pricing.
- For the purpose of implementing the major portion pricing, RVD will assume that the production volumes equal the sales volumes from the Reservation.
- The price received for the RIK portion of the gas represents 1/8 royalty share. The RVD will extrapolate the 1/8 royalty share to the entire 8/8 production and assume that the value for the 1/8 royalty share is representative of the prices received for the other portion of the gas sold from the Reservation.[1]
- RVD will analyze a sample of Jicarilla settlement statements from Northwest and El Paso and certify that the Tribe received the proper NGPA prices.
- ~~RVD will compare these values (wellhead values) and compare these values to a transportation-reduced price (net price) for the non-RIK volumes obtained from the AFS.~~
- ~~When calculating the transportation-reduced prices for the non-RIK volumes, RVD will combine product codes 03 (residue gas) and 04 (unprocessed gas) reported by the payors on the Report of Sales and Royalty Remittance (Form MMS-2014).~~
- The RVD will send issue letters/orders to the non-RIK payors only.

[1]Approximately 2/3 of the 1/8 royalty share was sold under RIK contracts.

The NGPA Category

Beginning in the mid-1980's, changes in the natural gas market have made the consideration of NGPA category when determining like-quality gas far less important. Natural gas began to be sold and marketed under short-term contracts at prices reflective of the natural gas marketplace rather than under long-term contracts at a regulatory mandated or maximum lawful price (MLP). However, since the major portion analysis will include the time period beginning 1984, RVD will identify gas value by NGPA category for periods prior to the 1989 settlements. In the post-settlement period, RVD will identify the settlement price. In the issue letters that RVD will send to the non-RIK payors, we will provide gas value by NGPA category and request that the payor identify the NGPA category of their gas prior to the contract settlement. If the payor does not provide the NGPA category of the gas, RVD will then issue an order to those payors based on a median value of all NGPA categories of gas. In addition, RVD will not send orders to payors where the MLP prices for non-RIK volumes are less than the median price. For the post-settlement period, RVD will issue an order to those payors who have paid less than the contract settlement price.

The January 1985 through December 1988 prices are based on the NGPA price plus tax reimbursements received by the Jicarilla Apache and are shown by NGPA category by month. Starting in January 1989, the major portion prices are based on the prices recieved under the Jicarilla Apache RIK contract and are shown by NGPA category by month.

Definition of Field or Area

The majority of the Reservation is in Rio Arriba County with a small portion extending into Sandoval County. The Reservation lies along the eastern edge of the San Juan Basin, New Mexico. Gas production is from the Pictured Cliffs Formation, Mesaverde Group, Gallup, Tocito, and fractured Mancos Formations, and the Dakota and Dakota-Morrison Formations. The Fruitland Formation produces methane primarily from coals (Fruitland Coal). During the meeting between MMS and the Tribe it was agreed to use the Reservation boundary as the major portion area.

Calculation of Estimated Major Portion Values

The major portion calculation has been divided into four time periods :

- **Period 1:NGPA pricing was in effect for both pipelines.**
- **Period 2:Both pipelines had negotiated reduced prices for a 6 - 12 month time period.**
- **Period 3:NGPA pricing was in effect for both pipelines**
- **Period 4:Northwest negotiated a buyout of their contract and El Paso negotiated**

a buydown of their contract.

The time periods and effective prices are shown below:

TABLE 1

Period	Time Period	El Paso Price	Northwest Price
1	1984-1986	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
2	January 1987 - June 1987	$2.50	NGPA & Tax Reimbursement
2	July 1987 - June 1988	NGPA & Tax Reimbursement	Contract Negotiated Price
3	July 1988 - December 1988	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
3	January 1989 - June 1989	NGPA & Tax Reimbursement; Contract Buydown 7/89	Contract Buyout - Feb
4	July 1989 - December 1989	$1.227 + settlement allocation per NGPA category	
4	1990	$1.276 + settlement allocation per NGPA category	
4	1991	$1.327 + settlement allocation per NGPA category	
4	1992	$1.380 + settlement allocation per NGPA category	
4	1993	$1.435 + settlement allocation per NGPA category	
4	1994	$1.493 + settlement allocation per NGPA	

		category	
4	1995	$1.553 + settlement allocation per NGPA category	

TABLE 2

Date	Severence Tax (Per MMBtu)	Privilage Tax (87.5% of Value)
1/1/84 through 5/30/85	$0.05	
6/1/85 through 1/31/86	$0.05	5.00%
2/1/86 through 1/31/87	$0.05	5.18%
2/1/87 through 1/31/88	$0.05	5.28%
2/1/88 through 12/31/88	$0.05	5.47%

The issue letters sent to payors will cite the requirement that royalty be based on the higher of the median value or gross proceeds accruing to the lessee as well as the requirement to perform dual accounting.

Dual Accounting Calculation

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.172 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.173 (1996). Royalty on gas produced from an Indian lease and ultimately processed (either by the lessee or any purchaser) must be computed by applying the dual accounting requirements specified by the lease and paid based on the method yielding the higher value. However, royalty is never to be based on a value which is less than the gross proceeds received by the lessee. (After March 31, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.176 through 206.179 (1996))).

Royalty on gas produced from an Indian lease and ultimately processed (either by the lessee or any purchaser must be computed by applying the dual accounting requirements specified by the lease. Value for the wellhead (unprocessed) stream is determined by the Btu method. The net realization method is used to determine the value of the processed stream. Indian royalty is to be calculated and paid based on the method yielding the higher value. However, royalty is never to be based on a value which is less than the gross proceeds received by the lessee.

For the Btu method, the volume of the unprocessed gas is measured at the wellhead and the Btu content is determined. The value of the gas is then calculated by multiplying the volume(adjusted for its Btu content) by the appropriate unit price.

In comparison, the net realization method determines the value of the gas based on the components of the gas. The aggregate of the values is determined and a processing allowance (not to exceed two-thirds of the total NGL value) is subtracted. After March 31, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.156 through 206.159 (1996)).

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8/29/97

METHODOLOGY FOR MAJOR PORTION AND DUAL ACCOUNTING ANALYSIS JICARILLA APACHE TRIBAL LEASES

Purpose

This report provides a background and describes the proposed methodology to be used in the major portion and dual accounting analyses that will be performed by the Royalty Valuation Division (RVD), Minerals Management Service (MMS), concerning natural gas produced from Jicarilla Apache Tribal leases.

Background

On December 6, 1996, representatives of the Jicarilla Apache Tribe (Tribe) and MMS met to discuss the implementation of major portion pricing for the natural gas produced from the Jicarilla Reservation. From July 1, 1975, to June 30, 1995, the Tribe sold gas under royalty-in-kind (RIK) agreements. Until 1989, gas was bought by either the Northwest Pipeline Corporation (Northwest) or the El Paso Natural Gas Company (El Paso) under long-term contracts. In 1989, the Tribe entered into contract settlements with El Paso and Northwest, thus, allowing the companies to pay market prices rather than the Natural Gas Policy Act (NGPA) ceiling prices.

On May 28, 1997, representatives of the Tribe and MMS met in Dallas, Texas to discuss the implementation of the major portion and dual accounting analysis. MMS presented a proposal to the Tribe that MMS would issue orders to perform major portion based on MLP for each payor's applicable category of gas rather than calculating a bundled median value based on all of the RIK sales data. The Tribe concurred with this approach. The Tribe also concurred that the orders should include dual accounting.

On June 17, 1997, representatives of the Tribe and MMS met to review the contract settlements, sources of data, pricing data, and combined major portion/dual accounting order to perform.

The RVD will use the Auditing and Financial System (AFS) database to determine prices paid by those payors who paid in-value. The prices paid by the payors who paid in-value will be compared to Tribal data and RVD will issue orders to those payors for any under payments plus interest.

Regulatory Criteria

The oil and gas valuation regulations found at 30 CFR 206 (1987), have long required that the "estimated reasonable value" of production be used for the purposes of computing royalties. Due consideration is given to the highest price paid for a part or for a major portion of gas of like quality in the same field, to the price received by the lessee, to posted prices, and to other relevant matters. Title 25 CFR 211 (Indian tribal) and the terms of the Jicarilla leases also specify that the value may, at the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered at the time of production for the major portion of gas and/or natural gasoline and/or all other hydrocarbon substances produced and sold from the field where the leased lands are located.

The amended valuation regulations at 30 CFR §§ 206.172 and 206.173 (1996) address the issue of major portion for Indian lands. Specifically, the regulations provide:

> For any Indian leases which provide that the Secretary may consider the highest price paid or offered for a major portion of production (major portion) in determining value of production for royalty purposes, if data are available to compute a major portion MMS will, where practicable, compare the value determined in accordance with this section with the major portion. The value to be used in determining the value of production for royalty purposes shall be the higher of those two values.

For natural gas, these regulations specify that a major portion price is determined for a particular quality of gas in the same field (or, if necessary, to obtain a reasonable sample from the same area). For this study, the Tribe specified the Reservation boundary as the area. Like-quality gas is gas of similar physical, chemical, and legal characteristics. Legal characteristics are generally the applicable NGPA category or subcategory and the regulated or deregulated status of the gas.
The price associated with the volume that causes the cumulative volume, summed beginning with the volume associated with the highest price (lowest price beginning March 1, 1988) to exceed 50 percent plus 1 Mcf of the total sales volume is deemed to be the major portion price. Approximately two-thirds of the Tribal production was sold under the RIK program at established NGPA pricing or at a contract price established between the purchasers and the Tribe. The Tribal volumes represented well over 50% of the total volumes and therefore the Tribal price was equated to the majority price.

Dual accounting requirements are specified by Indian lease terms, Federal regulations, and MMS instructions. Federal regulations at 25 CFR §§ 211.13 (1996) and 212.16 (1996) state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the

> value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.152 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.153 (1996). Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.

Major Portion Methodology

Under the agreement reached between the MMS and Jicarilla representatives, the major portion methodology will identify monthly estimated median values for all gas production in the Jicarilla Reservation utilizing Tribal RIK data for the time period January 1984 through June 1995. The following key issues were agreed to by RVD and the Tribe at the December 6 and June 17 meetings:

- RVD will consider the Reservation as the "area" for calculating the major portion pricing.
- For the purpose of implementing the major portion pricing, RVD will assume that the production volumes equal the sales volumes from the Reservation.
- The price received for the RIK portion of the gas represents 1/8 royalty share. The RVD will extrapolate the 1/8 royalty share to the entire 8/8 production and assume that the value for the 1/8 royalty share is representative of the prices received for the other portion of the gas sold from the Reservation.[1]
- RVD will analyze a sample of Jicarilla settlement statements from Northwest and El Paso and certify that the Tribe received the proper NGPA prices.
- RVD will compare these values (wellhead values) and compare these values to a transportation-reduced price (net price) for the non-RIK volumes obtained from the AFS.
- When calculating the transportation-reduced prices for the non-RIK volumes, RVD will combine product codes 03 (residue gas) and 04 (unprocessed gas) reported by the payors on the Report of Sales and Royalty Remittance (Form MMS-2014).
- The RVD will send issue letters/orders to the non-RIK payors only.

[1]Approximately 2/3 of the 1/8 royalty share was sold under RIK contracts.

The NGPA Category

Beginning in the mid-1980's, changes in the natural gas market have made the consideration of NGPA category when determining like-quality gas far less important. Natural gas began to be sold and marketed under short-term contracts at prices reflective of the natural gas marketplace rather than under long-term contracts at a regulatory mandated or maximum lawful price (MLP). However, since the major portion analysis will include the time period beginning 1984, RVD will identify gas value by NGPA category for periods prior to the 1989 settlements. In the post-settlement period, RVD will identify the settlement price. In the issue letters that RVD will send to the non-RIK payors, we will provide gas value by NGPA category and request that the payor identify the NGPA category of their gas prior to the contract settlement. If the payor does not provide the NGPA category of the gas, RVD will then issue an order to those payors based on a median value of all NGPA categories of gas. In addition, RVD will not send orders to payors where the MLP prices for non-RIK volumes are less than the median price. For the post-settlement period, RVD will issue an order to those payors who have paid less than the contract settlement price.

The January 1985 through December 1988 prices are based on the NGPA price plus tax reimbursements received by the Jicarilla Apache and are shown by NGPA category by month. Starting in January 1989, the major portion prices are based on the prices recieved under the Jicarilla Apache RIK contract and are shown by NGPA category by month.

Definition of Field or Area

The majority of the Reservation is in Rio Arriba County with a small portion extending into Sandoval County. The Reservation lies along the eastern edge of the San Juan Basin, New Mexico. Gas production is from the Pictured Cliffs Formation, Mesaverde Group, Gallup, Tocito, and fractured Mancos Formations, and the Dakota and Dakota-Morrison Formations. The Fruitland Formation produces methane primarily from coals (Fruitland Coal). During the meeting between MMS and the Tribe it was agreed to use the Reservation boundary as the major portion area.

Calculation of Estimated Median Values

Data Processing

The AFS data on Form MMS-2014 will be processed on the MMS computer system. The

criteria for selecting this data is: (1) all AFS data within the Reservation boundary; (2) the product codes of 03 (residue gas) and 04 (unprocessed gas); and (3) the transaction codes of 01 (royalty) and 11 (transportation allowance). The program will sort the data base by lease, revenue source, selling arrangement, sales year, sales month, royalty quantity, and royalty value. The program will then identify all negative (adjusted) royalty quantities and values and search for a matching positive line. If a match is found, both the positive and negative line will be removed. Next, those negative lines without a matching positive (indicative of misreporting) will be removed from further processing.

The last operation is to calculate $/MMBtu gas prices by adjusting for the quality of the gas. The price will be calculated by using the reported royalty quantity and royalty value, and the associated transportation allowance costs will be subtracted from this sum to arrive at a net royalty value.

The Form MMS-2014 lines occasionally do not have a reported Btu content, or the Btu content is not within a reasonable range (900 - 1500), ~~or the payor reports the Btu content as 1000.~~ The MMS will calculate a monthly volume-weighted average Btu values for the Reservation area based on known Btu values contained within the AFS data.

Estimated Median Value Calculation

Upon completion of processing the RIK Tribal data, individual gas sales records covering the time period January 1984 through June 1995 will be sorted by sales year, sales month, and the calculated $/MMBtu net price. A program will then calculate the cumulative volume for each record, resetting the cumulative total when the production month changes. The price associated with the volume that causes the cumulative volume, summed beginning with the volume associated with the highest price (lowest price beginning March 1, 1988) to exceed 50 percent plus 1 Mcf of the total sales volume for the production month will be identified as the estimated (net) median gas value. The estimated (net) median value will then be compared to the net value for the non-RIK volumes.

The issue letters sent to payors will cite the requirement that royalty be based on the higher of the median value or gross proceeds accruing to the lessee as well as the requirement to perform dual accounting.

Dual Accounting Calculation

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.172 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.173 (1996). Royalty on gas produced from an Indian lease and ultimately processed (either by the lessee or any purchaser) must be computed by applying the dual accounting requirements specified by the lease and paid based on the method yielding the higher value. However, royalty is never to be based on a value which is less than the gross proceeds received by the lessee. (After March 31, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.176 through 206.179 (1996))).

Royalty on gas produced from an Indian lease and ultimately processed (either by the lessee or any purchaser must be computed by applying the dual accounting requirements specified by the lease. Value for the wellhead (unprocessed) stream is determined by the Btu method. The net realization method is used to determine the value of the processed stream. Indian royalty is to be calculated and paid based on the method yielding the higher value. However, royalty is never to be based on a value which is less than the gross proceeds received by the lessee.

For the Btu method, the volume of the unprocessed gas is measured at the wellhead and the Btu content is determined. The value of the gas is then calculated by multiplying the volume(adjusted for its Btu content) by the appropriate unit price.

In comparison, the net realization method determines the value of the gas based on the components of the gas. The aggregate of the values is determined and a processing allowance (not to exceed two-thirds of the total NGL value) is subtracted. After March 31, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.156 through 206.159 (1996)).

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June 18, 2004

METHODOLOGY FOR MAJOR PORTION AND DUAL ACCOUNTING ANALYSIS JICARILLA APACHE TRIBAL LEASES

Purpose

The purpose of this report is to provide a background and discuss the results of major portion and dual accounting analyses recently undertaken by the Royalty Valuation Division (RVD), Royalty Management Program (RMP), Minerals Management Service (MMS), concerning natural gas produced from Jicarilla Apache Tribal leases.

Background

On December 6, 1996, representatives of the Jicarilla Apache Tribe (Jicarilla Tribe) and MMS met to discuss the implementation of major portion pricing for the natural gas produced from the Jicarilla Reservation. From July 1, 1975, to June 30, 1995, the Jicarilla Tribe sold gas under royalty-in-kind (RIK) agreements. Until 1989, gas was bought by either the Northwest Pipeline Corporation (Northwest) or the El Paso Natural Gas Company (El Paso) under long-term contracts. In 1989, the Jicarilla Tribe entered into contract settlements with El Paso and Northwest, thus, allowing the companies to pay market prices rather than the Natural Gas Policy Act (NGPA) ceiling prices.

On May 28, 1997, representatives of the Jicarilla Tribe and MMS met in Dallas, Texas to discuss the implementation of the major portion and dual accounting analysis. MMS presented a proposal to the Jicarilla Tribe that MMS would issue orders to perform major portion based on NGPA prices for each payor's applicable category of gas. The Jicarilla Tribe concurred with this approach. The Jicarilla Tribe also concurred that the orders should also include dual accounting.

On June 17, 1997, representatives of the Jicarilla Tribe and MMS met to review the contract settlements, sources of data, pricing data, and the major portion/dual accounting order to perform.

Regulatory Criteria

The oil and gas valuation regulations found at 30 CFR §206 (1987), have long required that the "estimated reasonable value" of production be used for the purposes of computing royalties. Due consideration is given to the highest price paid for a part or for a major portion of gas of like quality in the same field, to the price received by the lessee, to posted prices, and to other relevant matters. Title 25 CFR § 211 (Indian tribal) and the terms of the Jicarilla leases also specify that the value may, at the discretion of the Secretary of the

Interior, be calculated on the basis of the highest price paid or offered at the time of production for the major portion of gas and/or natural gasoline and/or all other hydrocarbon substances produced and sold from the field where the leased lands are located.

The amended valuation regulations at 30 CFR §§ 206.172 and 206.173 (1996) address the issue of major portion for Indian lands. Specifically, the regulations provide:

> For any Indian leases which provide that the Secretary may consider the highest price paid or offered for a major portion of production (major portion) in determining value of production for royalty purposes, if data are available to compute a major portion MMS will, where practicable, compare the value determined in accordance with this section with the major portion. The value to be used in determining the value of production for royalty purposes shall be the higher of those two values.

For natural gas, these regulations specify that a major portion price is calculated for a like quality of gas in the same field (or, if necessary, to obtain a reasonable sample from the same area). Like-quality gas is gas of similar physical, chemical, and legal characteristics. Legal characteristics are generally the applicable NGPA category or subcategory and the regulated or deregulated status of the gas.

The price associated with the volume that causes the cumulative volume, summed beginning with the volume associated with the highest price (lowest price beginning March 1, 1988) to exceed 50 percent plus 1 Mcf of the total sales volume is deemed to be the major portion price. Approximately two-thirds of the Jicarilla production was sold under the RIK program at established NGPA pricing or at a contract price established between the purchasers and the Jicarilla Tribe. The Jicarilla RIK volumes represented well over 50% of the total volumes and therefore the Jicarilla price was equated to the majority price.

Dual accounting requirements are specified by Indian lease terms, Federal regulations, and MMS instructions. Federal regulations at 25 CFR §§ 211.13 (1996) and 212.16 (1996) state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.152 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.153 (1996). Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.

Major Portion Methodology

Under the agreement reached between the MMS and Jicarilla representatives, the major portion methodology will identify the prices paid under contracts and settlement agreements and calculate the estimated major portion by NGPA category for all gas production in the Jicarilla Reservation utilizing RIK data for the time period January 1984 through June 1995. The following key issues were agreed to by RVD and the Jicarilla Tribe at the December 6 and June 17 meetings:

- RVD will consider the Reservation as the "area" for calculating the major portion pricing.
- For the purpose of implementing the major portion pricing, RVD will assume that the production volumes equal the sales volumes from the Reservation.
- The price received for the RIK portion of the gas represents 1/8 royalty share. The RVD will extrapolate the 1/8 royalty share to the entire 8/8 production and assume value for the 1/8 royalty share is representative of the prices received for the other portion of the gas sold from the Reservation.[1]
- RVD will analyze a sample of Jicarilla settlement statements from Northwest and El Paso and certify that the Jicarilla Tribe received the proper NGPA prices.
- RVD will send orders to the non-RIK payors only.

The NGPA Category

The major portion analysis covers from January 1984 through June 1995. Beginning with 1984, RVD identified gas values by NGPA category for periods prior to the 1989 settlements. In the post-settlement period, RVD identified the settlement price by NGPA category. In the orders that RVD will send to the non-RIK payors, we will provide gas value by NGPA category and request that the payor identify the NGPA category of their gas, and time periods for which the company was a payor between January 1984 and June 1995.

The January 1984 through December 1986 and July 1988 through December 1988 prices are based on the NGPA prices plus tax reimbursements received by the Jicarilla Apache and are

[1] Approximately 2/3 of the 1/8 royalty share was sold under RIK contracts.

shown by NGPA category by month. The NGPA categories identified include:

102 New natural gas	103 New onshore production
104 Post - 1974 gas	104 1973-1974 Biennium gas
104 Replacement gas	104 Flowing gas
104 Rocky Mountain gas	105 Existing intrastate gas
108 Stripper gas	109 Other gas

The January 1987 through June 1988 major portion prices are based on a weighted average price received by the Jicarilla Apache resulting from a negotiated temporary price reduction between the Tribe and Northwest and El Paso. Starting in January 1989, the major portion prices are based on the prices received under the Jicarilla Apache RIK contract plus contract settlements and are shown by NGPA category by month.

RVD used the Auditing and Financial System (AFS) database to determine prices paid by those payors who paid in-value and to determine that the RIK prices represent the major portion price. The RVD will review the responses to the September 29, 1995, Dear Payor letter and will issue orders to dual account and pay royalties on major portion prices. For those companies who stated that they performed dual accounting, RVD compared prices paid by the payors who paid in-value to the calculated major portion prices to determine that orders should be issued. RVD will issue orders to those payors who paid in value (Attachment 4) requiring payments on the higher of gross proceeds prices or major portion prices for any under payments plus interest. The orders will require dual accounting based on the higher of these prices.

