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<u>VIA TELEFAX (303) 231-3194</u>

Mr. David S. Guzy
Chief
Rules and Procedures Staff
Minerals Management Service
Royalty Management Program
P.O. Box 25165, MS 3101
Denver, CO 80225-0165

Re: **Comments of the Jicarilla Apache Tribe on the Proposed Amendments to Transportation Allowance Regulations for Federal and Indian Leases to Specify Allowable Costs and Related Amendments to Gas Valuation Regulations, 30 C.F.R. Part 206**

Dear Mr. Guzy:

The following comments are submitted to the Minerals Management Service ("MMS") on behalf of the Jicarilla Apache Tribe ("Tribe") with respect to the proposed transportation allowance regulations as published in the Federal Register. It is important to observe at the outset that in the recent past Indian gas valuation regulations have been promulgated and published. These regulations are separate from the federal gas valuation regulations in recognition of the very distinct differences in federal oil and gas leases and tribal oil and gas leases. Those distinct differences are equally relevant to rules governing transportation allowances. As a general proposition in light of this difference, as recognized by MMS in promulgating separate valuation regulations, it is respectfully suggested that separate regulations dealing with transportation allowances for Indian oil and gas leases be considered.

In order to understand the full import of these differences, references should be made to the standard federal oil and gas lease of the Department of Interior's Bureau of Land Management form 3120-7 (February 1977) as contrasted with the standard Bureau of Indian

Affairs Oil and Gas Mining Lease for Tribal Indian Lands, form 5-157 (July 1964). Paragraph 3(c) of the tribal oil and gas lease has no provision in it for any allowance or deduction for transportation. The specific reference to allowances are limited to an allowance for the cost of manufacture of marketable products such as propane, butane, etc. In addition, as the duties of the United States Department of Interior have been interpreted by the United States Court of Appeals for the Tenth Circuit in the Supron case brought by the Tribe, the obligation of the United States in supervising these leases is to maximize the monetary return under the leases. Therefore, it is critical in compliance with the maximization of revenue duties of the Secretary of Interior that no allowance of any kind be permitted unless it is clearly demonstrated to be in the economic interest of the lessor tribe. This obligation should be contrasted with the very different royalty provision that is contained in the federal leases. For example, in paragraph 4, under the standard of the Bureau of Land Management lease referred to above, it is provided that:

> rentals or minimum royalties may be waived, suspended, or reduced; and royalties on the entire leasehold or any portion thereof segregated for royalty purpose may be reduced if the Secretary of Interior finds that, for the purpose of encouraging the greatest ultimate recovery of oil or gas and in the interest of conservation of natural resources, it is necessary, in his judgment, to do so in order to promote development, or because the lease cannot be successfully operated under the terms fixed herein.

There is no similar provision in a tribal lease that would permit the Secretary of Interior to waive or reduce the collection of royalty. In fact, the Secretary of Interior is limited in subparagraph 3(g) that in implementing regulations to govern tribal leases, the Secretary of Interior cannot provide a "regulation . . . [that] shall effect a change in rate of royalty or annual rental herein specified without the written consent of the parties to this lease." This very real difference is very important to keep in mind in conjunction with the Secretary of Interior's trust responsibilities as interpreted by the Tenth Circuit in the Supron decision.

With these general observations as a background for review of the proposed rule and the impact as described in the FERC Order 636 proposed rule analysis required by the Department of Interior-Departmental Manual Part 512, Chapter 2, the following should be observed and considered by the agency.

Tribal oil and gas leases contemplate in the form lease, not meaningfully revised since 1964, that the sale of the product would occur at the wellhead. Indeed, for many years, gas sales in fact