<u>Definition of Field or Area</u>

The majority of the Reservation is within Rio Arriba County, New Mexico, with a small portion extending into Sandoval County, New Mexico. The Reservation lies along the eastern edge of the San Juan Basin. Gas production is from the Pictured Cliffs Formation, Mesaverde Group, Gallup, Tocito, and fractured Mancos Formations, and the Dakota and Dakota-Morrison Formations. The Fruitland Formation produces methane primarily from coals (Fruitland Coal). CFR 205 § 172 state major portion will be calculated on "like quality of gas in the same field (or, if necessary, to obtain a reasonable sample from the same area)." However, the State of New Mexico utilizes pool, rather than, field definitions. A pool is a "common source of supply" and is generally based on a geologic horizon. The State of New Mexico Oil and Gas Commission defines 30 pools that overly or are within the Jicarilla Reservation boundary. In several cases, several pools overly one another and/or extend well outside the Reservation boundary. Consequently, we are unable to define distinct field boundaries for Jicarilla gas production. Therefore, for this study, the Jicarilla Reservation boundary will be defined as the area. During the June 17, 1997 meeting between MMS and the Jicarilla Tribe, the Tribal representative agreed to use the Reservation boundary as the major portion area.

Calculation of Estimated Major Portion Values

The major portion calculation has been divided into four time periods :

- Period 1: NGPA pricing was in effect for both El Paso and Northwest contracts.
- Period 2: El Paso negotiated a temporary price reduction from the NGPA prices for the January through June 1987 period. Northwest negotiated a temporary price reduction from the NGPA prices for the July 1987 through December 1988 period.
- Period 3: NGPA pricing was in effect for both pipelines.
- Period 4: Northwest negotiated a buy out of their contract and El Paso negotiated a buy down of their contract.

The time periods and effective prices are shown in Table 1.

TABLE 1
Natural Gas Pricing Variations

Period	Time Period	El Paso Price	Northwest Price
1	1984-1986	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
2	January 1987 - June 1987	$2.50	NGPA & Tax Reimbursement
2	July 1987 - June 1988	NGPA & Tax Reimbursement	Contract Negotiated Price
3	July 1988 - December 1988	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
3	January 1989 - June 1989	NGPA & Tax Reimbursement; Contract Buy down 7/89	Contract Buy out - 2/89
4	July 1989 - December 1989	$1.227 + buy down	Buy out
4	1990	$1.276 + buy down	Buy out
4	1991	$1.327 + buy down	Buy out
4	1992	$1.380 + buy down	Buy out
4	1993	$1.435 + buy down	Buy out
4	1994	$1.493 + buy down	Buy out
4	1995	$1.553 + buy down	Buy out

Tax Reimbursement information was provided by the Jicarilla Tribal Tax manual and is shown in Table 2.

TABLE 2
Jicarilla Tax Rates

Date	Severance Tax (Per MMBtu)	Privilege Tax (87.5% of Value)
1/1/84 through 5/30/85	$0.05	
6/1/85 through 1/31/86	$0.05	5.00%
2/1/86 through 1/31/87	$0.05	5.18%
2/1/87 through 1/31/88	$0.05	5.28%
2/1/88 through 12/31/88	$0.05	5.47%

Major portion prices were determined by prices received under the Jicarilla RIK contract and are shown in Attachment 1. For periods 1 and 3, the major portions prices were the sum of the published NGPA prices and the tax reimbursments. The prices received by the Tribe in Period 2 (the market out period) and Period 4 (the post-settlement period) are calculated as discussed below.

During the market out period (Period 2), January 1987 through June 1988, RVD calculated a weighted average price received for each NGPA category by multiplying the contract price times the Strata estimate reserve volumes and dividing the total value for El Paso and Northwest by the total Strata estimate volumes (Attachment 3).

After the Northwest and El Paso contract settlements, major portion prices were determined by adding the settlement proceeds by NGPA category to the actual prices received under the El Paso settlement to determine the total consideration received under the RIK contract for each NGPA category. Documents provided in support of the RIK contract settlements proceeds provided detailed information on the settlement monies received for each NGPA categories. These amounts were used to determine the major portion prices by category.

Strata Evaluation Associates, Inc. (Strata) calculated the amounts due the Jicarilla Tribe for contract settlements with El Paso and Northwest based on volumetric decline curve analysis of the wells supplying El Paso and Northwest. The contract settlements were based on the difference between the projected NGPA prices due under the original contract and the price negotiated under the buy out or buy down contract. Based on the projected NGPA prices and volumetric analysis, Strata calculated an annual present value estimate of the remaining reserves for both El Paso and Northwest (Column B) as shown on Attachment 1. This value was then discounted using a 10% discount rate (Column C). This discounted settlement value was further reduced during negotiations between the Jicarilla Apache Tribe and the pipeline companies. A settlement factor was calculated by dividing the actual settlement amount by the discounted settlement . This settlement factor was then applied to the discounted amounts to determine a total annual settlement value (Column D). The annual settlement value was then divided by the annual present value estimate to generate a discount factor (Column E). A price differential (Column H) was calculated between the projected NGPA price (Column G) and the buy down/buy out price (Column G). This differential represents the undiscounted value that the Tribe would have received if the contract had not been bought out or bought down. The undiscounted value was then discounted using the discount factor discussed above to generate a settled price differential (column I). This differential was then added to the buy down/buy out price to determine the major portion price (Column J) by category.

For those NGPA prices that were less than the buy down/buy out price, the major portion prices were equated tot he actual buy down/buy out price (coulmn L, M).

RVD the calculated a weighted average price for the Northwest contract and the El Paso contract. This price was calculated by multiplying the price received for each NGPA category for by Strata reserve volume and dividing both calculated values by the total volume for El Paso and Northwest (Attachment 2).

The orders will cite the requirement that royalty be based on the higher of the major portion value or gross proceeds accruing to the lessee as well as the requirement to perform dual accounting. Sales by affiliates may provide information concerning gross proceeds to the lessee and the appropriate benchmark value in some situations and thus may be considered in determining royalty values.

Dual Accounting Calculation

Dual accounting requirements are specified by Indian lease terms and Federal regulations found at 25 CFR § 211.13 (1996) which state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that <u>royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater</u> [Emphasis added.]

Dual accounting is defined as a valuation method that requires the lessee to compute royalties based on the <u>greater of</u>: (1) the value of the gas prior to processing (as determined under 30 CFR § 206.172 (1996)), or (2) the combined value of the residue gas and gas plant products resulting from processing the gas (as determined under 30 CFR § 206.173 (1996)), plus the value of any condensate recovered downstream of the point of royalty settlement without resorting to processing (30 CFR § 206.52(1996)). However, the value of production can never be less than the gross proceeds accruing to the lease (30 CFR §§ 206.172(h) and 206.173(h) (1996)). After March 1, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR §§ 206.176 through 206.179 (1996)).

RVD reviewed comparable contracts for the sales of natural gas liquids (NGLP's). RVD found 2 contracts with sales in the San Juan Basin. Both these contracts called for Mt. Belview spot prices for NGLP's. RVD determined that the comparable contract price for NGLP's for the reservation was the average Mt. Belview, Texas spot market prices. The orders will require the calculations for liquids be based on the higher of the gross proceeds price received for liquids or the average Mt. Belview spot market price.

Data Retrieval

During September 1996, AFS data as reported on Form MMS-2014, was extracted from the AFS database, processed and downloaded to a Microsoft Access table on the RVD Local Area Network. The criteria for extracting this data were: (1) all AFS data reported under Fund Code 550 (the fund code for the Jicarilla Reservation); (2) the product codes of 03 (residue gas) and 04 (unprocessed gas); and (3) the transaction codes of 01 (royalty) and 11 (transportation allowance).

Data Processing

Once extracted from the AFS database, the information was processed by a program that removed adjustments to previously submitted information. This program first sorted the database by lease, product code, revenue source, selling arrangement, sales year, sales month, royalty quantity, and royalty value. The program then identified all negative (adjusted) royalty quantities and values and searched for a matching positive line. If a match was found, both the positive and negative lines were removed. Next, those negative lines without a matching positive (indicative of misreporting) were written to an error file and removed from further processing.

The next operation performed on the data was to determine major portion prices. We calculated MMBtu prices by adjusting for the quality of the gas.

A problem encountered in the data was that some records did not have a reported gas quality or bad a Btu content that was not within a reasonable range. Option included removing those records, using the quality last reported for the lease, or assuming a quality.

After analyzing this problem, we decided that given our manpower restrictions and obvious misreporting from the payors, the best option was to calculate a gas quality from the data available. We determined the 1996 average quality reported on the Form 3160 for all Jicarilla leases and calculated the range reported on all Jicarilla leases. We used the average Btu reported on the Form 3160 for each lease for all 04 lines submitted that did not report a quality or reported a quality outside of the average range. We used the average Btu reported on the MMS-2014 for all 03 lines submitted that did not report a quality or reported a quality outside of the average range.

Major Portion Value Calculation

Upon completion of processing, the database for the Jicarilla Reservation contained 47,463 records. In addition, MMS did not properly require the purchaser's of RIK production to report those sales on the MMS-2014, so RVD had to manually add the RIK sales data to the major portion calculation. MMS extracted AFS database lines for each month and arrayed lines by MMBtu price from highest price to lowest price (at the bottom). RVD then determined the amount of RIK production sold from the Jicarilla purchase statements by month and determined an average MMBtu price. RVD calculated that price at which 50 percent (by volume) plus 1 mcf of the gas (starting from the bottom) is sold.

RVD downloaded all royalty payments for Fund Code 550 (Jicarilla Tribe). We then summarized the payments for 2/88 by payor. We added the total RIK volumes purchased by El Paso and Northwest for 2/88 and determined the total sales for the reservation. RVD then divided total RIK sales by the total sales for the reservation to determine the percentage of reservation gas which was sold as RIK. Our review indicated that 66% of the royalty production on the reservation was sold as RIK therefore, the major portion prices were always the equivalent of the RIK values
(Attachment 5).

Global Settlements

The Jicarilla Tribe has entered global settlement agreements with Conoco Inc., Columbus Energy, and Jerome McHugh. RVD reviewed these settlements and determined that the settlements covered all the time periods when these companies were responsible for royalty payments on Jicarilla Tribal leases, therefore, RVD will not issue orders to these companies.

Conclusion

Our review of the major portion values calculated from data reported to MMS on the Form MMS-2014 and the data reported to the Jicarilla Tribe of the RIK purchase statements shows that they are reasonable prices paid for a major portion of like-quality production sold from the Jicarilla Reservation. The use of these major portion values

enforces the major portion price requirements found in the lease terms and upholds our trust responsibility to the Jicarilla Tribe.
RVD plans to send orders to 40 companies after the Jicarilla Tribe concurs with our major portion methodology.

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DRAFT - FOR REVIEW ONLY

June 18, 2004

METHODOLOGY FOR MAJOR PORTION AND DUAL ACCOUNTING ANALYSIS JICARILLA APACHE TRIBAL LEASES

Purpose

The purpose of this report is to provide a background and discuss the results of major portion and dual accounting analyses performed by the Royalty Valuation Division (RVD), Royalty Management Program (RMP), Minerals Management Service (MMS), concerning natural gas produced from Jicarilla Apache Tribal leases.

Background

On December 6, 1996, representatives of the Jicarilla Apache Tribe (Jicarilla Tribe) and MMS met to discuss the implementation of major portion pricing for the natural gas produced from the Jicarilla Reservation. From July 1, 1975, to June 30, 1995, the Jicarilla Tribe sold gas under royalty-in-kind (RIK) agreements. Until 1989, gas was bought by either the Northwest Pipeline Corporation (Northwest) or the El Paso Natural Gas Company (El Paso) under long-term contracts. In 1989, the Jicarilla Tribe entered into contract settlements with El Paso and Northwest, thus, allowing the companies to pay market prices rather than the Natural Gas Policy Act (NGPA) ceiling prices.

On May 28, 1997, representatives of the Jicarilla Tribe and MMS met in Dallas, Texas to discuss the methodology for the major portion and dual accounting analysis. MMS presented a proposal to the Jicarilla Tribe that MMS would issue orders to perform major portion based on NGPA based prices recieived by the Jicarilla Tribal RIK agreements for each applicable category of gas. The Jicarilla Tribe concurred with this approach. The Jicarilla Tribe also concurred that the orders should also include dual accounting.

On June 17, 1997, representatives of the Jicarilla Tribe and MMS met to review the contract settlements, sources of data, pricing data, and the major portion/dual accounting order to perform.

Regulatory Criteria

The oil and gas valuation regulations found at 30 CFR § 206 (1996), have long required that the "estimated reasonable value" of production be used for the purposes of computing royalties. Due consideration is given to the highest price paid for a part or for a major portion of gas of like quality in the same field, to the price received by the lessee, to posted prices, and to other relevant matters. Title 25 CFR § 211 (1996) and the terms of the Jicarilla leases also specify that the value may, at the discretion of the Secretary of the

Interior, be calculated on the basis of the highest price paid or offered at the time of production for the major portion of gas and/or natural gasoline and/or all other hydrocarbon substances produced and sold from the field where the leased lands are located.

The amended valuation regulations at 30 CFR §§ 206.172 and 206.173 (1996) address the issue of major portion for Indian lands. Specifically, the regulations provide:

> For any Indian leases which provide that the Secretary may consider the highest price paid or offered for a major portion of production (major portion) in determining value of production for royalty purposes, if data are available to compute a major portion MMS will, where practicable, compare the value determined in accordance with this section with the major portion. The value to be used in determining the value of production for royalty purposes shall be the higher of those two values.

For natural gas, these regulations specify that a major portion price is calculated for a like quality of gas in the same field (or, if necessary, to obtain a reasonable sample from the same area). Like-quality gas is gas of similar physical, chemical, and legal characteristics. Legal characteristics are generally the applicable NGPA category or subcategory.

The price associated with the volume that causes the cumulative volume, summed beginning with the volume associated with the highest price (lowest price beginning March 1, 1988) to exceed 50 percent plus 1 Mcf of the total sales volume is deemed to be the major portion price. Approximately two-thirds of the Jicarilla production was sold under the RIK program at established NGPA pricing or at a contract price based on NGPA pricing. The Jicarilla RIK volumes represented well over 60% of the total volumes and therefore the Jicarilla price was equated to the majority price.

Dual accounting requirements are specified by Indian lease terms, Federal regulations, and MMS instructions. Federal regulations at 25 CFR §§ 211.13 (1996) and 212.16 (1996) state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that <u>royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater</u> [Emphasis added.]

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.152 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.153 (1996). Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.

Major Portion Methodology

Under the agreement reached between the MMS and Jicarilla representatives, the major portion methodology will identify the prices paid under RIK contracts and settlement agreements and calculate the estimated major portion price by NGPA category for all gas production in the Jicarilla Reservation utilizing RIK data for the time period January 1984 through June 1995. The following key issues were agreed to by RVD and the Jicarilla Tribe at the December 6, 1997, and June 17, 1997, meetings:

- RVD will consider the Reservation as the "area" for calculating the major portion pricing.
- The price received for the RIK portion of the gas represents 1/8 royalty share. The RVD will extrapolate the 1/8 royalty share to the entire 8/8 production and assume value for the 1/8 royalty share is representative of the prices received for the other portion of the gas sold from the Reservation.[1]
- RVD will analyze a sample of Jicarilla settlement statements from Northwest and El Paso and certify that the Jicarilla Tribe received the proper NGPA prices.
- RVD will send orders to the payor who paid royalties in value only.

The NGPA Category

The major portion analysis covers from January 1984 through June 1995. Beginning with 1984, RVD identified gas values by NGPA category for periods prior to the 1989 RIK settlements. In the post-settlement period, RVD identified the settlement price by NGPA category. In the orders that RVD will send to the non-RIK payors, we will provide gas value by NGPA category and request that the payor identify the NGPA category of their gas, and time periods, and leases for which the company was a payor between January 1984 and June 1995.

The January 1984 through December 1986 and July 1988 through December 1988 prices are based on the NGPA prices plus tax reimbursements received by the Jicarilla Tribe and are shown by NGPA category by month. The NGPA categories identified include:

[1] Approximately 2/3 of the 1/8 royalty share was sold under RIK contracts.

102 New natural gas	103 New onshore production
104 Post - 1974 gas	104 1973-1974 Biennium gas
104 Replacement gas	104 Flowing gas
104 Rocky Mountain gas	105 Existing intrastate gas
108 Stripper gas	109 Other gas

The January 1987 through June 1988 major portion prices are based on a weighted average price received by the Jicarilla Apache resulting from a negotiated temporary price reduction between the Tribe and Northwest and El Paso. Starting in January 1989, the major portion prices are based on the prices received under the Jicarilla Apache RIK contract plus contract settlements and are shown by NGPA category by month.

RVD used the Auditing and Financial System (AFS) database to determine prices paid by those payors who paid in-value and to determine that the RIK prices represent the major portion price. The RVD will review the responses to the September 29, 1995, Dear Payor letter and will issue orders to dual account and pay royalties on major portion prices. For those companies who stated that they performed dual accounting, RVD compared prices paid by the payors who paid in-value to the calculated major portion prices to determine that orders should be issued. RVD will issue orders to those payors who paid in value (Attachment 1) requiring payments on the higher of gross proceeds prices or major portion prices for any under payments plus interest. The orders will require dual accounting based on the higher of these prices.

Definition of Field or Area

The majority of the Reservation is within Rio Arriba County, New Mexico, with a small portion extending into Sandoval County, New Mexico. The Reservation lies along the eastern edge of the San Juan Basin. Gas production is from the Pictured Cliffs Formation, Mesaverde Group, Gallup, Tocito, and fractured Mancos Formations, and the Dakota and Dakota-Morrison Formations. The Fruitland Formation produces methane primarily from coals (Fruitland Coal). 30 CFR 205 § 172 states major portion will be calculated on "like quality of gas in the same field (or, if necessary, to obtain a reasonable sample from the same area)." However, the State of New Mexico utilizes pool, rather than, field definitions. A pool is a "common source of supply" and is generally based on a geologic horizon. The State of New Mexico Oil and Gas Commission defines 30 pools that overly or are within the Jicarilla Reservation boundary. In several cases, several pools overly one another and/or extend well outside the Reservation boundary. Consequently, we are unable to define distinct field boundaries for Jicarilla gas production. Therefore, for this study, the Jicarilla Reservation boundary will be defined as the area. During the June 17, 1997, meeting between MMS and the Jicarilla Tribe, the Tribal representative agreed to use the Reservation boundary as the major portion area.

Calculation of Estimated Major Portion Values

The major portion calculation has been divided into four time periods :

- Period 1: January 1984 through December 1986, NGPA pricing was in effect for both El Paso and Northwest contracts.
- Period 2: El Paso negotiated a temporary price reduction from the NGPA prices for the January 1987 through June 1987. Northwest negotiated a temporary price reduction from the NGPA prices for the July 1987 through December 1988.
- Period 3: July 1988 through December 1988, NGPA pricing was in effect for both pipelines.
- Period 4: Northwest negotiated a buy out of their contract and El Paso negotiated a buy down of their contract.

The time periods and effective prices are shown in Table 1.

TABLE 1
Natural Gas Pricing Variations

Period	Time Period	El Paso Price	Northwest Price
1	1984-1986	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
2	January 1987 - June 1987	$2.50	NGPA & Tax Reimbursement
2	July 1987 - June 1988	NGPA & Tax Reimbursement	Contract Negotiated Price
3	July 1988 - December 1988	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
3	January 1989 - June 1989	NGPA & Tax Reimbursement; Contract Buy down 7/89	Contract Buy out - 2/89
4	July 1989 - December 1989	$1.227 + buy down	Buy out
4	1990	$1.276 + buy down	Buy out
4	1991	$1.327 + buy down	Buy out
4	1992	$1.380 + buy down	Buy out
4	1993	$1.435 + buy down	Buy out
4	1994	$1.493 + buy down	Buy out
4	1995	$1.553 + buy down	Buy out

Tax Reimbursement information was provided by the Jicarilla Tribal Tax manual and is shown in Table 2.

TABLE 2
Jicarilla Tax Rates

Date	Severance Tax (Per MMBtu)	Privilege Tax (100% less royalty value)
1/1/84 through 5/30/85	$0.05	
6/1/85 through 1/31/86	$0.05	5.00%
2/1/86 through 1/31/87	$0.05	5.18%
2/1/87 through 1/31/88	$0.05	5.28%
2/1/88 through 12/31/88	$0.05	5.47%

Major portion prices were determined by prices received under the Jicarilla RIK contract and are shown in Attachment 2.. For periods 1 and 3, the major portions prices were the sum of the published NGPA prices and the tax reimbursments. The prices received by the Tribe in Period 2 (the market out period) and Period 4 (the post-settlement period) are calculated as discussed below.

During the market out period (Period 2), January 1987 through June 1988, RVD calculated a weighted average price received for each NGPA category by multiplying the contract price times the Strata estimate reserve volumes for El Paso and Northwest and dividing the total value by the total Strata estimate volumes (Attachment 3).

After the Northwest and El Paso contract settlements, major portion prices were determined by adding the settlement proceeds by NGPA category to the actual prices received under the El Paso contract and the estimated buy out prices under the Northwest contract to determine the total consideration received under the RIK contract for each NGPA category. Strata Evaluation Associates, Inc. (Strata) **documents provided in support of the RIK contract settlements proceeds provided detailed information on the settlement monies received for NGPA categories. These amounts were used to determine the major portion prices by category.**

Strata calculated the amounts due the Jicarilla Tribe for contract settlements with El Paso and Northwest based on estimated reserves of the wells supplying El Paso and Northwest. The contract settlements were based on the difference between the projected NGPA prices due under the original contract and the price negotiated under the buy out or buy down contract. Based on the projected NGPA prices and volumetric analysis, Strata calculated an annual present value estimate of the remaining reserves for both El Paso and Northwest (Column B) as shown on Attachment 4. This value was then discounted using a 10% discount rate (Column C). This discounted settlement value was further reduced during negotiations between the Jicarilla Apache

Tribe and the pipeline companies. A discount factor (Column E) was calculated by dividing the actual settlement amount (Column C) by the Value of Estimated Reserves (Column B) . The estimated NGPA price was scheduled from the Strata report for each NGPA category (Example: Column G 102). A price differential (Column H) was calculated between the projected NGPA price (Column G) and the buy down/buy out price (Column F). This differential represents the undiscounted value that the Tribe would have received if the contract had not been bought out or bought down. The settled price differential (Column I) was calculated by multiplying the discount factor (Column E) times the price differential (Column H). This differential was then added to the buy down/buy out price to determine the major portion price (Column J) by category.

This procedure was used to calculate all NGPA pricing categories, except those NGPA prices that were less than the buy down/buy out price, for which the major portion prices were equated to the actual buy down/buy out price (Column X, Y).

RVD then calculated a weighted average price for the Northwest contract and the El Paso contract. This price was calculated by multiplying the price received for each NGPA category by the Strata reserve volume and dividing both calculated values by the total volume for El Paso and Northwest (Attachment 5).

The orders will cite the requirement that royalty be based on the higher of the major portion value or gross proceeds accruing to the lessee as well as the requirement to perform dual accounting. Sales by affiliates may provide information concerning gross proceeds to the lessee and the appropriate benchmark value in some situations and thus may be considered in determining royalty values.

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Dual accounting requirements are specified by Indian lease terms and Federal regulations found at 25 CFR § 211.13 (1996) which state:

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Dual accounting is defined as a valuation method that requires the lessee to compute royalties based on the greater of : (1) the value of the gas prior to processing (as determined under 30 CFR § 206.172 (1996)), or (2) the combined value of the residue gas and gas plant products resulting from processing the gas (as determined under 30 CFR § 206.173 (1996)), plus the value of any condensate recovered downstream of the point of royalty settlement without resorting to processing (30 CFR § 206.52(1996)). However, the value of production can never be less than the gross proceeds accruing to the lease (30 CFR §§ 206.172(h) and 206.173(h) (1996)) . After March 1, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR §§ 206.176 through 206.179 (1996)).

RVD reviewed comparable contracts for the sales of natural gas liquids (NGLP's). RVD found 2 contracts with sales in the San Juan Basin (Attach 7). Both these contracts called for Mt. Belview, Texas spot prices for NGLP's. RVD determined that the comparable contract price for NGLP's for the reservation was the average Mt. Belview, Texas spot market price. The orders will require the calculations for liquids be based on the higher of the gross proceeds price received for liquids or the average Mt. Belview spot market price.

Data Retrieval

During September 1996, AFS data as reported on Form MMS-2014, was extracted from the AFS database, processed and downloaded to a Microsoft Access table on the RVD Local Area Network. The criteria for extracting this data was: (1) all AFS data reported under Fund Code 550 (the fund code for the Jicarilla Reservation); (2) the product codes of 03 (residue gas) and 04 (unprocessed gas); and (3) the transaction codes of 01 (royalty) and 11 (transportation allowance).

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Once extracted from the AFS database, the information was processed by a program that removed adjustments to previously submitted information. This program first sorted the database by lease, product code, revenue source, selling arrangement, sales year, sales month, royalty quantity, and royalty value. The program then identified all negative (adjusted) royalty quantities and values and searched for a matching positive line. If a match was found, both the positive and negative lines were removed. Next, those negative lines without a matching positive (indicative of misreporting) were written to an error file and removed from further processing.

The next operation performed on the data was to determine major portion prices. We calculated MMBtu prices by adjusting for the quality of the gas.

A problem encountered in the data was that some records did not have a reported gas quality or bad a Btu content that was not within a reasonable range. Option included

removing those records, using the quality last reported for the lease, or assuming a quality. After analyzing this problem, we decided that given our manpower restrictions and obvious misreporting from the payors, the best option was to calculate a gas quality from the data available. We determined the 1996 average quality reported on the Form 3160 for all Jicarilla leases and calculated the range reported on all Jicarilla leases. We used the average Btu reported on the Form 3160 for each lease for all 04 lines submitted that did not report a quality or reported a quality outside of the average range. We used the average Btu reported on the MMS-2014 for all 03 lines submitted that did not report a quality or reported a quality outside of the average range.

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RVD downloaded all royalty payments for Fund Code 550 (Jicarilla Tribe). We then summarized the payments for 2/88 by payor. We added the total RIK volumes purchased by El Paso and Northwest for 2/88 and determined the total sales for the reservation. RVD then divided total RIK sales by the total sales for the reservation to determine the percentage of reservation gas which was sold as RIK. Our review indicated that 66% of the royalty production on the reservation was sold as RIK therefore, the major portion prices were always the equivalent of the RIK prices (Attachment 6).

Global Settlements

The Jicarilla Tribe has entered global settlement agreements with Conoco Inc., Columbus Energy, and Jerome McHugh. RVD reviewed these settlements and determined that the settlements covered all the time periods when these companies were responsible for royalty payments on Jicarilla Tribal leases, therefore, RVD will not issue orders to these companies.

Conclusion

Our review of the major portion values calculated from data reported to MMS on the Form MMS-2014 and the data reported to the Jicarilla Tribe on the RIK purchase statements shows that they are reasonable prices paid for a major portion of like-quality production sold from the Jicarilla Reservation. The use of these major portion values enforces the major portion price requirements found in the lease terms and upholds our trust responsibility to the Jicarilla Tribe.

RVD plans to send orders to 40 companies after the Jicarilla Tribe concurs with our major portion methodology.

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DRAFT - FOR REVIEW ONLY

November 7, 1997

METHODOLOGY FOR MAJOR PORTION AND DUAL ACCOUNTING ANALYSIS JICARILLA APACHE TRIBAL LEASES

Purpose

The purpose of this report is to provide a background and to discuss the results of major portion and dual accounting analyses recently undertaken by the Royalty Valuation Division (RVD), Royalty Management Program (RMP), Minerals Management Service (MMS), for natural gas produced from Jicarilla Apache Tribal leases.

Background

On December 6, 1996, representatives of the Jicarilla Apache Indian Tribe (Jicarilla Tribe) and MMS met to discuss the implementation of major portion pricing for the natural gas produced from the Jicarilla Reservation. From July 1, 1975, to June 30, 1995, the Jicarilla Tribe sold gas under royalty-in-kind (RIK) agreements. Until 1989, gas was bought by either the Northwest Pipeline Corporation (Northwest) or the El Paso Natural Gas Company (El Paso) under long-term contracts. In 1989, the Jicarilla Tribe entered into contract settlements with El Paso and Northwest, thus, allowing the companies to pay market prices rather than the Natural Gas Policy Act (NGPA) ceiling prices.

On May 28, 1997, representatives of the Jicarilla Tribe and MMS met in Dallas, Texas to discuss the implementation of the major portion and dual accounting analysis. MMS presented a proposal to the Jicarilla Tribe that MMS would issue orders to perform major portion based on Jicarilla Tribal RIK prices for each NGPA category. The Jicarilla Tribe concurred with this approach. The Jicarilla Tribe also concurred that the orders should also include dual accounting.

On June 17, 1997 and October 8, 1997, representatives of the Jicarilla Tribe and MMS met to review the contract settlements, sources of data, pricing data, and the major portion/dual accounting order to perform.

Regulatory Criteria

The oil and gas valuation regulations found at 30 CFR § 206 (1987), have long required that the "estimated reasonable value" of production be used for the purposes of computing royalties. Due consideration is given to the highest price paid for a part or for a major portion of gas of like quality in the same field, to the price received by the lessee, to posted prices, and to other relevant matters. Title 25 CFR § 211 (Indian tribal) and the terms of the Jicarilla leases also specify that the value may, at the discretion of the Secretary of the

Interior, be calculated on the basis of the highest price paid or offered at the time of production for the major portion of gas and/or natural gasoline and/or all other hydrocarbon substances produced and sold from the field where the leased lands are located.

The amended valuation regulations at 30 CFR §§ 206.172(a)(3)(I) and 206.173(a)(3)(I) (1996) address the issue of major portion for Indian lands. Specifically, the regulations provide:

> For any Indian leases which provide that the Secretary may consider the highest price paid or offered for a major portion of production (major portion) in determining value of production for royalty purposes, if data are available to compute a major portion MMS will, where practicable, compare the value determined in accordance with this section with the major portion. The value to be used in determining the value of production for royalty purposes shall be the higher of those two values.

For natural gas, these regulations specify that a major portion price is calculated for a like quality of gas in the same field (or, if necessary, to obtain a reasonable sample from the same area). Like-quality gas is gas of similar physical, chemical, and legal characteristics. Legal characteristics are generally the applicable NGPA category or subcategory.

The price associated with the volume that causes the cumulative volume, summed beginning with the volume associated with the highest price (lowest price beginning March 1, 1988) to exceed 50 percent plus 1 Mcf of the total sales volume is deemed to be the major portion price. Approximately two-thirds of the *Jicarilla production* was sold under the RIK contracts.

Dual accounting requirements are specified by Indian lease terms, regulations, and MMS instructions. The regulations at 25 CFR §§ 211.13 (1996) and 212.16 (1996) state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that <u>royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater</u> [Emphasis added.]

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.152 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.153 (1996). Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.

Major Portion Methodology

Under the agreement reached between the MMS and Jicarilla representatives, the major portion methodology will identify the prices paid under RIK contracts and RIK settlement agreements and calculate the major portion by NGPA category for all gas production in the Jicarilla Apache Reservation utilizing RIK data for the time period January 1984 through June 1995. The following key issues were agreed to by RVD and the Jicarilla Tribe at the December 6, 1996 and June 17, 1997 meetings:

- RVD will consider the Reservation as the "area" for calculating the major portion pricing.
- The price received for the RIK portion of the gas represents 1/8 royalty share. RVD will extrapolate the 1/8 royalty share to the entire 8/8 sales volume and assume the value for the 1/8 royalty share is representative of the prices received for the other portion of the gas sold from the Reservation.[1]
- RVD will analyze samples of Jicarilla settlement statements from Northwest and El Paso and certify that the Jicarilla Tribe received the proper NGPA prices.
- RVD will send orders to the non-RIK payors only.

The NGPA Category

The major portion analysis covers from January 1984 through June 1995. Beginning with January 1984, RVD identified gas values by NGPA category for periods prior to the 1989 settlements. In the post-settlement period, RVD identified the settlement price by NGPA category. In the orders that RVD will send to the non-RIK payors, we will provide major portion prices by NGPA category and request that the payor identify the NGPA category of their gas, time periods, and lease for which the company was a payor between January 1984 and June 1995.

The January 1984 through December 1986 and July 1988 through December 1988 major portion prices are based on the NGPA prices plus tax reimbursements received by the Jicarilla Tribe and

[1]Approximately 2/3 of the 1/8 royalty share was sold under RIK contracts.

are shown by in Attachment __NGPA category by month and year. The NGPA categories identified include:

102 New natural gas	103 New onshore production
104 Post - 1974 gas	104 1973-1974 Biennium gas
104 Replacement gas	104 Flowing gas
104 Rocky Mountain gas	105 Existing intrastate gas
108 Stripper gas	109 Other gas

The January 1987 through June 1988 major portion prices are based on a weighted average price received by the Jicarilla Tribe resulting from a negotiated temporary price reduction between the Jicarilla Tribe and Northwest and El Paso. Starting in January 1989, the major portion prices are based on the prices received under the Jicarilla RIK contract plus contract settlements and are shown by NGPA category by month and year.

RVD used the Auditing and Financial System (AFS) database to determine prices paid by those payors who paid in-value and to further support that the RIK prices represent the major portion price (Attachment ___).

Definition of Field or Area

The majority of the Reservation is within Rio Arriba County, New Mexico, with a small portion extending into Sandoval County, New Mexico. The Reservation lies along the eastern edge of the San Juan Basin. Gas production is from the Pictured Cliffs Formation, Mesaverde Group, Gallup, Tocito, and fractured Mancos Formations, and the Dakota and Dakota-Morrison Formations. The Fruitland Formation produces methane primarily from coals (Fruitland Coal). The regulations at 30 CFR 206 §§ 172(a)(3)(ii) and 173(a)(3)(ii) state that major portion will be calculated on "like quality of gas in the same field (or, if necessary, to obtain a reasonable sample from the same area)." However, the State of New Mexico utilizes pool, rather than, field definitions. A pool is a "common source of supply" and is generally based on a geologic horizon. The State of New Mexico Oil and Gas Commission defines 30 pools that overly or are within the Jicarilla Reservation boundary. In several cases, several pools overly one another and/or extend well outside the Reservation boundary. Consequently, we are unable to define distinct field boundaries for Jicarilla gas production. Therefore, for this study, the Jicarilla Reservation boundary will be defined as the area. During the June 17, 1997 meeting between MMS and the Jicarilla Tribe, the Tribal representative agreed to use the Reservation boundary as the major portion area.

Data Retrieval

During September 1996, AFS data as reported on The Report of Sales and Royalty Remittance (Form MMS-2014), was extracted from the AFS database, processed and

downloaded to a Microsoft Access table on the RVD Local Area Network. The criteria for extracting this data were: (1) all AFS data reported under Fund Code 550 (the fund code for the Jicarilla Reservation); (2) the product codes of 03 (residue gas) and 04 (unprocessed gas); and (3) the transaction codes of 01 (royalty) and 11 (transportation allowance).

Data Processing

Once extracted from the AFS database, the information was processed by a program that removed adjustments to previously submitted information. This program first sorted the database by lease, product code, revenue source, selling arrangement, sales year, sales month, royalty quantity, and royalty value. The program then identified all negative (adjusted) royalty quantities and values and searched for a matching positive line. If a match was found, both the positive and negative lines were removed. Next, those negative lines without a matching positive (indicative of misreporting) were written to an error file and removed from further processing.

The next operation performed on the data was to determine major portion prices. We calculated $/MMBtu prices by adjusting for the quality of the gas.

A problem encountered in the data was that some records did not have a reported gas quality or bad a Btu content that was not within a reasonable range. Options included removing those records, using the quality last reported for the lease, or assuming a quality. After analyzing this problem, we decided that given our manpower restrictions and obvious misreporting from the payors, the best option was to calculate a gas quality from the data available. We determined the 1996 average quality reported on the Monthly Report of Operations (Form MMS 3160) for all Jicarilla leases and calculated the range reported on all Jicarilla leases. We used the average Btu reported on the Form MMS 3160 for each lease for all 04 lines submitted that did not report a quality or reported a quality outside of the average range. We used the average Btu reported on the Form MMS-2014 for all 03 lines submitted that did not report a quality or reported a quality outside of the average range.

Major Portion AFS Analysis

Upon completion of processing, the database for the Jicarilla Reservation contained 47,463 records. In addition, MMS did not require the purchaser's of RIK production to report those sales on the Form MMS-2014, so RVD manually added the RIK sales data to the major portion calculation. MMS extracted AFS database lines for each month and arrayed lines by $/MMBtu from the highest price to lowest price. RVD then determined the amount of RIK production sold from the Jicarilla purchase statements by month and determined an average $/MMBtu price. RVD calculated that price at which 50 percent (by volume) plus 1 MMBtu of the gas (starting from the bottom) is sold.

RVD downloaded all royalty payments for Fund Code 550 (Jicarilla Tribe). We then summarized the payments for February 1988 by payor. We added the total RIK volumes purchased by El Paso and Northwest for February 1988 and determined the total sales for the Reservation. RVD then divided total RIK sales by the total sales for the reservation to determine the percentage of Reservation gas which was sold as RIK. Our review indicated that 66 percent of the royalty production on the Reservation was sold as RIK. Therefore, RVD concluded that the major portion price based on RIK data represent approximately 66 percent of the sales volume when compared to the sales volume reported by in-value payors on Form MMS 2014. (Attachment 5).

Calculation of Major Portion Values

The major portion calculation has been divided into four time periods :

- Period 1: NGPA pricing was in effect for both El Paso and Northwest contracts (January 1984 through December 1986.)
- Period 2: El Paso negotiated a temporary price reduction from the NGPA prices for the January 1987 through June 1987. Northwest negotiated a temporary price reduction from the NGPA prices for the July 1987 through December 1988 period.
- Period 3: NGPA pricing was in effect for both contracts.
- Period 4: Northwest negotiated a buy out of their contract and El Paso negotiated a buy down of their contract.

The time periods and effective prices are shown in Table 1. Tax Reimbursement information was obtained from the Jicarilla Tribal Tax manual and is shown in Table 2.

Major portion prices were determined by prices received under the Jicarilla RIK contract and are shown in Attachment 1. For periods 1 and 3, the major portions prices were the sum of the published NGPA prices and the tax reimbursments. The prices received by the Tribe in Period 2 (the market out period) and Period 4 (the post-settlement period) are calculated as discussed below.

During the market out period (Period 2), January 1987 through June 1988, RVD calculated a weighted average price received for each NGPA category by multiplying the contract price times the Strata Evaluation Associates, Inc. (Strata)[2] reserve volume estimate and dividing the total El Paso and Northwest value for by the total Strata volume estimate(Attachment 3).

After the Northwest and El Paso contract settlements, major portion prices were determined

[2] Strata Evaluation Associates, Inc., Parker, Colorado performed an evaluation of the producing capacity of all wells that contributed to the Northwest or El Paso systems as of July 1, 1989

by allocating the El Paso and Northwest settlement proceeds by NGPA category to the actual prices received under the El Paso settlement agreement to determine the total consideration received under the RIK contract for each NGPA category. Documents provided in support of the RIK contract settlements proceeds provided detailed information on the settlement monies received for each NGPA categories. These amounts were used to determine the major portion prices by category.

Strata calculated the amounts due the Jicarilla Tribe for contract settlements with El Paso and Northwest based on volumetric decline curve analysis of the estimated reserves of the wells

TABLE 1
Natural Gas Pricing Variations

Period	Time Period	El Paso Price	Northwest Price
1	January 1984 - December 1986	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
2	January 1987 - June 1987	$2.50	NGPA & Tax Reimbursement
2	July 1987 - June 1988	NGPA & Tax Reimbursement	Contract Negotiated Price
3	July 1988 - December 1988	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
3	January 1989 - June 1989	NGPA & Tax Reimbursement; Contract Buy down 7/89	Contract Buy out - 2/89
4	July 1989 - December 1989	$1.227 + buy down	Buy out
4	1990	$1.276 + buy down	Buy out
4	1991	$1.327 + buy down	Buy out
4	1992	$1.380 + buy down	Buy out
4	1993	$1.435 + buy down	Buy out
4	1994	$1.493 + buy down	Buy out
4	1995	$1.553 + buy down	Buy out

TABLE 2
Jicarilla Tax Rates

Date	Severance Tax (Per MMBtu)	Privilege Tax (87.5% of Value)
1/1/84 through 5/30/85	$0.05	
6/1/85 through 1/31/86	$0.05	5.00%

2/1/86 through 1/31/87	\$0.05	5.18%
2/1/87 through 1/31/88	\$0.05	5.28%
2/1/88 through 12/31/88	\$0.05	5.47%

supplying El Paso and Northwest. The contract settlements were based on the difference between the projected NGPA prices due under the original contract and the price negotiated under the buy out or buy down contract. Based on the projected NGPA prices and volumetric analysis, Strata calculated an annual present value estimate of the remaining reserves for both El Paso and Northwest (Column B) as shown on Attachment 1. This value was then discounted using a 10% discount rate (Column C). This settlement value was further reduced during negotiations between the Jicarilla Tribe and the companies (Column D). A settlement factor was calculated by dividing the total actual settlement amount by the Strata estimated settlement. For El Paso this was about 87% and for Northwest this was about 70%. This factor was then applied to the discounted amounts to determine a total annual settlement value (Column D). The annual settlement value was then divided by the annual present value estimate to generate a settlement discount factor (Column E). A price differential (Column H) was calculated between the projected NGPA price (Column G) and the buy down/buy out price (Column F). This differential represents the undiscounted value that the Tribe would have received if the contract had not been bought-out or bought-down. The undiscounted value was then discounted using the settlement discount factor discussed above to generate a settled price differential (column I). This differential was then added to the buy-down/buy-out price to determine the major portion price (Column J) by category.

This procedure was used to calculate all NGPA pricing categories, except those NGPA prices that were less than the buy-down/buy-out price, for which the major portion prices were equated to the actual buy-down/buy-out price (columns L, M).

RVD then calculated a weighted average price. This price was calculated by multiplying the appropriate El Paso and Northwest price received for each NGPA category by Strata reserve volume for El Paso and Northwest and dividing both calculated values by the total volume for El Paso and Northwest (Attachment 2).

The orders will cite the requirement that royalty be based on the higher of the major portion value or gross proceeds accruing to the lessee as well as the requirement to perform dual accounting. Sales by affiliates may provide information concerning gross proceeds to the lessee and the appropriate benchmark value in some situations and thus may be considered in determining royalty values.

<u>Dual Accounting Calculation</u>

Dual accounting requirements are specified by Indian lease terms and regulations found at 25

CFR § 211.13 (a) (1996) which state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that requires the lessee to compute royalties based on the greater of: (1) the value of the gas prior to processing (as determined under 30 CFR § 206.172 (1996)), or (2) the combined value of the residue gas and gas plant products resulting from processing the gas (as determined under 30 CFR § 206.173 (1996)), plus the value of any condensate recovered downstream of the point of royalty settlement without resorting to processing (30 CFR § 206.52 (1996)). However, the value of production can never be less than the gross proceeds accruing to the lease (30 CFR §§ 206.172(h) and 206.173(h) (1996)). After March 1, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR §§ 206.176 through 206.179 (1996)).

RVD will review the responses to the September 29, 1995, Dear Payor letter and will issue orders to dual account and pay royalties on major portion prices. For those companies who stated that they performed dual accounting, RVD compared prices paid by the payors who paid in-value to the calculated major portion prices to determine that orders should be issued. RVD will issue orders to those payors who paid in value (Attachment 4) requiring payments on the higher of gross proceeds prices or major portion prices for any under payments plus interest. The orders will require dual accounting based on the higher of these prices.

RVD reviewed comparable contracts for the sales of natural gas liquids (NGLs). RVD found two contracts[3] with sales in the San Juan Basin. Both these contracts called for Mt. Belvieu, Texas spot prices for NGLs. RVD determined that the comparable contract price for NGLP's for the reservation was the average Mt. Belvieu spot market prices. The orders will require the calculations for liquids be based on the higher of the gross proceeds received for liquids or the average Mt. Belvieu spot market price.

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[3] Jerome P. McHugh and _______, ___, 19__; Richardson Operating Company and Conoco Inc., July 1993

Global Settlements

The Jicarilla Tribe has entered global settlement agreements with Conoco Inc., Columbus Energy, and Jerome McHugh. RVD reviewed these settlements and determined that the settlements covered all the time periods when these companies were responsible for royalty payments on Jicarilla Tribal leases, therefore, RVD will not issue orders for major portion and dual accounting to these companies.

Conclusion

Our review of the major portion values calculated from data reported to MMS on the Form MMS-2014 and the data reported to the Jicarilla Tribe of the RIK purchase statements shows that they are reasonable prices paid for a major portion of like-quality production sold from the Reservation. The use of these major portion values enforces the major portion price requirements found in the lease terms and upholds our trust responsibility to the Jicarilla Tribe.

RVD plans to send orders to 40 companies after the Jicarilla Tribe concurs with our major portion methodology.

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June 18, 2004 (8:33AM)

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November 12, 1997

METHODOLOGY FOR MAJOR PORTION AND DUAL ACCOUNTING ANALYSIS JICARILLA APACHE TRIBAL LEASES

Purpose

The purpose of this report is to provide a background and to discuss the results of major portion and dual accounting analyses recently undertaken by the Royalty Valuation Division (RVD), Royalty Management Program (RMP), Minerals Management Service (MMS), for natural gas produced from Jicarilla Apache Tribal leases.

Background

On December 6, 1996, representatives of the Jicarilla Apache Indian Tribe (Jicarilla Tribe) and MMS met to discuss the implementation of major portion pricing for the natural gas produced from the Jicarilla Reservation (Reservation). From July 1, 1975, to June 30, 1995, the Jicarilla Tribe sold gas under royalty-in-kind (RIK) agreements. Until 1989, gas was bought by either the Northwest Pipeline Corporation (Northwest) or the El Paso Natural Gas Company (El Paso) under long-term contracts. In 1989, the Jicarilla Tribe entered into contract settlements with El Paso and Northwest, thus, allowing the companies to pay market prices rather than the Natural Gas Policy Act (NGPA) ceiling prices.

On May 28, 1997, representatives of the Jicarilla Tribe and MMS met in Dallas, Texas to discuss the implementation of the major portion and dual accounting analyses. MMS presented a proposal to the Jicarilla Tribe that recommended MMS would issue orders to perform major portion based on Jicarilla Tribal RIK prices for each NGPA category. The Jicarilla Tribe concurred with this approach. The Jicarilla Tribe also concurred that the orders should also include dual accounting.

On June 17, 1997, and October 8, 1997, representatives of the Jicarilla Tribe and MMS met to review the contract settlements, sources of data, pricing data, and the major portion/dual accounting order to perform.

Regulatory Criteria

The oil and gas valuation regulations found at 30 CFR § 206 (1987), have long required that the "estimated reasonable value" of production be used for the purposes of computing royalties. Due consideration is given to the highest price paid for a part or for a major portion of gas of like quality in the same field, to the price received by the lessee, to posted prices, and to other relevant matters. Title 25 CFR § 211 (Indian tribal) and the terms of the Jicarilla Tribal leases also specify that the value may, at the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered at the time of production for the major portion of gas and/or natural gasoline and/or all other hydrocarbon substances produced and sold from the field where the leased lands are located.

The amended valuation regulations at 30 CFR §§ 206.172(a)(3)(i) and 206.173(a)(3)(i) (1996) address the issue of major portion for Indian lands. Specifically, the regulations provide:

> For any Indian leases which provide that the Secretary may consider the highest price paid or offered for a major portion of production (major portion) in determining value of production for royalty purposes, if data are available to compute a major portion MMS will, where practicable, compare the value determined in accordance with this section with the major portion. The value to be used in determining the value of production for royalty purposes shall be the higher of those two values.

For natural gas, these regulations specify that a major portion price is calculated for like-quality gas in the same field (or, if necessary, to obtain a reasonable sample from the same area). Like-quality gas is gas of similar physical, chemical, and legal characteristics. Legal characteristics are generally the applicable NGPA category or subcategory.

Dual accounting requirements are specified by Indian lease terms, regulations, and MMS instructions. The regulations at 25 CFR §§ 211.13 (1996) and 212.16 (1996) state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.152 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.153 (1996). Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.

Major Portion Methodology

Under the agreement reached between the MMS and Jicarilla representatives, the major portion methodology will identify the prices paid under RIK contracts and RIK settlement agreements and calculate the major portion by NGPA category for all gas production in the Jicarilla Apache Reservation utilizing RIK data for the time period January 1984 through June 1995. The following key issues were agreed to by RVD and the Jicarilla Tribe at the December 6, 1996, and June 17, 1997, meetings:

- RVD will consider the Reservation as the "area" for calculating the major portion pricing.
- The price received for the RIK portion of the gas represents 1/8 royalty share. RVD will extrapolate the 1/8 royalty share to the entire 8/8 sales volume and assume the value for the 1/8 royalty share is representative of the prices received for the other portion of the gas sold from the Reservation.[1]
- RVD will analyze samples of Jicarilla settlement statements from Northwest and El Paso and certify that the Jicarilla Tribe received the proper NGPA prices.
- RVD will send orders to the non-RIK payors only.

The NGPA Category

The major portion analysis covers the period from January 1984 through June 1995. Beginning with January 1984, RVD identified gas values by NGPA category for periods prior to the 1989 settlements. In the post-settlement period, RVD identified the settlement price by NGPA category. In the orders that RVD will send to the non-RIK payors, we will provide major portion prices by NGPA category and request that the payor identify the NGPA category of their gas, the time periods, and the lease(s) for which the company was a payor between January 1984 and June 1995.

The January 1984 through December 1986 and July 1988 through December 1988 major portion prices are based on the NGPA prices plus tax reimbursements received by the Jicarilla Tribe and are shown by in Attachment 1 by NGPA category for each month/year. The NGPA categories identified include:

[1]Approximately 2/3 of the 1/8 royalty share was sold under RIK contracts.

102 New natural gas	103 New onshore production
104 Post - 1974 gas	104 1973-1974 Biennium gas
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108 Stripper gas	109 Other gas

The January 1987 through June 1988 major portion prices are based on a weighted average price received by the Jicarilla Tribe resulting from a negotiated temporary price reduction between the Jicarilla Tribe and Northwest and El Paso. Starting in January 1989, the major portion prices are based on the prices received under the Jicarilla RIK contract plus contract settlements and are shown by NGPA category for each month/year.

RVD used the Auditing and Financial System (AFS) database to determine prices paid by those payors who paid in-value and to further support that the RIK prices represent the major portion price (Attachment2).

Definition of Field or Area

The majority of the Reservation is within Rio Arriba County, New Mexico, with a small portion extending into Sandoval County, New Mexico. The Reservation lies along the eastern edge of the San Juan Basin. Gas production is from the Pictured Cliffs Formation, Mesaverde Group, Gallup, Tocito, and fractured Mancos Formations, and the Dakota and Dakota-Morrison Formations. The Fruitland Formation produces methane primarily from coals (Fruitland Coal). The regulations at 30 CFR §§ 206 172(a)(3)(ii) and 173(a)(3)(ii) state that major portion will be calculated on "like quality of gas in the same field (or, if necessary, to obtain a reasonable sample from the same area)." However, the State of New Mexico utilizes pools, rather than, field definitions. A pool is a "common source of supply" and is generally based on a geologic horizon. The State of New Mexico Oil and Gas Commission defines 30 pools that overly or are within the Reservation boundary. In several cases, several pools overly one another and/or extend well outside the Reservation boundary. Consequently, we are unable to define distinct field boundaries for Jicarilla gas production. Therefore, for this study, the Reservation boundary will be defined as the area. During the June 17, 1997, meeting between MMS and the Jicarilla Tribe, the Tribal representative agreed to use the Reservation boundary as the major portion area.

Data Retrieval

During September 1996, AFS data as reported on the Report of Sales and Royalty Remittance (Form MMS-2014), was extracted from the AFS database, processed and downloaded to a Microsoft Access table on the RVD Local Area Network. The criteria for extracting this data were: (1) all AFS data reported under Fund Code 550 (the fund code for the Reservation); (2) the product codes 03 (residue gas) and 04 (unprocessed gas); and (3) the transaction codes 01 (royalty) and 11 (transportation allowance).

Data Processing

Once extracted from the AFS database, the information was processed by a program that removed adjustments to previously submitted information. This program first sorted the database by lease, product code, revenue source, selling arrangement, sales year, sales month, royalty quantity, and royalty value. The program then identified all negative (adjusted) royalty quantities and values and searched for a matching positive line. If a match was found, both the positive and negative lines were removed. Next, those negative lines without a matching positive (indicative of misreporting) were written to an error file and removed from further processing.

The next operation performed on the data was to determine major portion prices. We calculated $/MMBtu prices by adjusting for the quality of the gas.

A problem encountered in the data was that some records did not have a reported gas quality or an incorrect Btu content that was not within a reasonable range. Options included removing those records, using the quality last reported for the lease, or assuming a quality. After analyzing this problem, we decided that given our limited resources, the best option was to calculate a gas quality from the data available. We determined the 1996 average quality reported on the Monthly Report of Operations (Form MMS 3160) for all Jicarilla leases and calculated the range reported on all Jicarilla leases. We used the average Btu reported on the Form MMS 3160 for each lease for all 04 lines submitted that did not report a quality or reported a quality outside of the average range. We used the average Btu reported on the Form MMS-2014 for all 03 lines submitted that did not report a quality or reported a quality outside of the average range.

AFS Analysis of Major Portion

Upon completion of processing, the database for the Reservation contained 47,463 records. In addition, MMS did not require the purchaser's of RIK production to report those sales on the Form MMS-2014. In an effort to verify that the RIK data is the major portion price RVD created an off-line MMS-2014 and manually added the RIK sales data to the price array for February 1988. MMS extracted AFS database lines February 1988 and arrayed lines by $/Mcf from the highest price to lowest price. RVD then determined the amount of RIK production sold from the Jicarilla purchase statements by month and determined an average $/Mcf price. RVD calculated that price at which 50 percent (by volume) plus 1 Mcf of the gas (starting from the bottom) is sold (Attachment 6).

RVD downloaded all royalty payments for Fund Code 550 (Jicarilla Tribe). We then summarized the payments for February 1988 by payor. Using data from settlement statements, we added the total RIK volumes purchased by El Paso and Northwest for February 1988 and determined the total sales for the Reservation. RVD then divided total

RIK sales by the total sales for the reservation to determine the percentage of Reservation gas which was sold as RIK. Our review indicated that for February 1988 sales month, 66 percent of the royalty production on the Reservation was sold as RIK, therefore, RVD concluded that the major portion price based on RIK data represents approximately 66 percent of the sales volume for February 1988 sales month, when compared to the sales volume reported by in-value payors on Form MMS 2014. (Attachment 5).

Calculation of Major Portion Values

The major portion calculation has been divided into four time periods :

- Period 1: NGPA pricing was in effect for both El Paso and Northwest contracts (January 1984 through December 1986.)
- Period 2: El Paso negotiated a temporary price reduction from the NGPA prices for the January 1987 through June 1987. Northwest negotiated a temporary price reduction from the NGPA prices for the July 1987 through December 1988 period.
- Period 3: NGPA pricing was in effect for both contracts.
- Period 4: Northwest negotiated a buy out of their contract and El Paso negotiated a buy down of their contract.

The time periods and effective prices are shown in Table 1. Tax reimbursement information was obtained from the Jicarilla Tribal Tax manual and is shown in Table 2.

Major portion prices were determined by prices received under the Jicarilla RIK contracts and are shown in Attachment 1. For periods 1 and 3, the major portions prices were the sum of the published NGPA prices and the tax reimbursments. The prices received by the Jicarilla Tribe in Period 2 (the market-out period) and Period 4 (the post-settlement period) are calculated as discussed below.

During the market-out period (Period 2), January 1987 through June 1988, RVD calculated a weighted-average price received for each NGPA category by multiplying the contract price times the Strata Evaluation Associates, Inc. (Strata)[2] reserve volume estimate and dividing the total El Paso and Northwest value by the total Strata volume estimate (Attachment 3).

After the Northwest and El Paso contract settlements, major portion prices were determined by allocating the El Paso and Northwest settlement proceeds by NGPA category to the actual prices received under the El Paso settlement agreement to determine the total consideration

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[2] Strata Evaluation Associates, Inc., Parker, Colorado performed an evaluation of the producing capacity of all wells that contributed to the Northwest or El Paso systems as of July 1, 1989

received under the RIK contract for each NGPA category. Documents provided in support of the RIK contract settlements proceeds provided detailed information on the settlement monies received for each NGPA categories. These amounts were used to determine the major portion prices by category.

Strata calculated the amounts due the Jicarilla Tribe for contract settlements with El Paso and Northwest based on volumetric decline curve analysis of the estimated reserves of the wells.

TABLE 1
Natural Gas Pricing Variations

Period	Time Period	El Paso Price	Northwest Price
1	January 1984 - December 1986	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
2	January 1987 - June 1987	$2.50	NGPA & Tax Reimbursement
2	July 1987 - June 1988	NGPA & Tax Reimbursement	Contract Negotiated Price
3	July 1988 - December 1988	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
3	January 1989 - June 1989	NGPA & Tax Reimbursement; Contract Buy down 7/89	Contract Buy out - 2/89
4	July 1989 - December 1989	$1.227 + buy down	Buy out
4	1990	$1.276 + buy down	Buy out
4	1991	$1.327 + buy down	Buy out
4	1992	$1.380 + buy down	Buy out
4	1993	$1.435 + buy down	Buy out
4	1994	$1.493 + buy down	Buy out
4	1995	$1.553 + buy down	Buy out

TABLE 2
Jicarilla Tax Rates

Date	Severance Tax (Per MMBtu)	Privilege Tax (87.5% of Value)
1/1/84 through 5/30/85	$0.05	
6/1/85 through 1/31/86	$0.05	5.00%
2/1/86 through 1/31/87	$0.05	5.18%

2/1/87 through 1/31/88	$0.05	5.28%
2/1/88 through 12/31/88	$0.05	5.47%

supplying El Paso and Northwest. The contract settlements were based on the difference between the projected NGPA prices due under the original contract and the price negotiated under the buy out or buy down contract. Based on the projected NGPA prices and volumetric analysis, Strata calculated an annual present value estimate of the remaining reserves for both El Paso and Northwest (Column B) as shown on Attachment 2. This value was then discounted using a 10% discount rate (Column C). This settlement value was further reduced during negotiations between the Jicarilla Tribe and the companies (Column D). A settlement factor was calculated by dividing the total actual settlement amount by the Strata estimated settlement. For El Paso this was about 87% and for Northwest this was about 70%. This factor was then applied to the discounted amounts to determine a total annual settlement value (Column D). The annual settlement value was then divided by the annual present value estimate to generate a settlement discount factor (Column E). A price differential (Column H) was calculated between the projected NGPA price (Column G) and the buy down/buy out price (Column F). This differential represents the undiscounted value that the Tribe would have received if the contract had not been bought-out or bought-down. The undiscounted value was then discounted using the settlement discount factor discussed above to generate a settled price differential (column I). This differential was then added to the buy-down/buy-out price to determine the major portion price (Column J) by category.

The above procedure was used to calculate all NGPA pricing categories, except those NGPA prices that were less than the buy-down/buy-out price, for which the major portion prices were equated to the actual buy-down/buy-out price (Columns L, M).

RVD then calculated a weighted-average price. This price was calculated by multiplying the appropriate El Paso and Northwest price received for each NGPA category by Strata reserve volume for El Paso and Northwest and dividing both calculated values by the total volume for El Paso and Northwest (Attachment 2).

The orders will cite the requirement that royalty be based on the higher of the major portion value or gross proceeds accruing to the lessee as well as the requirement to perform dual accounting. Sales by affiliates may provide information concerning gross proceeds to the lessee and the appropriate benchmark value and thus may be considered in determining royalty values.

Dual Accounting Calculation

Dual accounting requirements are specified by Indian lease terms and regulations found at 25 CFR § 211.13 (a) (1996) which state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that requires the lessee to compute royalties based on the greater of: (1) the value of the gas prior to processing (as determined under 30 CFR § 206.172 (1996)), or (2) the combined value of the residue gas and gas plant products resulting from processing the gas (as determined under 30 CFR § 206.173 (1996)), plus the value of any condensate recovered downstream of the point of royalty settlement without resorting to processing (30 CFR § 206.52 (1996)). However, the value of production can never be less than the gross proceeds accruing to the lease (30 CFR §§ 206.172(h) and 206.173(h) (1996)). After March 1, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR §§ 206.176 through 206.179 (1996)).

RVD will review the responses to the September 29, 1995, Dear Payor letter and will issue orders to perform dual accounting and pay royalties on major portion prices. For those companies who stated that they performed dual accounting, RVD compared prices paid by the payors who paid in-value to the calculated major portion prices to determine whether orders should be issued. RVD will issue orders to those payors who paid in value (Attachment 7) requiring payments on the higher of gross proceeds or major portion prices for any under payments plus interest. The orders will require dual accounting based on the higher of gross proceeds or major portion prices.

RVD reviewed comparable contracts for the sales of natural gas liquids (NGLs). RVD obtained two contracts[3] with sales in the San Juan Basin. Both these contracts called for Mt. Belvieu, Texas, spot prices for NGL's. RVD determined that the comparable contract price for NGL's for the Reservation was the average Mt. Belvieu spot market price. The orders will require the calculations for liquids to be based on the higher of the gross proceeds received for liquids or the average Mt. Belvieu spot market price (Attachment 4).

Global Settlements

[3] Jerome P. McHugh and FT&T, Inc., October 30, 1989; Richardson Operating Company and Conoco Inc., July 1993

The Jicarilla Tribe has entered global settlement agreements with Conoco Inc., Columbus Energy, and Jerome McHugh. RVD reviewed these settlements and determined that the settlements covered all the time periods when these companies were responsible for royalty payments on Jicarilla Tribal leases, therefore, RVD will not issue orders for major portion and dual accounting to these companies.

Conclusion

Our review of the major portion values calculated from the data reported to the Jicarilla Tribe on the RIK purchase statements shows that they are reasonable prices paid for a major portion of like-quality production sold from the Reservation. The use of these major portion values enforces the major portion price requirements found in the lease terms and upholds our trust responsibility to the Jicarilla Tribe.

RVD plans to send orders to 40 (Attachment 7) companies after the Jicarilla Tribe concurs with our major portion methodology.

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June 18, 2004 (8:34AM)

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REPORT AND ATTACHMENTS CONTAIN PROPRIETARY DATA
FOR RELEASE ONLY TO THE JICARILLA APACHE INDIAN TRIBE

November 20, 1997

METHODOLOGY FOR MAJOR PORTION AND DUAL ACCOUNTING ANALYSIS JICARILLA APACHE TRIBAL LEASES

Purpose

The purpose of this report is to provide a background and to discuss the results of major portion and dual accounting analyses recently undertaken by the Royalty Valuation Division (RVD), Royalty Management Program (RMP), Minerals Management Service (MMS), for natural gas produced from Jicarilla Apache Tribal leases.

Background

On December 6, 1996, representatives of the Jicarilla Apache Indian Tribe (Jicarilla Tribe) and MMS met to discuss the implementation of major portion pricing for the natural gas produced from the Jicarilla Reservation (Reservation). From July 1, 1975, to June 30, 1995, the Jicarilla Tribe sold gas under royalty-in-kind (RIK) agreements. Until 1989, gas was bought by either the Northwest Pipeline Corporation (Northwest) or the El Paso Natural Gas Company (El Paso) under long-term contracts. In 1989, the Jicarilla Tribe entered into contract settlements with El Paso and Northwest, thus allowing the companies to pay market prices rather than the Natural Gas Policy Act (NGPA) ceiling prices.

On May 28, 1997, representatives of the Jicarilla Tribe and MMS met in Dallas, Texas, to discuss the implementation of the major portion and dual accounting analyses. MMS presented a proposal to the Jicarilla Tribe that recommended MMS would issue orders to perform major portion based on Jicarilla Tribal RIK prices for each NGPA category. The Jicarilla Tribe concurred with this approach. The Jicarilla Tribe also concurred that the orders should also include dual accounting.

On June 17 and October 8, 1997, representatives of the Jicarilla Tribe and MMS met to review the contract settlements, sources of data, pricing data, and the major portion/dual accounting order to perform.

Regulatory Criteria

The oil and gas valuation regulations found at 30 CFR 206 (1987), have long required that the "estimated reasonable value" of production be used for the purposes of computing royalties. Due consideration is given to the highest price paid for a part or for a major portion of gas of like quality in the same field, to the price received by the lessee, to posted prices, and to other relevant matters. Title 25 CFR 211 (1997) (Indian Tribal) and the terms of the Jicarilla Tribal leases also specify that the value may, at the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered at the time of production for the major portion of gas and/or natural gasoline and/or all other hydrocarbon substances produced and sold from the field where the leased lands are located.

The amended valuation regulations at 30 CFR §§ 206.172(a)(3)(i) and 206.173(a)(3)(i) (1997) address the issue of major portion for Indian lands. Specifically, the regulations provide:

> For any Indian leases which provide that the Secretary may consider the highest price paid or offered for a major portion of production (major portion) in determining value of production for royalty purposes, if data are available to compute a major portion MMS will, where practicable, compare the value determined in accordance with this section with the major portion. The value to be used in determining the value of production for royalty purposes shall be the higher of those two values.

For natural gas, these regulations specify that a major portion price is calculated for like-quality gas in the same field (or, if necessary, to obtain a reasonable sample from the same area). Like-quality gas is gas of similar physical, chemical, and legal characteristics. Legal characteristics are generally the applicable NGPA category or subcategory.

Dual accounting requirements are specified by Indian lease terms, regulations, and MMS instructions. Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.172 (1997), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.173 (1997). Where the specific provisions of a lease are inconsistent with these regulations, the lease agreement shall govern to the extent of that inconsistency.

Major Portion Methodology

Under the agreement reached between MMS and Jicarilla representatives, the major portion methodology will identify the prices paid under RIK contracts and RIK settlement agreements and calculate the major portion by NGPA category for all gas production in the Reservation utilizing RIK data for the time period January 1984 through June 1995. The following key issues were agreed to by RVD and the Jicarilla Tribe at the December 6, 1996, and June 17, 1997, meetings:

- RVD will consider the Reservation as the "area" for calculating the major portion

pricing.

- **The price received for the RIK portion of the gas represents the one-eighth royalty share. RVD will extrapolate the one-eighth royalty share to the entire eight-eighths sales volume and assume the value for the one-eighth royalty share is representative of the prices received for the other portion of the gas sold from the Reservation.**
- **RVD will analyze samples of Jicarilla settlement statements from Northwest and El Paso and certify that the Jicarilla Tribe received the proper NGPA prices.**
- **RVD will send orders to the non-RIK payors only.**

The NGPA Category

The major portion analysis covers the period from January 1984 through June 1995. Beginning with January 1984, RVD identified gas values by NGPA category for periods prior to the 1989 settlements. In the post-settlement period, RVD identified the settlement price by NGPA category. In the orders that RVD will send to the non-RIK payors, we will provide major portion prices by NGPA category and request that the payor identify the NGPA category of their gas, the time periods, and the lease(s) for which the company was a payor between January 1984 and June 1995.

The January 1984 through December 1986 and July 1988 through December 1988 major portion prices are based on the published NGPA prices plus tax reimbursements received by the Jicarilla Tribe. These prices are shown in Attachment 1 by NGPA category for each month/year. The NGPA categories identified are as follows:

102 New natural gas	103 New onshore production
104 Post - 1974 gas	104 1973-1974 Biennium gas
104 Replacement gas	104 Flowing gas
104 Rocky Mountain gas	105 Existing intrastate gas
108 Stripper gas	109 Other gas

The January 1987 through June 1988 major portion prices are based on a weighted-average price received by the Jicarilla Tribe resulting from a negotiated temporary price reduction between the Jicarilla Tribe, Northwest and El Paso. Starting in January 1989, the major portion prices are based on the prices received under the Jicarilla Tribal RIK contract plus contract settlements. The prices are shown in Attachment 1 by NGPA category for each month/year.

RVD used the Auditing and Financial System (AFS) database to determine prices paid by those payors who paid in-value and to further support that the RIK prices represent the major portion price (Attachment 2).

Definition of Field or Area

The majority of the Reservation is within Rio Arriba County, New Mexico, with a small portion extending into Sandoval County, New Mexico. The Reservation lies along the eastern edge of the San Juan Basin. Gas production is from the Pictured Cliffs Formation, Mesaverde Group, Gallup, Tocito, and fractured Mancos Formations, and the Dakota and Dakota-Morrison Formations. The Fruitland Formation produces methane primarily from coals (Fruitland Coal). The regulations at 30 CFR §§ 206.172(a)(3)(ii) and 206.173(a)(3)(ii)(1997) state that major portion will be calculated on "like-quality gas sold under arm's-length contracts from the same field (or, if necessary, to obtain a reasonable sample, from the same area)." However, the State of New Mexico utilizes pools, rather than, field definitions. A pool is a "common source of supply" and is generally based on a geologic horizon. The State of New Mexico Oil and Gas Commission defines 30 pools that overlay or are within the Reservation boundary. In several cases, several pools overlay one another and/or extend well outside the Reservation boundary. Consequently, we are unable to define distinct field boundaries for Jicarilla Tribal gas production. Therefore, for this study, the Reservation boundary will be defined as the area. During the June 17, 1997, meeting between MMS and the Jicarilla Tribe, the Jicarilla Tribal representative agreed to use the Reservation boundary *as the major portion area.*

Data Retrieval

During September 1996, AFS data as reported on the Report of Sales and Royalty Remittance (Form MMS-2014), was extracted from the AFS database, processed and downloaded to a Microsoft Access table on the RVD Local Area Network. The criteria for extracting these data were: (1) all AFS data reported under Fund Code 550 (the fund code for the Reservation); (2) the product codes 03 (residue gas) and 04 (unprocessed gas); and (3) the transaction codes 01 (royalty) and 11 (transportation allowance).

Data Processing

Once extracted from the AFS database, the information was processed by a program that removed adjustments to previously submitted information. This program first sorted the database by lease, product code, revenue source, selling arrangement, sales year, sales month, royalty quantity, and royalty value. The program then identified all negative (adjusted) royalty quantities and values and searched for a matching positive line. If a match was found, both the positive and negative lines were removed. Next, those negative lines without a matching positive (indicative of misreporting) were written to an error file and removed from further processing.

The next operation performed on the data was to determine prices paid by the in-value payors. We calculated $/MMBtu prices by adjusting for the quality of the gas.

A problem encountered in the data was that some records did not have a reported gas quality or the reported Btu content was not within a reasonable range. Options included removing those records, using the quality last reported for the lease, or assuming a quality. After analyzing this problem, we decided that given our limited resources, the best option was to calculate a gas quality from the data available. We determined the 1996 average quality reported on the Monthly Report of Operations (Form MMS-3160) for all Jicarilla leases and calculated the average Btu range reported on all Jicarilla leases. For all product code 04 (unprocessed gas) lines submitted that did not report a quality or reported a quality outside of the average Btu range, we used the calculated average Btu reported on the Form MMS-3160 for each lease. For all product code 03 (residue gas) lines submitted that did not report a quality or reported a quality outside of the reasonable range, we calculated an average Btu reported on the Form MMS-2014 for the time period.[1]

AFS Analysis of Major Portion Prices

The purchaser's of RIK production (El Paso and Northwest) did not report RIK sales on Form MMS-2014. In an effort to verify that the imputed weighted-average RIK price[2] is the price at which 50 percent plus 1 MMBtu (by volume) of gas was sold, we extracted AFS database lines for the in-value payors for the sample month/year February 1988. RVD then arrayed the $/MMBtu prices and the volumes reported on the Form MMS-2014 by the in-value payors from the highest to the lowest price. We manually added the RIK prices and volumes for El Paso and Northwest to create an off-line Form MMS-2014. We added this off-line Form MMS-2014 RIK data to the price array. RVD determined the price at which 50 percent (by volume) plus 1 MMBtu of the gas (starting from the top) was sold (Attachment 2). This analysis concluded that the major portion price for February 1988 was the weighted- average RIK price.

[1]The Form MMS-3160 does not contain a Btu for the residue gas. Therefore, RVD used the Btu information obtained from the Form MMS-2014.

[2]RVD calculated a weighted- average $/MMBtu price for the RIK volumes.

In addition, RVD also conducted an analysis to determine what percentage the extrapolated eight-eighths RIK sales volumes represented when compared to the total sales volumes reported by the in-value payors on the Form MMS-2014. RVD downloaded all Form MMS-2014 data from AFS for Fund Code 550 (Jicarilla Tribe). We then totaled the sales volumes by payor for February 1988. From the El Paso and Northwest settlement statements, RVD determined the RIK volumes purchased. We then calculated the eight-eighths RIK sales volume by dividing the one-eighth RIK volume by the royalty rates. To determined the total sales for the Reservation, RVD added the eight-eighths RIK sales volume to the Form MMS-2014 in-value sales volumes. We then divided the eight-eighths RIK sales volume by the total sales volume for the Reservation. From this analysis, RVD concluded that eight-eighths RIK sales volumes represent approximately 67 percent of the total sales volumes on the Reservation for the February 1988 sales month (Attachment 3).

The results of the above analyses further support that the data used to perform the major portion analysis were sufficient for that purpose and the values derived by RVD from the Jicarilla Tribal RIK data were reasonable.

Calculation of Major Portion Values

The major portion calculation has been divided into four time periods :

- Period 1: NGPA pricing was in effect for both El Paso and Northwest contracts (January 1984 through December 1986).
- Period 2: El Paso negotiated a temporary price reduction from the NGPA prices for the January 1987 through June 1987. Northwest negotiated a temporary price reduction from the NGPA prices for the July 1987 through June 1988 period.
- Period 3: NGPA pricing was in effect for both contracts.
- Period 4: Northwest negotiated a buy out of their contract and El Paso negotiated a buy down of their contract.

The time periods and effective prices are shown in Table 1. Tax reimbursement information was obtained from the Jicarilla Tribal Tax manual and is shown in Table 2.

Major portion prices were calculated by using the prices received under the Jicarilla RIK contracts and are shown in Attachment 1. For periods 1 and 3, the major portion prices are the sum of the published NGPA prices and the tax reimbursements. The prices received by the Jicarilla Tribe in Period 2 (the market-out period) and Period 4 (the post-settlement period) are calculated as discussed below.

During the market-out period (Period 2- January 1987 through June 1988), RVD calculated a weighted-average price received for each NGPA category by multiplying the contract price times the Strata Evaluation Associates, Inc. (Strata),[3] reserve volume estimate and dividing the total El Paso and Northwest values by the total Strata volume estimate (Attachment 4).

After the effective date of the Northwest and El Paso contract settlements, major portion prices were calculated by allocating the El Paso and Northwest settlement proceeds by NGPA category to the actual prices received under the El Paso settlement agreement to determine the total consideration received under the RIK contract for each NGPA category. Documents provided in support of the RIK contract settlements proceeds provided detailed information on the settlement monies received for each NGPA category. These amounts were used to calculate the major portion prices by category.

Strata calculated the amounts due to the Jicarilla Tribe for contract settlements with El Paso and Northwest based on volumetric decline curve analysis of the estimated reserves of the wells.

TABLE 1
Natural Gas Pricing Variations

Period	Time Period	El Paso Price	Northwest Price
1	January 1984 - December 1986	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
2	January 1987 - June 1987	$2.50	NGPA & Tax Reimbursement
2	July 1987 - June 1988	NGPA & Tax Reimbursement	Contract Negotiated Price
3	July 1988 - December 1988	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
3	January 1989 - June 1989	NGPA & Tax Reimbursement;	Contract Buy out - 2/89

[3]. Strata Evaluation Associates, Inc., Parker, Colorado, performed an evaluation of the producing capacity of all wells that contributed to the Northwest or El Paso systems as of July 1, 1989.

		Contract Buy down 7/89	
4	July 1989 - December 1989	$1.227 + buy down	Buy out
4	1990	$1.276 + buy down	Buy out
4	1991	$1.327 + buy down	Buy out
4	1992	$1.380 + buy down	Buy out
4	1993	$1.435 + buy down	Buy out
4	1994	$1.493 + buy down	Buy out
4	1995	$1.553 + buy down	Buy out

TABLE 2
Jicarilla Tax Rates

Date	Severance Tax (Per MMBtu)	Privilege Tax (87.5% of Value)
1/1/84 through 5/30/85	$0.05	
6/1/85 through 1/31/86	$0.05	5.00%
2/1/86 through 1/31/87	$0.05	5.18%
2/1/87 through 1/31/88	$0.05	5.28%
2/1/88 through 12/31/88	$0.05	5.47%

The contract settlements were based on the difference between the projected NGPA prices due under the original contract and the price negotiated under the buy out or buy down contract. Based on the projected NGPA prices and volumetric analysis, Strata calculated an annual present value estimate of the remaining reserves for both El Paso and Northwest (Column B) as shown on Attachment 5. This value was then discounted using a 10 percent discount rate (Column C). This settlement value was further reduced during negotiations between the Jicarilla Tribe and the companies (Column D). A settlement factor was calculated by dividing the total actual settlement amount by the Strata estimated settlement. For El Paso this was about 87 percent and for Northwest this was about 70 percent. This factor was then applied to the discounted amounts to determine a total annual settlement value (Column D). The annual settlement value was then divided by the annual present value estimate to generate a settlement discount factor (Column E). A price differential (Column H) was calculated between the projected NGPA price (Column G) and the buy down/buy out price (Column F). This differential represents the difference between the contract price not bought-out or not bought-down minus the buy down/buy out price. The undiscounted value was then discounted using the settlement discount factor discussed above to generate a settled price differential (Column I). This differential was then added to the buy-down/buy-out price to determine the major portion price (Column J) by category.

The above procedure was used to calculate all NGPA pricing categories, except those NGPA prices that were less than the buy-down/buy-out price, for which the major portion prices were equated to the actual buy-down/buy-out price (Columns K and L).

RVD then calculated a weighted-average price. This price was calculated by multiplying the appropriate El Paso and Northwest price received for each NGPA category by the Strata reserve volume for El Paso and Northwest and dividing both calculated values by the total volume for El Paso and Northwest (Attachment 5).

Dual Accounting Calculation

Dual accounting requirements are specified by Indian lease terms and regulations found at 25 CFR § 211.13(a) (1997) which state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater. [Emphasis added.]

Dual accounting is defined as a valuation method that requires the lessee to compute royalties based on the greater of: (1) the value of the gas prior to processing (as determined under 30 CFR § 206.172 (1997)), or (2) the combined value of the residue gas and gas plant products resulting from processing the gas (as determined under 30 CFR § 206.173 (1997)), plus the value of any condensate recovered downstream of the point of royalty settlement without resorting to processing (30 CFR § 206.52 (1997)). However, the value of production can never be less than the gross proceeds accruing to the lessee (30 CFR §§ 206.172(h) and 206.173(h) (1997)). After March 1, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (30 CFR §§ 206.176 through 206.179 (1997)).

RVD will review the responses to the September 29, 1995, Dear Payor letter and will issue orders to perform dual accounting and pay royalties on major portion prices.[4] For those companies who stated that they performed dual accounting, RVD compared prices paid by the payors who paid in-value to the calculated major portion prices to determine whether orders should be issued. RVD will issue orders to those payors who paid in value (Attachment 6) and will require payments on the higher of the gross proceeds or the major portion price.

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[4]**The orders will cite the requirement that royalty be based on the higher of the major portion value or gross proceeds accruing to the lessee as well as the requirement to perform dual accounting.** Sales by affiliates may provide information concerning gross proceeds to the lessee and the appropriate benchmark value and thus may be considered in determining royalty values.

RVD reviewed contracts for the sales of natural gas liquids (NGL's). RVD obtained two comparable contracts[5] with sales in the San Juan Basin. Under both of these contracts, the referenced price for NGL's was the Mt. Belvieu, Texas, spot prices. Thus, RVD determined that a comparable contract price for NGL's for the Reservation was the average Mt. Belvieu spot market price. The orders will require the calculations for NGL's to be based on the higher of the gross proceeds received for the NGL's or the average Mt. Belvieu spot market price (Attachment 7).

Global Settlements

The Jicarilla Tribe has entered global settlement agreements with Conoco Inc., Columbus Energy, and Jerome McHugh. RVD reviewed these settlements and determined that the settlements covered all the time periods when these companies were responsible for royalty payments on Jicarilla Tribal leases. Therefore, RVD will not issue orders for major portion and dual accounting to these companies.

Conclusion

Our review of the major portion values calculated from the data reported to the Jicarilla Tribe on the RIK purchase statements shows that they are reasonable prices paid for a major portion of like-quality production sold from the Reservation. The use of these major portion values enforces the major portion price requirements found in the lease terms and upholds our trust responsibility to the Jicarilla Tribe.

RVD plans to send orders to 39 companies (Attachment 6) after the Jicarilla Tribe concurs with our major portion methodology.

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[5]These contracts include: Jerome P. McHugh (Buyer) and FT&T, Inc., (Seller) dated October 30, 1989, and Richardson Operating Company (Buyer) and Conoco Inc., (Seller) dated July 1993 (Attachment 8).

REPORT AND ATTACHMENTS CONTAIN PROPRIETARY DATA
FOR RELEASE ONLY TO THE JICARILLA APACHE INDIAN TRIBE

January 14, 1998

METHODOLOGY FOR MAJOR PORTION AND DUAL ACCOUNTING ANALYSIS JICARILLA APACHE TRIBAL LEASES

Purpose

The purpose of this report is to provide a background and to discuss the results of major portion and dual accounting analyses recently undertaken by the Royalty Valuation Division (RVD), Royalty Management Program (RMP), Minerals Management Service (MMS), for natural gas produced from Jicarilla Apache Tribal leases.

Background

On December 6, 1996, representatives of the Jicarilla Apache Indian Tribe (Jicarilla Tribe) and MMS met to discuss the implementation of major portion pricing for the natural gas produced from the Jicarilla Reservation (Reservation). From July 1, 1975, to June 30, 1995, the Jicarilla Tribe sold gas under royalty-in-kind (RIK) agreements. Until 1989, gas was bought by either the Northwest Pipeline Corporation (Northwest) or the El Paso Natural Gas Company (El Paso) under long-term contracts. In 1989, the Jicarilla Tribe entered into contract settlements with El Paso and Northwest, thus allowing the companies to pay market prices rather than the Natural Gas Policy Act (NGPA) ceiling prices.

On May 28, 1997, representatives of the Jicarilla Tribe and MMS met in Dallas, Texas, to discuss the implementation of the major portion and dual accounting analyses. MMS presented a proposal to the Jicarilla Tribe that recommended MMS would issue orders to perform major portion based on Jicarilla Tribal RIK prices for each NGPA category. The Jicarilla Tribe concurred with this approach. The Jicarilla Tribe also concurred that the orders should also include dual accounting.

On June 17 and October 8, 1997, representatives of the Jicarilla Tribe and MMS met to review the contract settlements, sources of data, pricing data, and the major portion/dual accounting order to perform. On January 12, representatives of the Jicarilla Tribe and MMS met to review the draft Methodology Report and the draft Order to Perform.

Regulatory Criteria

The oil and gas valuation regulations found at 30 CFR 206 (1987), have long required that the "estimated reasonable value" of production be used for the purposes of computing royalties. Due consideration is given to the highest price paid for a part or for a major portion of gas of like quality in the same field, to the price received by the lessee, to posted prices, and to other relevant matters. Title 25 CFR 211 (1997) (Indian Tribal) and the terms of the Jicarilla Tribal leases also specify that the value may, at the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered at the time of production for the major portion of gas and/or natural gasoline and/or all other hydrocarbon substances produced and sold from the field where the leased lands are located.

The amended valuation regulations at 30 CFR §§ 206.172(a)(3)(i) and 206.173(a)(3)(i) (1997) address the issue of major portion for Indian lands. Specifically, the regulations provide:

> For any Indian leases which provide that the Secretary may consider the highest price paid or offered for a major portion of production (major portion) in determining value of production for royalty purposes, if data are available to compute a major portion MMS will, where practicable, compare the value determined in accordance with this section with the major portion. The value to be used in determining the value of production for royalty purposes shall be the higher of those two values.

For natural gas, these regulations specify that a major portion price is calculated for like-quality gas in the same field (or, if necessary, to obtain a reasonable sample from the same area). Like-quality gas is gas of similar physical, chemical, and legal characteristics. Legal characteristics are generally the applicable NGPA category or subcategory.

Dual accounting requirements are specified by Indian lease terms, regulations, and MMS instructions. Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.172 (1997), to the value of that same gas after processing (the combined values of the residue gas and gas plant products), as determined under 30 CFR § 206.173 (1997). Where the specific provisions of a lease are inconsistent with these regulations, the lease agreement shall govern to the extent of that inconsistency.

Major Portion Methodology

Under the agreement reached between MMS and Jicarilla representatives, the major portion methodology will identify the prices paid under RIK contracts and RIK settlement agreements and calculate the major portion by NGPA category for all gas production in the Reservation utilizing RIK data for the time period January 1984 through June 1995. The following key issues were agreed to by RVD and the Jicarilla Tribe at the December 6, 1996, and June 17, 1997, meetings:

- **RVD will consider the Reservation as the "area" for calculating the major portion pricing.**
- **The price received for the RIK portion of the gas represents the one-eighth royalty share. RVD will extrapolate the one-eighth royalty share to the entire eight-eighths sales volume and assume the value for the one-eighth royalty share is representative of the prices received for the other portion of the gas sold from the Reservation.**
- **RVD will analyze samples of Jicarilla settlement statements from Northwest and El Paso and certify that the Jicarilla Tribe received the proper NGPA prices.**
- **RVD will send orders to the non-RIK payors only.**

The NGPA Category

The major portion analysis covers the period from January 1984 through June 1995. Beginning with January 1984, RVD identified gas values by NGPA category for periods prior to the 1989 settlements. In the post-settlement period, RVD identified the settlement price by NGPA category. In the orders that RVD will send to the non-RIK payors, we will provide major portion prices by NGPA category and request that the payor identify the NGPA category of their gas, the time periods, and the lease(s) for which the company was a payor between January 1984 and June 1995.

The January 1984 through December 1986 and July 1988 through December 1988 major portion prices are based on the published NGPA prices plus tax reimbursements received by the Jicarilla Tribe. These prices are shown in Attachment 1 by NGPA category for each month/year. The NGPA categories identified are as follows:

102 New natural gas	103 New onshore production
104 Post - 1974 gas	104 1973-1974 Biennium gas
104 Replacement gas	104 Flowing gas
104 Rocky Mountain gas	105 Existing intrastate gas
108 Stripper gas	109 Other gas

The January 1987 through June 1988 major portion prices are based on a weighted-average price received by the Jicarilla Tribe resulting from a negotiated temporary price reduction between the Jicarilla Tribe, Northwest and El Paso. Starting in January 1989, the major portion prices are based on the prices received under the Jicarilla Tribal RIK contract plus contract settlements. The prices are shown in Attachment 1 by NGPA category for each month/year.

Definition of Field or Area

The majority of the Reservation is within Rio Arriba County, New Mexico, with a small portion extending into Sandoval County, New Mexico. The Reservation lies along the

eastern edge of the San Juan Basin. Gas production is from the Pictured Cliffs Formation, Mesaverde Group, Gallup, Tocito, and fractured Mancos Formations, and the Dakota and Dakota-Morrison Formations. The Fruitland Formation produces methane primarily from coals (Fruitland Coal). The regulations at 30 CFR §§ 206.172(a)(3)(ii) and 206.173(a)(3)(ii)(1997) state that major portion will be calculated on "like-quality gas sold under arm's-length contracts from the same field (or, if necessary, to obtain a reasonable sample, from the same area)." However, the State of New Mexico utilizes pools, rather than, field definitions. A pool is a "common source of supply" and is generally based on a geologic horizon. The State of New Mexico Oil and Gas Commission defines 30 pools that overlay or are within the Reservation boundary. In several cases, several pools overlay one another and/or extend well outside the Reservation boundary. Consequently, we are unable to define distinct field boundaries for Jicarilla Tribal gas production. Therefore, for this study, the Reservation boundary will be defined as the area. During the June 17, 1997, meeting between MMS and the Jicarilla Tribe, the Jicarilla Tribal representative agreed to use the Reservation boundary as the major portion area.

Data Retrieval

During September 1996, AFS data as reported on the Report of Sales and Royalty Remittance (Form MMS-2014), was extracted from the AFS database, processed and downloaded to a Microsoft Access table on the RVD Local Area Network. The criteria for extracting these data were: (1) all AFS data reported under Fund Code 550 (the fund code for the Reservation); (2) the product codes 03 (residue gas) and 04 (unprocessed gas); and (3) the transaction codes 01 (royalty) and 11 (transportation allowance).

Data Processing

Once extracted from the AFS database, the information was processed by a program that removed adjustments to previously submitted information. This program first sorted the database by lease, product code, revenue source, selling arrangement, sales year, sales month, royalty quantity, and royalty value. The program then identified all negative (adjusted) royalty quantities and values and searched for a matching positive line. If a match was found, both the positive and negative lines were removed. Next, those negative lines without a matching positive (indicative of misreporting) were written to an error file and removed from further processing.

The next operation performed on the data was to determine prices paid by the in-value payors. We calculated $/MMBtu prices by adjusting for the quality of the gas.

A problem encountered in the data was that some records did not have a reported gas quality or the reported Btu content was not within a reasonable range. Options included removing those records, using the quality last reported for the lease, or assuming a quality.

After analyzing this problem, we decided that given our limited resources, the best option was to calculate a gas quality from the data available. We determined the 1996 average quality reported on the Monthly Report of Operations (Form MMS-3160) for all Jicarilla leases and calculated the average Btu range reported on all Jicarilla leases. For all product code 04 (unprocessed gas) lines submitted that did not report a quality or reported a quality outside of the average Btu range, we used the calculated average Btu reported on the Form MMS-3160 for each lease. For all product code 03 (residue gas) lines submitted that did not report a quality or reported a quality outside of the reasonable range, we calculated an average Btu reported on the Form MMS-2014 for the time period.[1]

AFS Analysis of Major Portion Prices

RVD conducted an analysis to determine what percentage the extrapolated eight-eighths RIK sales volumes represented when compared to the total sales volumes reported by the in-value payors on the Form MMS-2014. RVD downloaded all Form MMS-2014 data from AFS for Fund Code 550 (Jicarilla Tribe). We then totaled the sales volumes by payor for February 1988. From the El Paso and Northwest settlement statements, RVD determined the RIK volumes purchased. We then calculated the eight-eighths RIK sales volume by dividing the one-eighth RIK volume by the royalty rates. To determined the total sales for the Reservation, RVD added the eight-eighths RIK sales volume to the Form MMS-2014 in-value sales volumes. We then divided the eight-eighths RIK sales volume by the total sales volume for the Reservation. From this analysis, RVD concluded that eight-eighths RIK sales volumes represent approximately 67 percent of the total sales volumes on the Reservation for the February 1988 sales month (Attachment 2).

The results of the above analyses further support that the data used to perform the major portion analysis were sufficient for that purpose and the values derived by RVD from the Jicarilla Tribal RIK data were reasonable.

Calculation of Major Portion Values

The major portion calculation has been divided into four time periods :

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[1]The Form MMS-3160 does not contain a Btu for the residue gas. Therefore, RVD used the Btu information obtained from the Form MMS-2014.

- Period 1: NGPA pricing was in effect for both El Paso and Northwest contracts (January 1984 through December 1986).
- Period 2: El Paso negotiated a temporary price reduction from the NGPA prices for the January 1987 through June 1987. Northwest negotiated a temporary price reduction from the NGPA prices for the July 1987 through June 1988 period.
- Period 3: NGPA pricing was in effect for both contracts.
- Period 4: Northwest negotiated a buy out of their contract and El Paso negotiated a buy down of their contract.

The time periods and effective prices are shown in Table 1. Tax reimbursement information was obtained from the Jicarilla Tribal Tax manual and is shown in Table 2.

TABLE 1
Natural Gas Pricing Variations

Period	Time Period	El Paso Price	Northwest Price
1	January 1984 - December 1986	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
2	January 1987 - June 1987	$2.50	NGPA & Tax Reimbursement
2	July 1987 - June 1988	NGPA & Tax Reimbursement	Contract Negotiated Price
3	July 1988 - December 1988	NGPA & Tax Reimbursement	NGPA & Tax Reimbursement
3	January 1989 - June 1989	NGPA & Tax Reimbursement; Contract Buy down 7/89	Contract Buy out - 2/89
4	July 1989 - December 1989	$1.227 + buy down	Buy out
4	1990	$1.276 + buy down	Buy out
4	1991	$1.327 + buy down	Buy out
4	1992	$1.380 + buy down	Buy out
4	1993	$1.435 + buy down	Buy out
4	1994	$1.493 + buy down	Buy out
4	1995	$1.553 + buy down	Buy out

Major portion prices were calculated by using the prices received under the Jicarilla RIK contracts and are shown in Attachment 1. For periods 1 and 3, the major portion prices are the sum of the published NGPA prices and the tax reimbursements. The prices received by the

Jicarilla Tribe in Period 2 (the market-out period) and Period 4 (the post-settlement period) are calculated as discussed below.

During the market-out period (Period 2- January 1987 through June 1988), RVD calculated a weighted-average price received for each NGPA category by multiplying the contract price times the Strata Evaluation Associates, Inc. (Strata),[2] reserve volume estimate and dividing the total El Paso and Northwest values by the total Strata volume estimate (Attachment 3).

TABLE 2
Jicarilla Tax Rates

Date	Severance Tax (Per MMBtu)	Privilege Tax (87.5% of Value)
1/1/84 through 5/30/85	$0.05	
6/1/85 through 1/31/86	$0.05	5.00%
2/1/86 through 1/31/87	$0.05	5.18%
2/1/87 through 1/31/88	$0.05	5.28%
2/1/88 through 12/31/88	$0.05	5.47%

After the effective date of the Northwest and El Paso contract settlements, major portion prices were calculated by allocating the El Paso and Northwest settlement proceeds by NGPA category to the actual prices received under the El Paso settlement agreement to determine the total consideration received under the RIK contract for each NGPA category. Documents provided in support of the RIK contract settlements proceeds provided detailed information on the settlement monies received for each NGPA category. These amounts were used to calculate the major portion prices by category.

[2] Strata Evaluation Associates, Inc., Parker, Colorado, performed an evaluation of the producing capacity of all wells that contributed to the Northwest or El Paso systems as of July 1, 1989.

Strata calculated the amounts due to the Jicarilla Tribe for contract settlements with El Paso and Northwest based on volumetric decline curve analysis of the estimated reserves of the wells.

The contract settlements were based on the difference between the projected NGPA prices due under the original contract and the price negotiated under the buy out or buy down contract. Based on the projected NGPA prices and volumetric analysis, Strata calculated an annual present value estimate of the remaining reserves for both El Paso and Northwest (Column B) as shown on Attachment 4. This value was then discounted using a 10 percent discount rate (Column C). This settlement value was further reduced during negotiations between the Jicarilla Tribe and the companies (Column D). A settlement factor was calculated by dividing the total actual settlement amount by the Strata estimated settlement. For El Paso this was about 87 percent and for Northwest this was about 70 percent. This factor was then applied to the discounted amounts to determine a total annual settlement value (Column D). The annual settlement value was then divided by the annual present value estimate to generate a settlement discount factor (Column E). A price differential (Column H) was calculated between the projected NGPA price (Column G) and the buy down/buy out price (Column F). This differential represents the difference between the contract price not bought-out or not bought-down minus the buy down/buy out price. The undiscounted value was then discounted using the settlement discount factor discussed above to generate a settled price differential (Column I). This differential was then added to the buy-down/buy-out price to determine the major portion price (Column J) by category.

The above procedure was used to calculate all NGPA pricing categories, except those NGPA prices that were less than the buy-down/buy-out price, for which the major portion prices were equated to the actual buy-down/buy-out price (Columns K and L).

RVD then calculated a weighted-average price. This price was calculated by multiplying the appropriate El Paso and Northwest price received for each NGPA category by the Strata reserve volume for El Paso and Northwest and dividing both calculated values by the total volume for El Paso and Northwest (Attachment 4).

Dual Accounting Calculation

Dual accounting requirements are specified by Indian lease terms and regulations found at 25 CFR § 211.13(a) (1997) which state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that <u>royalty will be computed on the value of gas or casinghead gas, or</u>

on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater. [Emphasis added.]

Dual accounting is defined as a valuation method that requires the lessee to compute royalties based on the greater of: (1) the value of the gas prior to processing (as determined under 30 CFR § 206.172 (1997)), or (2) the combined value of the residue gas and gas plant products resulting from processing the gas (as determined under 30 CFR § 206.173 (1997)), plus the value of any condensate recovered downstream of the point of royalty settlement without resorting to processing (30 CFR § 206.52 (1997)). However, the value of production can never be less than the gross proceeds accruing to the lessee (30 CFR §§ 206.172(h) and 206.173(h) (1997)). After March 1, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (30 CFR §§ 206.176 through 206.179 (1997)). **RVD will review the responses to the September 29, 1995, Dear Payor letter and will issue orders to perform dual accounting and pay royalties on major portion prices.[3] For those companies who stated that they performed dual accounting, RVD compared prices paid by the payors who paid in-value to the calculated major portion prices to determine whether orders should be issued. RVD will issue orders to those payors who paid in value (Attachment 5) and will require payments on the higher of the gross proceeds or the major portion price.**

RVD reviewed contracts for the sales of natural gas liquids (NGL's). RVD obtained two comparable contracts[4] with sales in the San Juan Basin. Under both of these contracts, the referenced price for NGL's was the Mt. Belvieu, Texas, spot prices. Thus, RVD determined that a comparable contract price for NGL's for the Reservation was the average Mt. Belvieu spot market price. The orders will require the calculations for NGL's to be based on the higher of the gross proceeds received for the NGL's or the average Mt. Belvieu spot market price (Attachment 6).

Global Settlements

[3]**The orders will cite the requirement that royalty be based on the higher of the major portion value or gross proceeds accruing to the lessee as well as the requirement to perform dual accounting.** Sales by affiliates may provide information concerning gross proceeds to the lessee and the appropriate benchmark value and thus may be considered in determining royalty values.

[4]**These contracts include: Jerome P. McHugh (Buyer) and FT&T, Inc., (Seller) dated October 30, 1989, and Richardson Operating Company (Buyer) and Conoco Inc., (Seller) dated July 1993 (Attachment 7).**

The Jicarilla Tribe has entered global settlement agreements with Conoco Inc., Columbus Energy, and Jerome McHugh. RVD reviewed these settlements and determined that the settlements covered all the time periods when these companies were responsible for royalty payments on Jicarilla Tribal leases. Therefore, RVD will not issue orders for major portion and dual accounting to these companies.

Conclusion

Our review of the major portion values calculated from the data reported to the Jicarilla Tribe on the RIK purchase statements shows that they are reasonable prices paid for a major portion of like-quality production sold from the Reservation. The use of these major portion values enforces the major portion price requirements found in the lease terms and upholds our trust responsibility to the Jicarilla Tribe.

RVD plans to send orders to 39 companies (Attachment 5) after the Jicarilla Tribe concurs with our major portion methodology.

List of Attachments

1. Major Portion Pricing
2. 2/88 volume summary
3. Weighted average pricing calculation
4. Major portion pricing calculations
5. List of payors
6. Average NGL Prices
7. Contracts

September 15, 1997

MMS-RVD-OG
Mail Stop 3152

CERTIFIED MAIL--
RETURN RECEIPT REQUESTED

Name
Company
Address
City, State, Zip

Dear Name

In carrying out the trust responsibility of the United States in the administration of Indian oil and gas leases, the Minerals Management Service (MMS) has long recognized the primacy of the lease terms. As a royalty payor on Jicarilla Apache Indian Tribal leases, you are obligated to comply with Section 3(c) **Rental and royalty**, of the Indian lease terms. More specifically, the regulations state that major portion analysis for oil and gas and dual accounting for gas (accounting for comparison) must be performed in determining the value of production for royalty purposes. (Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.)

For major portion, Federal Regulations (25 CFR § 211.13 (1996)) state:

> During the period of supervision, "value" for the purposes of the lease may, in the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the supervisor.

This requirement is also embodied in the gas valuation regulations found at 30 CFR §§ 206.172 and 206.173 (1996).

Dual accounting requirements are specified by Indian lease terms and Federal regulations found

at 25 CFR § 211.13 (1996) which state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that compares the value of the gas prior to processing, as determined under 30 CFR § 206.172 (1996), to the value of that same gas after processing (the combined values of the residue gas and gas plant products plus the value of any condensate recovered downstream of the point of royalty settlement without resorting to processsing), as determined under 30 CFR § 206.173 (1996). Royalty on gas produced from an Indian lease and ultimately processed (either by the lessee or any purchaser) must be computed by applying the dual accounting requirements specified by the lease and paid based on the method yielding the higher value. However, royalty is never to be based on a value which is less than the gross proceeds received by the lessee. (After March 31, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.176 through 206.179 (1996)).

Major Portion

MMS has performed major portion analyses for natural gas production from Jicarilla Apache leases for the period **January 1984 through June 1995**. We have used gas sales data reported by the Jicarilla Apache Tribe (Jicarilla Apache) under their Royalty-in-Kind (RIK) program to determine major portion prices for the Jicarilla Apache Indian Reservation (Reservation) by production month. We have determined that the Jicarilla Apache sold the majority of their RIK production based on the Maximum Lawful Price (MLP) as set by the Natural Gas Policy Act (NGPA) in the following categories:

102 New natural gas	103 New onshore production
104 Flowing gas	104 Replacement gas
105 Existing intrastate	106 Alternate MLP
107 Tight gas	108 Stripper gas
109 Other gas	

Enclosure 1 provides a list of major portion prices to be used in the dual accounting calculation. The January 1985 through December 1988 prices are based on the NGPA price plus tax reimbursements received by the Jicarilla Apache and are shown by NGPA category by month. Starting in January 1989, the major portion prices are based on the prices recieved under the Jicarilla Apache RIK contract and are shown by NGPA category by month. Enclosure 2 provides a list of your accounting identification (AID) numbers for the Reservation, the wells pertaining to each lease, and the NGPA category for the wells. If you are not responsible for payment of royalties for the lease numbers in Enclosure 2 between January 1984 and June 1995, please identify the responsible party and the date your responsibility ended.

NOTE: The following section entitled Dual Accounting pertain to both those payors that stated they did or did not perform dual accounting. The final letter will be modified for each set of payors

Dual Accounting - did perform

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 3-6), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1996).

In section 3(c) entitled "Rental and Royalty" of Jicarilla Apache leases, we determined that the lease terms require dual accounting. MMS issued an order (September 29, 1995) to (*Short company name*) to provide a declaration of policy on dual accounting. On your response, you stated that the company did perform dual accounting on the Indian leases for which *Short company name* is a royalty payor. A review of sample months show that your dual accounting calculations were based on prices less than major portion prices shown in Attachment 1. As a result, additional royalties may be due.

Dual Accounting - Did not perform

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 3-6), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1996).

MMS issued an order (September 29, 1995) to (*Short company name*) to provide a declaration of policy on dual accounting. On your response, you stated that the company did not perform dual accounting on the Indian leases for which *Short company name* is a royalty payor. In section 3(c) entitled "Rental and Royalty" of Jicarilla Apache leases, we determined that the lease terms require dual accounting. As a result, additional royalties may be due

Order to Perform

Therefore, in order to comply with regulations and lease terms, **within 90 days of receipt** of this letter, *Short company name* is ordered to perform the following:

1. Please compare the values shown on Enclosure 1 to the values *Short company name* reported to MMS on Form MMS-2014 from **January 1984 through June 1995**. From January 1984 through June 1995, use the higher of your gross proceeds or the price shown in Attachment 1 in the calculation described in Step (2). Please identify and document with copies of contracts or lease settlement statements, any differences you feel are not valid.

2. Using the higher of the gross proceeds or major portion price please calculate a dual accounting value (processed gas plus liquids value) and an unprocessed (well head) value, and recalculate royalties due following the dual accounting requirements.

   In the dual accounting calculation, the processed gas value includes residue gas values, natural gas liquids values, and condensate values less a processing allowance. (A processing allowance can only be claimed if a processing allowance form has been previously filed with MMS.) We have reviewed comparable contract prices and determined that Mt. Belvieu, Texas average spot prices provide a comparable contract price. Therefore, liquids values used in the calculation must be the higher of actual gross proceeds price or the Mt. Belvieu, Texas average spot price as shown in Enclosure 7.

   If *Short company name* is unable to obtain the necessary information to perform dual accounting as required by the lease terms, *Short company name* is directed to apply the theoretical dual accounting as explained in the MMS' "Dear Payor" letter dated July 27, 1992 (Enclosure 4). MMS has provided a worksheet for theoretical dual accounting calculations and a diskette with the Excel worksheet in order to assist *Short company name* in completing dual accounting calculations (Enclosure 8). If needed, MMS can provide assistance in completing these calculations.

3. Compare royalties due as calculated in step (2) above to royalties previously paid for each month and pay any additional royalties due. All such redeterminations are to be documented in the format shown in Enclosure 9.

Payment Instructions

Please be aware of the following when paying the additional royalties pertaining to major portion and dual accounting:

- Your payments should be made in accordance with the regulations at 30 CFR § 218.51 (1996), and accompanied by an appropriately completed green Form MMS-2014 (Enclosure 10). You will be in compliance with the order only if your payment and a copy of a properly completed green Form MMS-2014 is mailed to:

Jicarilla Apache Tribe
P.O. Box 2053
Albuquerque, NM 87103

- The completed original green Form MMS-2014 and a copy of your payment should be mailed to:

Minerals Management Service
Royalty Valuation Division
P.O. Box 5810
Denver, Colorado 80127-5810

- If you have questions on the completion of the Form MMS-2014, please contact your Reports Branch representative at (800) 525-0309 or (303) 231-3288. If you are not currently a royalty payor to MMS please contact Joseph Cornellisson at (303) 275-7239 for further instructions.

- For additional royalties, you must use adjustment reason code 49 when you report your additional royalties on Form MMS-2014. This adjustment reason code must be used for both the reversal line and the re-entry line.

- Appropriate late payment charges pursuant to 30 CFR § 218.102 (1996) will be computed and billed to *Short company name* upon receipt of payment of any additional royalties due.

All documentation supporting your compliance with this order should be retained until MMS completes its follow-up compliance testing. Section 109 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), promulgated in 30 CFR § 241.51 (1996), authorizes MMS to assess civil penalties for failure or refusal to comply with the requirements of FOGRMA or any statute, regulation, rule, order, lease, or permit. Consequently, your failure to comply with the terms of this order may be considered a violation pursuant to 30 CFR § 241.51 (1996) and could subject you to appropriate penalties as provided therein.

Appeal Rights

You have the right to appeal in accordance with the provisions of 30 CFR 290 (1996). Any appeal taken will be to the Deputy Commissioner of Indian Affairs and must be filed within 30 days from the receipt of this order at the following address:

Ms. Deborah Gibbs Tschudy
Chief, Royalty Valuation Division
Minerals Management Service

P.O. Box 25165, Mail Stop 3152
Denver, Colorado 80225-0165

Any notice of appeal must be accompanied by written statement of reasons, as you deem adequate to justify reversal or modification of this directive. Within 90 days from receipt of this order, the appellant will be permitted to file additional statement of reasons or written briefs.

With the exception of the time fixed for filing a notice of appeal, the time for filing any document in connection with an appeal may be extended. Extensions for filing the statement of reasons will not be permitted unless requested in writing by the appellant (within the 30-day period allowed for filing the appeal) with justification showing good cause for the time extension and delivered to Deborah Gibbs Tschudy at the above address.

In accordance with the provisions of 30 CFR § 243.2 (1996), compliance with this order will be suspended by reason of an appeal having been taken.

If you have any comments or questions concerning this request, contact Joseph Cornellisson at (303) 275-7239.

Sincerely,

Deborah Gibbs Tschudy
Chief, Royalty Valuation Division

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19

October 2, 1997

MMS-RVD-OG
Mail Stop 3152

CERTIFIED MAIL--
RETURN RECEIPT REQUESTED

Name
Company
Address
City, State, Zip

Dear Name

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> During the period of supervision, "value" for the purposes of the lease may, in the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the supervisor.

This requirement is also embodied in the gas valuation regulations found at 30 CFR §§ 206.172 and 206.173 (1996).

Dual accounting requirements are specified by Indian lease terms and Federal regulations found

at 25 CFR § 211.13 (1996) which state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that requires the lessee to compute royalties based on the greater of: (1) the value of the gas prior to processing (as determined under 30 CFR § 206.172 (1996)), or (2) the combined value of the residue gas and gas plant products resulting from processing the gas (as determined under 30 CFR § 206.173 (1996)), plus the value of any condensate recovered downstream of the point of royalty settlement without resorting to processing (30 CFR § 206.52). However, the value of production can never be less than the gross proceeds accruing to the lease. After March 1, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.176 through 206.179 (1996)).

Major Portion

MMS has performed major portion analyses for natural gas production from Jicarilla Apache leases for the period **January 1984 through June 1995**. We have used gas sales data reported by the Jicarilla Apache Tribe (Jicarilla Apache) under their Royalty-in-Kind (RIK) program to determine major portion prices for the Jicarilla Apache Indian Reservation (Reservation) by production month. We have determined that the Jicarilla Apache sold the majority of their RIK production based on the Maximum Lawful Price (MLP) as set by the Natural Gas Policy Act (NGPA) in the following categories:

102 New natural gas	103 New onshore production
104 Flowing gas	104 Replacement gas
105 Existing intrastate	108 Stripper gas
109 Other gas	

Enclosure 1 provides a list of major portion prices. These prices are based on the prices received under the Jicarilla Apache RIK contract and are shown by NGPA category by month. Enclosure 2 provides a list of your accounting identification (AID) numbers for the Reservation.. If you are not responsible for payment of royalties for the lease numbers in Enclosure 2 between January 1984 and June 1995, please identify the responsible party and the date your responsibility ended.

NOTE: The following section entitled Dual Accounting pertain to both those payors that stated they did or did not perform dual accounting. The final letter will be modified for each payor

Dual Accounting - did perform

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 3-6), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1996).

MMS has determined that the Jicarilla Apache lease terms require dual accounting (Section 3(c) entitled "Rental and Royalty"). MMS issued an order (September 29, 1995) to *(Short company name)* to provide a declaration of policy on dual accounting. On your response, you stated that the company did perform dual accounting on the Indian leases for which *Short company name* is a royalty payor. A review of sample months show that your dual accounting calculations were based on prices less than major portion prices shown in Enclosure 1. As a result, additional royalties may be due.

Dual Accounting - Did not perform

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 3-6), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1996).

MMS issued an order (September 29, 1995) to *(Short company name)* to provide a declaration of policy on dual accounting. On your response, you stated that the company did not perform dual accounting on the Indian leases for which *Short company name* is a royalty payor. MMS has determined that the Jicarilla Apache lease terms require dual accounting (Section 3© entitled "Rental and Royalty"). As a result, additional royalties may be due.

Order to Perform

In order to comply with the regulations and lease terms, **within <u>90</u> days of receipt** of this letter, *Short company name* is ordered to perform the following dual accounting and major portion calculations. Please follow the steps below to determine the value of the production for royalty purposes:

1. Calculate the **unprocessed gas value** for the period January 1984 through June 1995:

a) If your gas is sold at the wellhead under an arm's-length contract, your gross proceeds determines the value.

b) If your gas is sold at the wellhead under a non-arm's-length contract or a no sale situation, you must use the gas valuation benchmarks to determine the value.

c) The unprocessed gas value is the greater of:

- the value calculated in a or b above, as applicable, or the major portion price shown on Enclosure 1.

2. Calculate the **processed gas value** for the period January 1984 through June 1995:

a) If your gas is processed under an arm's-length contract, the processed value is your gross proceeds for the combined value of

- the residue gas,
- the gas plant products, and
- the condensate recovered downstream of the point of royalty settlement without resorting to processing,
- less a transportation and processing allowance. (A processing allowance can only be claimed if a processing allowance form has been previously filed with MMS.)

If *Short company name* is unable to obtain the necessary information to perform dual accounting as required by the lease terms, *Short company name* is directed to apply the theoretical dual accounting as explained in the MMS' "Dear Payor" letter dated July 27, 1992 (Enclosure 4). MMS has provided a worksheet for both actual and theoretical dual accounting calculations and a diskette with a Microsoft Excel worksheet in order to assist *Short company name* in completing dual accounting calculations (Enclosure 8). An example of the dual accounting calculations is shown in Enclosure 9. If needed, MMS can provide assistance in completing these calculations.

c) The value of the processed gas is the greater of: the combined value of the processed gas calculated in a or b above, as applicable, or the combined value of:

- the residue gas using the major portion price in Enclosure 1,
- the gas plant products using the Mt. Belvieu, Texas average spot price as shown in Enclosure 7 as the comparable contract price,

- the condensate based on the gross proceeds under the arm's-length contracts,
- less any transportation or processing allowances.

3. To comply with the dual accounting requirement, the value for royalty purposes is the greater of:

   - the unprocessed gas value (determined in Step No. 1),
   - the processed gas value (determined in Step No. 2), or
   - your gross proceeds.

4. To determine the royalty due compare the greater value determined in Step No. 3 above to the values *Short company name* reported to MMS on Form MMS-2014 from **January 1984 through June 1995**. All such redeterminations are to be documented in the format shown in Enclosure 10. Please identify and document with copies of contracts or lease settlement statements, any differences you feel are not valid.

Payment Instructions

Please be aware of the following when paying the additional royalties pertaining to major portion and dual accounting:

- Your payments should be made in accordance with the regulations at 30 CFR § 218.51 (1996), and accompanied by an appropriately completed green Form MMS-2014 (Enclosure 11). You will be in compliance with the order only if your payment and a copy of a properly completed green Form MMS-2014 is mailed to:

  Jicarilla Apache Tribe
  P.O. Box 2053
  Albuquerque, NM 87103

- The completed original green Form MMS-2014 and a copy of your payment should be mailed to:

  Minerals Management Service
  Royalty Valuation Division
  P.O. Box 5810
  Denver, Colorado 80127-5810

- If you have questions on the completion of the Form MMS-2014, please contact your Reports

Branch representative at (800) 525-0309 or (303) 231-3288. If you are not currently a royalty payor to MMS please contact Joseph Cornellisson at (303) 275-7239 for further instructions.

- For additional royalties, you must use adjustment reason code 49 when you report your additional royalties on Form MMS-2014. This adjustment reason code must be used for both the reversal line and the re-entry line.

- Appropriate late payment charges pursuant to 30 CFR § 218.102 (1996) will be computed and billed to *Short company name* upon receipt of payment of any additional royalties due.

All documentation supporting your compliance with this order should be retained until MMS completes its follow-up compliance testing. Section 109 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), promulgated in 30 CFR § 241.51 (1996), authorizes MMS to assess civil penalties for failure or refusal to comply with the requirements of FOGRMA or any statute, regulation, rule, order, lease, or permit. Consequently, your failure to comply with the terms of this order may be considered a violation pursuant to 30 CFR § 241.51 (1996) and could subject you to appropriate penalties as provided therein.

Appeal Rights

You have the right to appeal in accordance with the provisions of 30 CFR 290 (1996). A copy of the Appeals Procedures and Bonding Requirements is attached (Enclosure 12).

In accordance with the provisions of 30 CFR § 243.2 (1996), compliance with this order will be suspended by reason of an appeal having been taken.

If you have any comments or questions concerning this request, contact Joseph Cornellisson at (303) 275-7239.

Sincerely,

Deborah Gibbs Tschudy
Chief, Royalty Valuation Division

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September 29, 1997

MMS-RVD-OG
Mail Stop 3152

CERTIFIED MAIL--
RETURN RECEIPT REQUESTED

Name
Company
Address
City, State, Zip

Dear Name

In carrying out the trust responsibility of the United States in the administration of Indian oil and gas leases, the Minerals Management Service (MMS) has long recognized the primacy of the lease terms. As a royalty payor on Jicarilla Apache Indian Tribal leases, you are obligated to comply with Section 3(c) **Rental and royalty**, of the Indian lease terms. More specifically, the regulations state that major portion analysis for oil and gas and dual accounting for gas (accounting for comparison) must be performed in determining the value of production for royalty purposes. (Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.)

For major portion, Federal Regulations (25 CFR § 211.13 (1996)) state:

> During the period of supervision, "value" for the purposes of the lease may, in the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the supervisor.

This requirement is also embodied in the gas valuation regulations found at 30 CFR §§ 206.172 and 206.173 (1996).

Dual accounting requirements are specified by Indian lease terms and Federal regulations found

at 25 CFR § 211.13 (1996) which state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that requires the lessee to compute royalties based on the highest value resulting from three separate computations: (1) the value of the wet gas stream at the wellhead adjusted for Btu content (as determined under 30 CFR § 206.172 (1996)), (2) the value of the separate components after processing and after reducing the values of the liquids to reflect the manufacturing allowance (as determined under 30 CFR § 206.173 (1996)), and (3) gross proceeds accruing to the lease. (After March 1, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR § 206.176 through 206.179 (1996)).

Major Portion

MMS has performed major portion analyses for natural gas production from Jicarilla Apache leases for the period **January 1984 through June 1995**. We have used gas sales data reported by the Jicarilla Apache Tribe (Jicarilla Apache) under their Royalty-in-Kind (RIK) program to determine major portion prices for the Jicarilla Apache Indian Reservation (Reservation) by production month. We have determined that the Jicarilla Apache sold the majority of their RIK production based on the Maximum Lawful Price (MLP) as set by the Natural Gas Policy Act (NGPA) in the following categories:

102 New natural gas	103 New onshore production
104 Flowing gas	104 Replacement gas
105 Existing intrastate	108 Stripper gas
109 Other gas	

Enclosure 1 provides a list of major portion prices to be used in the dual accounting calculation. These prices are based on the prices received under the Jicarilla Apache RIK contract and are shown by NGPA category by month. Enclosure 2 provides a list of your accounting identification (AID) numbers for the Reservation. If you are not responsible for payment of royalties for the lease numbers in Enclosure 2 between January 1984 and June 1995, please identify the responsible party and the date your responsibility ended.

NOTE: The following section entitled Dual Accounting pertain to both those payors that stated they did or did not perform dual accounting. The final letter will be modified for each payor

Dual Accounting - did perform

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 3-6), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1996).

MMS has determined that the Jicarilla Apache lease terms require dual accounting (Section 3(c) entitled "Rental and Royalty"). MMS issued an order (September 29, 1995) to (*Short company name*) to provide a declaration of policy on dual accounting. On your response, you stated that the company did perform dual accounting on the Indian leases for which *Short company name* is a royalty payor. A review of sample months show that your dual accounting calculations were based on prices less than major portion prices shown in Enclosure 1. As a result, additional royalties may be due.

Dual Accounting - Did not perform

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 3-6), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1996).

MMS issued an order (September 29, 1995) to (*Short company name*) to provide a declaration of policy on dual accounting. On your response, you stated that the company did not perform dual accounting on the Indian leases for which *Short company name* is a royalty payor. MMS has determined that the Jicarilla Apache lease terms require dual accounting (Section 3(c) entitled "Rental and Royalty"). As a result, additional royalties may be due

Order to Perform

Therefore, in order to comply with regulations and lease terms, **within 90 days of receipt** of this letter, *Short company name* is ordered to perform the following:

1. Please compare the values shown on Enclosure 1 to the values *Short company name* reported to MMS on Form MMS-2014 from **January 1984 through June 1995**. From January 1984 through June 1995, use the higher of your gross proceeds or the price

shown in Enclosure 1 in the calculation described in Step (2). Please identify and document with copies of contracts or lease settlement statements, any differences you feel are not valid.

2. Using the higher of the gross proceeds or major portion price please calculate a dual accounting (processed gas, liquids, plus condensate) value and an unprocessed (well head) value, and recalculate royalties due as required in the dual accounting requirements.

   In the dual accounting calculation, the processed gas value includes residue gas values, natural gas liquids values, and condensate values less a processing allowance. (A processing allowance can only be claimed if a processing allowance form has been previously filed with MMS.) MMS has reviewed comparable contract prices and determined that Mt. Belvieu, Texas average spot prices provide a comparable contract price. Therefore, liquids values used in the calculation must be the higher of actual gross proceeds liquids price or the Mt. Belvieu, Texas average spot price as shown in Enclosure 7. For condensate, use your gross proceeds value received.

   If *Short company name* is unable to obtain the necessary information to perform dual accounting as required by the lease terms, *Short company name* is directed to apply the theoretical dual accounting as explained in the MMS' "Dear Payor" letter dated July 27, 1992 (Enclosure 4). MMS has provided a worksheet for both actual and theoretical dual accounting calculations and a diskette with a Microsoft Excel worksheet in order to assist *Short company name* in completing dual accounting calculations (Enclosure 8). An example of the dual accounting calculations is shown in Enclosure 9. If needed, MMS can provide assistance in completing these calculations.

3. Compare royalties due as calculated in step (2) above to royalties previously paid for each month and pay any additional royalties due. All such redeterminations are to be documented in the format shown in Enclosure 10.

Payment Instructions

Please be aware of the following when paying the additional royalties pertaining to major portion and dual accounting:

- Your payments should be made in accordance with the regulations at 30 CFR § 218.51 (1996), and accompanied by an appropriately completed green Form MMS-2014 (Enclosure 11). You will be in compliance with the order only if your payment and a copy of a properly completed green Form MMS-2014 is mailed to:

Jicarilla Apache Tribe
P.O. Box 2053
Albuquerque, NM 87103

- The completed original green Form MMS-2014 and a copy of your payment should be mailed to:

Minerals Management Service
Royalty Valuation Division
P.O. Box 5810
Denver, Colorado 80127-5810

- If you have questions on the completion of the Form MMS-2014, please contact your Reports Branch representative at (800) 525-0309 or (303) 231-3288. If you are not currently a royalty payor to MMS please contact Joseph Cornellisson at (303) 275-7239 for further instructions.

- For additional royalties, you must use adjustment reason code 49 when you report your additional royalties on Form MMS-2014. This adjustment reason code must be used for both the reversal line and the re-entry line.

- Appropriate late payment charges pursuant to 30 CFR § 218.102 (1996) will be computed and billed to *Short company name* upon receipt of payment of any additional royalties due.

All documentation supporting your compliance with this order should be retained until MMS completes its follow-up compliance testing. Section 109 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), promulgated in 30 CFR § 241.51 (1996), authorizes MMS to assess civil penalties for failure or refusal to comply with the requirements of FOGRMA or any statute, regulation, rule, order, lease, or permit. Consequently, your failure to comply with the terms of this order may be considered a violation pursuant to 30 CFR § 241.51 (1996) and could subject you to appropriate penalties as provided therein.

Appeal Rights

You have the right to appeal in accordance with the provisions of 30 CFR 290 (1996). A copy of the Appeals Procedures and Bonding Rwquirements is attached (Enclosure 12).

In accordance with the provisions of 30 CFR § 243.2 (1996), compliance with this order will be suspended by reason of an appeal having been taken.

If you have any comments or questions concerning this request, contact Joseph Cornellisson at (303) 275-7239.

Sincerely,

Deborah Gibbs Tschudy
Chief, Royalty Valuation Division

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November 14, 1997

MMS-RVD-OG
Mail Stop 3152

CERTIFIED MAIL--
RETURN RECEIPT REQUESTED

Name
Company
Address
City, State, Zip

Dear Name

In carrying out the trust responsibility of the United States in the administration of Indian oil and gas leases, the Minerals Management Service (MMS) has long recognized the primacy of the lease terms. As a royalty payor on Jicarilla Apache Indian Tribal leases, you are obligated to comply with Section 3(c) **Rental and royalty**, of the Indian lease terms. More specifically, the regulations state that major portion analysis for oil and gas and dual accounting for gas (accounting for comparison) must be performed in determining the value of production for royalty purposes. (Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.)

For major portion, Federal Regulations (25 CFR § 211.13 (1996)) state:

> During the period of supervision, "value" for the purposes of the lease may, in the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the supervisor.

This requirement is also embodied in the gas valuation regulations found at 30 CFR §§ 206.172 and 206.173 (1996).

Dual accounting requirements are specified by Indian lease terms and Federal regulations found

at 25 CFR § 211.13 (1996) which state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater [Emphasis added.]

Dual accounting is defined as a valuation method that requires the lessee to compute royalties based on the greater of: (1) the value of the gas prior to processing (as determined under 30 CFR § 206.172 (1996)), or (2) the combined value of the residue gas and gas plant products resulting from processing the gas (as determined under 30 CFR § 206.173 (1996)), plus the value of any condensate recovered downstream of the point of royalty settlement without resorting to processing (30 CFR § 206.52(1996)). However, the value of production can never be less than the gross proceeds accruing to the lessee (30 CFR §§ 206.172(h) and 206.173(h) (1996)). After March 1, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR §§ 206.176 through 206.179 (1996)).

Major Portion

MMS has performed major portion analyses for natural gas production from Jicarilla Apache Tribal leases for the period **January 1984 through June 1995**. We have verified gas sales data reported by the Jicarilla Apache Indian Tribe (Jicarilla Apache) under their Royalty-in-Kind (RIK) program and used this data to determine major portion prices for the Jicarilla Apache Indian Reservation by production month. We have determined that the Jicarilla Apache sold all of their RIK production based on the prices as set by the Natural Gas Policy Act (NGPA) in the following categories:

102 New natural gas	103 New onshore production
104 Post - 1974 gas	104 1973-1974 Biennium gas
104 Replacement gas	104 Flowing gas
104 Rocky Mountain gas	105 Existing intrastate gas
108 Stripper gas	109 Other gas

Enclosure 1 lists major portion prices. These prices are based on the prices received under the Jicarilla Apache RIK contract and are shown by NGPA category by month. If you are not responsible for payment of royalties between January 1984 and June 1995, please identify the responsible party and the date your responsibility ended.

NOTE: The following section entitled Dual Accounting pertain to both those payors that stated they did or did not perform dual accounting. The final letter will be modified for each payor

Dual Accounting - did perform

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 2-5), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1996).

MMS has determined that the Jicarilla Apache lease terms require dual accounting (Section 3(c) entitled "Rental and Royalty"). MMS issued an order (September 29, 1995 (Enclosure 6)) to (*Short company name*) to provide a declaration of policy on dual accounting. On your response, you stated that the company did perform dual accounting on the Indian leases for which *Short company name* is a royalty payor. A review of sample months show that your dual accounting calculations were based on prices less than major portion prices shown in Enclosure 1. As a result, additional royalties may be due.

Dual Accounting - Did not perform

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 2-5), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1996).

MMS issued an order (September 29, 1995 (Enclosure 6)) to (*Short company name*) to provide a declaration of policy on dual accounting. On your response, you stated that the company did not perform dual accounting on the Indian leases for which *Short company name* is a royalty payor. MMS has determined that the Jicarilla Apache lease terms require dual accounting (Section 3(c) entitled "Rental and Royalty"). As a result, additional royalties may be due.

Order to Perform

In order to comply with the regulations and lease terms, **within 90 days of receipt** of this letter, *Short company name* is ordered to perform the following dual accounting and major portion calculations. Please identify all Jicarilla Apache leases and time periods for which *Short company name* was a payor between **January 1984 and June 1995** and follow the steps below to determine the value of the production for royalty purposes:

1. Calculate the **unprocessed gas value**:

a) The value of your gross proceeds if your gas is sold at the wellhead under an arm's-length contract (30 CFR § 206.172 (1996)).

b) The value determined if your gas is sold at the wellhead under a non-arm's-length contract or a no sale situation (30 CFR § 206.172 (1996)) using **the higher of the appropriate benchmark or gross proceeds.** Sales by affiliates may provide information concerning gross proceeds to the lessee **or** the appropriate benchmark value and thus may be considered in determining royalty values.

c) The value of the unprocessed gas is the greater of

- the value calculated in a or b above, as applicable, or
- the value based on the major portion price shown on Enclosure 1.

2. Calculate the **processed gas value**:

a) If your gas is processed under an arm's-length contract, the processed value is your gross proceeds for the combined value determined under 30 CFR § 206.173 (1996) of

- the residue gas,
- the gas plant products, and
- the condensate recovered downstream of the point of royalty settlement without resorting to processing,
- less a transportation and processing allowance. (After March 1, 1988, a processing allowance can only be claimed if a processing allowance form has been previously filed with MMS.)

b) If your gas is processed under a non-arm's-length contract, the processed value is the combined value determined under 30 CFR § 206.173 (1996) for

- the residue gas,
- the gas plant products, and
- the condensate recovered downstream of the point of royalty settlement without resorting to processing,
- less a transportation and processing allowance. (After March 1, 1988, a processing allowance can only be claimed if a processing allowance form has been previously filed with MMS.)
- (Sales by affiliates may provide information concerning gross proceeds to the lessee **or** the appropriate benchmark value and thus may be considered in determining royalty values.)

If *Short company name* is unable to obtain the necessary information to perform dual accounting as required by the lease terms, *Short company name* is directed to apply the theoretical dual accounting as explained in the MMS' "Dear Payor" letter dated July 27, 1992 (Enclosure 3). MMS has provided a worksheet for both actual and theoretical dual accounting calculations and a diskette with a Microsoft Excel worksheet in order to assist *Short company name* in completing dual accounting calculations (Enclosure 8). An example of the dual accounting calculations is shown in Enclosure 9. If needed, MMS can provide assistance in completing these calculations.

c) The value of the processed gas is the greater of: the combined value of the processed gas calculated in a or b above, as applicable, or the combined value of:

- the residue gas using the major portion price in Enclosure 1,
- the gas plant products using the Mt. Belvieu, Texas average spot price as shown in Enclosure 9 as the comparable contract price,
- the condensate based on the gross proceeds under arm's-length contracts,
- less a transportation and processing allowance. (After March 1, 1988, a processing allowance can only be claimed if a processing allowance form has been previously filed with MMS.)

3. To comply with the dual accounting requirement, the value for royalty purposes is the greater of:

- the unprocessed gas value (determined in Step No. 1),
- the processed gas value (determined in Step No. 2), or
- your gross proceeds.

4. To determine the royalty due compare the greater value in Step No. 3 above to the values *Short company name* reported to MMS on the Report of Sales and Royalty Remittance (Form MMS-2014) and pay any additional royalty amount due. Please document all such redeterminations in a format similiar to those shown in Enclosure 7. Please identify and document with copies of contracts or lease settlement statements, any differences you feel are not valid.

Payment Instructions

Please be aware of the following when paying the additional royalties pertaining to major portion and dual accounting:

- Your payments should be made in accordance with the regulations at 30 CFR § 218.51 (1996), and accompanied by an appropriately completed green Form MMS-2014 (Enclosure 10). You will be in compliance with the order only if your payment and a copy of a properly completed green Form MMS-2014 is mailed to:

Jicarilla Apache Tribe
P.O. Box 2053
Albuquerque, NM 87103

- The completed original green Form MMS-2014 and a copy of your payment should be mailed to:

Minerals Management Service
Royalty Valuation Division, **MS-3152**
P.O. Box 5810
Denver, Colorado 80127-5810

- If you have questions on the completion of the Form MMS-2014, please contact your Reports Branch representative at (800) 525-0309 or (303) 231-3288. If you are not currently a royalty payor to MMS please contact Joseph Cornellisson at (303) 275-7239 for further instructions.

- For additional royalties, you must use adjustment reason code 49 when you report your additional royalties on Form MMS-2014. This adjustment reason code must be used for both the reversal line and the re-entry line.

- Appropriate late payment charges pursuant to 30 CFR § 218.102 (1996) will be computed and billed to *Short company name* upon receipt of payment of any additional royalties due.

All documentation supporting your compliance with this order should be retained until MMS completes its follow-up compliance testing. Section 109 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), promulgated in 30 CFR § 241.51 (1996), authorizes MMS to assess civil penalties for failure or refusal to comply with the requirements of FOGRMA or any statute, regulation, rule, order, lease, or permit. Consequently, your failure to comply with the terms of this order may be considered a violation pursuant to 30 CFR § 241.51 (1996) and could subject you to appropriate penalties as provided therein.

Appeal Rights

You have the right to appeal in accordance with the provisions of 30 CFR 290 (1996). A copy of the Appeals Procedures and Bonding Requirements is attached (Enclosure 11).

In accordance with the provisions of 30 CFR § 243.2 (1996), compliance with this order will be suspended by reason of an appeal having been taken.

If you received a previous order(s) to perform dual accounting on Jicarilla leases, this order modifies the previous order(s). However, if you have appealled the previous dual accounting order(s), you cannot appeal the issue of dual accounting again.

If you have any comments or questions concerning this request, contact Joseph Cornellisson at (303) 275-7239.

Sincerely,

Deborah Gibbs Tschudy
Chief, Royalty Valuation Division

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MMS-RVD-OG
Mail Stop 3152

CERTIFIED MAIL--
RETURN RECEIPT REQUESTED

Name
Company
Address
City, State, Zip

Dear Name:

In carrying out the trust responsibility of the United States in the administration of Indian oil and gas leases, the Minerals Management Service (MMS) has long recognized the primacy of the lease terms. As a royalty payor on Jicarilla Apache Indian Tribal leases, you are obligated to comply with Section 3(c) **Rental and royalty**, of the Indian lease terms. More specifically, the regulations state that a major portion analysis for oil and gas and dual accounting for gas (accounting for comparison) must be performed in determining the value of production for royalty purposes. (Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.)

For major portion, regulations (25 CFR § 211.13(a) (1997)) state:

> During the period of supervision, "value" for the purposes of the lease may, in the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the supervisor.

This requirement is also embodied in the gas valuation regulations found at 30 CFR §§ 206.172 and 206.173 (1997).

Dual accounting requirements are specified by Indian lease terms and regulations found at 25 CFR § 211.13 (1997) which state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater. [Emphasis added.]

Dual accounting is defined as a valuation method that requires the lessee to compute royalties based on the greater of: (1) the value of the gas prior to processing (as determined under 30 CFR § 206.172), or (2) the combined value of the residue gas and gas plant products resulting from processing the gas (as determined under 30 CFR § 206.173), plus the value of any condensate recovered downstream of the point of royalty settlement without resorting to processing (30 CFR § 206.52 (1997)). However, the value of production can never be less than the gross proceeds accruing to the lessee (30 CFR §§ 206.172(h) and 206.173(h) (1997)). After March 1, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR §§ 206.176 through 206.179 (1997)).

Major Portion

MMS has performed major portion analyses for natural gas production from Jicarilla Apache Tribal leases for the period **January 1984 through June 1995**. We have verified gas sales data reported by the Jicarilla Apache Indian Tribe (Jicarilla Apache) under their Royalty-in-Kind (RIK) program and used this data to determine major portion prices for the Jicarilla Apache Indian Reservation by production month. We have determined that the Jicarilla Apache sold all of their RIK production based on the prices as set by the Natural Gas Policy Act (NGPA) in the following categories:

102 New natural gas	103 New onshore production
104 Post-1974 gas	104 1973-1974 Biennium gas
104 Replacement gas	104 Flowing gas
104 Rocky Mountain gas	105 Existing intrastate gas
108 Stripper gas	109 Other gas

Enclosure 1 lists major portion prices. These prices are based on the prices received under the Jicarilla Apache RIK contract and are shown by NGPA category by month/year. If you are not responsible for payment of royalties between January 1984 and June 1995, please identify the responsible party and the date your responsibility ended.

NOTE: The following section entitled Dual Accounting pertain to both those payors that stated they did or did not perform dual accounting. The final letter will be modified for each payor.

Dual Accounting (*Did Perform*)

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 2-5), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1997).

MMS has determined that the Jicarilla Apache lease terms require dual accounting (Section 3(c) entitled "Rental and Royalty"). MMS issued an order (September 29, 1995 (Enclosure 6)) to (*Short company name*) to provide a declaration of policy on dual accounting. On your response, you stated that the company did perform dual accounting on the Indian leases for which *(Short company name)* is a royalty payor. A review of sample months show that your dual accounting calculations were based on prices less than major portion prices shown in Enclosure 1. As a result, additional royalties may be due.

Dual Accounting (*Did not perform*)

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 2-5), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51.

MMS issued an order (September 29, 1995 (Enclosure 6)) to (*Short company name*) to provide a declaration of policy on dual accounting. On your response, you stated that the company did not perform dual accounting on the Indian leases for which (*Short company name*) is a royalty payor. MMS has determined that the Jicarilla Apache lease terms require dual accounting (Section 3(c) entitled "Rental and Royalty"). As a result, additional royalties may be due.

Order to Perform

In order to comply with the regulations and lease terms, **within 90 days of receipt** of this letter, (*Short company name*) is ordered to perform the following dual accounting and major portion calculations. Please identify all Jicarilla Apache leases and time periods for which *(Short company name)* was a payor between **January 1984 and June 1995** and follow the steps below to determine the value of the production for royalty purposes:

1. Calculate the **unprocessed gas value**:

    a. The value of your gross proceeds if your gas is sold at the wellhead under an arm's-length contract (30 CFR § 206.172).

    b. The value determined if your gas is sold at the wellhead under a non-arm's-length contract or a no sale situation (30 CFR § 206.172) using **the higher of the appropriate benchmark or gross proceeds.** Sales by affiliates may provide information concerning gross proceeds to the lessee **or** the appropriate benchmark value and thus may be considered in determining royalty values.

    c. The value of the unprocessed gas is the greater of:

    - The value calculated in a. or b. above, as applicable, or
    - The value based on the major portion price shown on Enclosure 1.

2. Calculate the **processed gas value**:

    a. If your gas is processed under an arm's-length contract, the processed value is your gross proceeds for the combined value (determined under 30 CFR § 206.173 (1997)) of:

    - The residue gas,
    - The gas plant products, and
    - The condensate recovered downstream of the point of royalty settlement without resorting to processing,
    - Less a transportation and processing allowance. (After March 1, 1988, allowances can only be claimed if appropriate allowance forms have been previously filed with MMS.)

    b. If your gas is processed under a non-arm's-length contract, the processed value is the combined value (determined under 30 CFR § 206.173) for:

    - The residue gas,
    - The gas plant products, and
    - The condensate recovered downstream of the point of royalty settlement without resorting to processing,

- Less a transportation and processing allowance. (After March 1, 1988, allowances can only be claimed if appropriate allowance forms have been previously filed with MMS.)
- (Sales by affiliates may provide information concerning gross proceeds to the lessee **or** the appropriate benchmark value and thus may be considered in determining royalty values.)

If (*Short company name*) is unable to obtain the necessary information to perform dual accounting as required by the lease terms, (*Short company name*) is directed to apply the theoretical dual accounting as explained in the MMS's "Dear Payor" letter dated July 27, 1992 (Enclosure 3). MMS has provided a worksheet for both actual and theoretical dual accounting calculations and a diskette (Enclosure 7) with a Microsoft Excel worksheet in order to assist (*Short company name*) in completing dual accounting calculations. An example of the dual accounting calculations is shown in Enclosure 8. If needed, MMS can provide assistance in completing these calculations.

c. The value of the processed gas is the greater of: the combined value of the processed gas calculated in a or b above, as applicable, or the combined value of:

- The residue gas using the major portion price in Enclosure 1,
- The gas plant products using the Mt. Belvieu, Texas, average spot price as shown in Enclosure 9 as the comparable contract price,
- The condensate based on the gross proceeds under arm's-length contracts,
- Less a transportation and processing allowance. (After March 1, 1988, allowances can only be claimed if an appropriate allowance form has been previously filed with MMS.)

3. To comply with the dual accounting requirement, the value for royalty purposes is the greater of:

- The unprocessed gas value (determined in Step No. 1),
- The processed gas value (determined in Step No. 2), or
- Your gross proceeds.

4. To determine the royalty due compare the greater value in Step No. 3 above to the values (*Short company name*) reported to MMS on the Report of Sales and Royalty Remittance (Form MMS-2014) and pay any additional royalty amount due. Please document all such redeterminations in a format similar to those shown in Enclosure 7. Please identify and

document with copies of contracts or lease settlement statements, any differences you feel are not valid.

Payment Instructions

Please be aware of the following when paying the additional royalties pertaining to major portion and dual accounting:

- Your payments should be made in accordance with the regulations at 30 CFR § 218.51, and accompanied by an appropriately completed green Form MMS-2014 (Enclosure 10). You will be in compliance with this Order only if your payment and a copy of a properly completed green Form MMS-2014 is mailed to:

  Jicarilla Apache Tribe
  P.O. Box 2053
  Albuquerque, New Mexico 87103

- The completed original green Form MMS-2014 and a copy of your payment should be mailed to:

  Minerals Management Service
  Royalty Valuation Division, MS-3152
  P.O. Box 5810
  Denver, Colorado 80127-5810

- If you have questions on the completion of the Form MMS-2014, please contact your Reports Branch representative at (800) 525-0309 or (303) 231-3288. If you are not currently a royalty payor to MMS please contact Joseph Cornellisson at (303) 275-7239 for further instructions.

- You must use adjustment reason code 49 when you report your additional royalties on Form MMS-2014. This adjustment reason code must be used for both the reversal line and the re-entry line.

- Appropriate late payment charges pursuant to 30 CFR § 218.102 (1997) will be computed and billed to (*Short company name*) upon receipt of payment of any additional royalties due.

All documentation supporting your compliance with this Order should be retained until MMS completes its follow-up compliance testing. Section 109 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), promulgated in 30 CFR § 241.51, authorizes MMS to assess civil penalties for failure or refusal to comply with the requirements of FOGRMA or any statute, regulation, rule, order, lease, or permit. Consequently, your failure to comply with the terms of this Order may be considered a violation pursuant to 30 CFR § 241.51 and could subject you to appropriate penalties as provided therein.

Appeal Rights

You have the right to appeal in accordance with the provisions of 30 CFR 290 (1997). A copy of the Appeals Procedures and Bonding Requirements is attached (Enclosure 11).

In accordance with the provisions of 30 CFR § 243.2 (1997), compliance with this Order will be suspended by reason of an appeal having been taken.

If you received a previous order to perform dual accounting on Jicarilla leases, this Order modifies the previous order. However, if you have appealed the previous dual accounting order, you cannot appeal the issue of dual accounting again to MMS.

If you have any comments or questions concerning this request, contact Joseph Cornellisson at (303) 275-7239.

Sincerely,

Deborah Gibbs Tschudy
Chief, Royalty Valuation Division

Enclosures

bcc: RM File:
RM Chron/DC
RM Chron/Lakewood
RVD (2)
O&G (2)

LMS:RMP/RVD:MS-3152:JCornellisson:gms:275-7239:11/19/97:oang:cornell:jicarilla:
mpdav6k.ord
Finalized:gms:11/20/97

ENCLOSURE 2

MMS-RVD-OG
Mail Stop 3152

CERTIFIED MAIL--
RETURN RECEIPT REQUESTED

Name
Company
Address
City, State, Zip

Dear Name:

In carrying out the trust responsibility of the United States in the administration of Indian oil and gas leases, the Minerals Management Service (MMS) has long recognized the primacy of the lease terms. As a royalty payor on Jicarilla Apache Indian Tribal leases, you are obligated to comply with Section 3(c) **Rental and royalty**, of the Indian lease terms. More specifically, the regulations state that a major portion analysis for oil and gas and dual accounting for gas (accounting for comparison) must be performed in determining the value of production for royalty purposes. (Where the specific provisions of a lease are inconsistent with these regulations, then the lease agreement shall govern to the extent of that inconsistency.)

For major portion, regulations (25 CFR § 211.13(a) (1997)) state:

> During the period of supervision, "value" for the purposes of the lease may, in the discretion of the Secretary of the Interior, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the supervisor.

This requirement is also embodied in the gas valuation regulations found at 30 CFR §§ 206.172 and 206.173 (1997).

Dual accounting requirements are specified by Indian lease terms and regulations found at 25 CFR § 211.13 (1997) which state:

> In determining the value for royalty purposes of products, such as natural gasoline, that are derived from treatment of gas, a reasonable allowance for the cost of manufacture shall be made, such allowance to be two-thirds of the value of the marketable product unless otherwise determined by the Secretary of the Interior on application of the lessee or on his own initiative, and that royalty will be computed on the value of gas or casinghead gas, or on the products thereof (such as residue gas, natural gasoline, propane, butane, etc.), whichever is the greater. [Emphasis added.]

Dual accounting is defined as a valuation method that requires the lessee to compute royalties based on the greater of: (1) the value of the gas prior to processing (as determined under 30 CFR § 206.172), or (2) the combined value of the residue gas and gas plant products resulting from processing the gas (as determined under 30 CFR § 206.173), plus the value of any condensate recovered downstream of the point of royalty settlement without resorting to processing (30 CFR § 206.52 (1997)). However, the value of production can never be less than the gross proceeds accruing to the lessee (30 CFR §§ 206.172(h) and 206.173(h) (1997)). After March 1, 1988, if royalties are paid pursuant to the processed gas valuation method, the requirements to submit appropriate allowance forms prior to claiming transportation and/or processing allowances must be met. (See 30 CFR §§ 206.176 through 206.179 (1997)).

Major Portion

MMS has performed major portion analyses for natural gas production from Jicarilla Apache Tribal leases for the period **January 1984 through June 1995**. We have verified gas sales data reported by the Jicarilla Apache Indian Tribe (Jicarilla Apache) under their Royalty-in-Kind (RIK) program and used this data to determine major portion prices for the Jicarilla Apache Indian Reservation by production month. We have determined that the Jicarilla Apache sold all of their RIK production based on the prices as set by the Natural Gas Policy Act (NGPA) in the following categories:

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Enclosure 1 lists major portion prices. These prices are based on the prices received under the Jicarilla Apache RIK contract and are shown by NGPA category by month/year. If you are not responsible for payment of royalties between January 1984 and June 1995, please identify the responsible party and the date your responsibility ended.

NOTE: The following section entitled Dual Accounting pertain to both those payors that stated they did or did not perform dual accounting. The final letter will be modified for each payor.

<u>Dual Accounting</u> (*Did Perform*)

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 2-5), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51 (1997).

MMS has determined that the Jicarilla Apache lease terms require dual accounting (Section 3(c) entitled "Rental and Royalty"). MMS issued an order (September 29, 1995 (Enclosure 6)) to (*Short company name*) to provide a declaration of policy on dual accounting. On your response, you stated that the company did perform dual accounting on the Indian leases for which *(Short company name)* is a royalty payor. A review of sample months show that your dual accounting calculations were based on prices less than major portion prices shown in Enclosure 1. As a result, additional royalties may be due.

<u>Dual Accounting</u> (*Did not perform*)

By "Dear Payor" letters dated September 30, 1988; July 27, 1992; February 2, 1993; and February 10, 1995 (Enclosures 2-5), MMS emphasized the requirement to perform dual accounting with notice that failure to comply with Indian lease terms and the regulations applicable to dual accounting would subject payors to enforcement actions by MMS, including civil penalties as provided by 30 CFR § 241.51.

MMS issued an order (September 29, 1995 (Enclosure 6)) to (*Short company name*) to provide a declaration of policy on dual accounting. On your response, you stated that the company did not perform dual accounting on the Indian leases for which (*Short company name*) is a royalty payor. MMS has determined that the Jicarilla Apache lease terms require dual accounting (Section 3(c) entitled "Rental and Royalty"). As a result, additional royalties may be due.

<u>Order to Perform</u>

In order to comply with the regulations and lease terms, **within <u>90</u> days of receipt** of this letter, (*Short company name*) is ordered to perform the following dual accounting and major portion calculations. Please identify all Jicarilla Apache leases and time periods for which (*Short company name)* was a payor between **January 1984 and June 1995** and follow the steps below to determine the value of the production for royalty purposes:

1. Calculate the **unprocessed gas value**:

   a. The value of your gross proceeds if your gas is sold at the wellhead under an arm's-length contract (30 CFR § 206.172).

   b. The value determined if your gas is sold at the wellhead under a non-arm's-length contract or a no sale situation (30 CFR § 206.172) using **the higher of the appropriate benchmark or gross proceeds.** The **first** arm's-length sale may be considered in determining the gross proceeds value. MMS may examine transactions by sales to affiliates in order to determine gross proceeds or the appropriate benchmark value.

   c. The value of the unprocessed gas is the greater of:

      - The value calculated in a. or b. above, as applicable, or
      - The value based on the major portion price shown on Enclosure 1.

2. Calculate the **processed gas value**:

   a. If your gas is processed under an arm's-length contract, the processed value is your *gross proceeds for the combined value (determined under 30 CFR § 206.173 (1997))* of:

      - The residue gas,
      - The gas plant products, and
      - The condensate recovered downstream of the point of royalty settlement without resorting to processing,
      - Less transportation and/or processing allowance(s). These allowances shall consist of the reasonable actual costs incurred. (After March 1, 1988, allowances can only be claimed if appropriate allowance forms have been previously filed with MMS.)

   b. If your gas is processed under a non-arm's-length contract, the processed value is the combined value (determined under 30 CFR § 206.173) for:

      - The residue gas,
      - The gas plant products, and
      - The condensate recovered downstream of the point of royalty settlement without resorting to processing,

- Less transportation and/or processing allowance(s). These allowances shall consist of the reasonable actual costs incurred. (After March 1, 1988, allowances can only be claimed if appropriate allowance forms have been previously filed with MMS.)
- (The **first** arm's-length sale may be considered in determining the gross proceeds value. MMS may examine transactions by sales to affiliates in order to determine gross proceeds or the appropriate benchmark value.)

If (*Short company name*) is unable to obtain the necessary information to perform dual accounting as required by the lease terms, (*Short company name*) is directed to apply the theoretical dual accounting as explained in the MMS's "Dear Payor" letter dated July 27, 1992 (Enclosure 3). MMS has provided a worksheet for both actual and theoretical dual accounting calculations and a diskette (Enclosure 7) with a Microsoft Excel worksheet in order to assist (*Short company name*) in completing dual accounting calculations. An example of the dual accounting calculations is shown in Enclosure 8. If needed, MMS can provide assistance in completing these calculations.

c. The value of the processed gas is the greater of: the combined value of the processed gas calculated in a or b above, as applicable, or the combined value of:

- The residue gas using the major portion price in Enclosure 1,
- The gas plant products using the Mt. Belvieu, Texas, average spot price as shown in Enclosure 9 as the comparable contract price,
- The condensate based on the gross proceeds under arm's-length contracts,
- Less transportation and/or processing allowance(s). These allowances shall consist of the reasonable actual costs incurred. (After March 1, 1988, allowances can only be claimed if an appropriate allowance form has been previously filed with MMS.)

3. To comply with the dual accounting requirement, the value for royalty purposes is the greater of:

- The unprocessed gas value (determined in Step No. 1),
- The processed gas value (determined in Step No. 2), or
- Your gross proceeds.

4. To determine the royalty due compare the greater value in Step No. 3 above to the values (*Short company name*) reported to MMS on the Report of Sales and Royalty Remittance (Form MMS-2014) and pay any additional royalty amount due. Please document all such

redeterminations in a format similar to those shown in Enclosure 7. Please identify and clearly document with copies of contracts or lease settlement statements, any differences you feel are not valid such as a major portion price that is greater than the maximum lawful price you received under an arm's-length contract.

Payment Instructions

Please be aware of the following when paying the additional royalties pertaining to major portion and dual accounting:

- Your payments should be made in accordance with the regulations at 30 CFR § 218.51, and accompanied by an appropriately completed green Form MMS-2014 (Enclosure 10). You will be in compliance with this Order only if your payment and a copy of a properly completed green Form MMS-2014 is mailed to:

  Jicarilla Apache Tribe
  P.O. Box 2053
  Albuquerque, New Mexico 87103

- The completed original green Form MMS-2014 and a copy of your payment should be mailed to:

  Minerals Management Service
  Royalty Valuation Division, MS-3152
  P.O. Box 5810
  Denver, Colorado 80127-5810

- If you have questions on the completion of the Form MMS-2014, please contact your Reports Branch representative at (800) 525-0309 or (303) 231-3288. If you are not currently a royalty payor to MMS please contact Joseph Cornellisson at (303) 275-7239 for further instructions.

- You must use adjustment reason code 49 when you report your additional royalties on Form MMS-2014. This adjustment reason code must be used for both the reversal line and the re-entry line.

- Appropriate late payment charges pursuant to 30 CFR § 218.102 (1997) will be computed and billed to (*Short company name*) upon receipt of payment of any additional royalties due.

All documentation supporting your compliance with this Order should be retained until MMS completes its follow-up compliance testing. Section 109 of the Federal Oil and Gas Royalty

Management Act of 1982 (FOGRMA), promulgated in 30 CFR § 241.51, authorizes MMS to assess civil penalties for failure or refusal to comply with the requirements of FOGRMA or any statute, regulation, rule, order, lease, or permit. Consequently, your failure to comply with the terms of this Order may be considered a violation pursuant to 30 CFR § 241.51 and could subject you to appropriate penalties as provided therein. Furthermore, failure to comply can also result in lease cancellation as provided for in 30 CFR § 241.20 (b) which state:

> Failure be the lessee, operator, revenue playor, or other authorized person, or party to complete the necessary remedial action within the time and in the maneer prescribed by the notice may subject lease to cancellation proceedings pursuant to . . . or provisions of 25 CFR for Indian leases.

The provisions of 25 CFR § 211.20 state:

> Failure of the lessee to comply with any provision of the lease, of the operating regulations, of the regulations in this part, order of the superintendent or his representative, shall subject the lease to cancellation by the Secretary of the Interior or the lessee to a penalty of not more than $500 per day for each and every day the terms of the lease, the regualtions, or such orders are violated; or to both such penalty and cancelllation.

Appeal Rights

You have the right to appeal in accordance with the provisions of 30 CFR 290 (1997). A copy of the Appeals Procedures and Bonding Requirements is attached (Enclosure 11).

In accordance with the provisions of 30 CFR § 243.2 (1997), compliance with this Order will be suspended by reason of an appeal having been taken.

If you received a previous order to perform dual accounting on Jicarilla leases, this Order modifies the previous order to the extent of the prices used in the dual accounting calculations and/or the time period involved. However, if you have previously appealed the requirement of dual accounting, you cannot appeal the issue of dual accounting again to MMS.

If you have any comments or questions concerning this request, contact Joseph Cornellisson at (303) 275-7239.

Sincerely,

Deborah Gibbs Tschudy
Chief, Royalty Valuation Division

Enclosures

bcc: RM File:
RM Chron/DC
RM Chron/Lakewood
RVD (2)
O&G (2)

LMS:RMP/RVD:MS-3152:JCornellisson:gms:275-7239:11/19/97:oang:cornell:jicarilla:
mpdav6k.ord
Finalized:gms:11/20/97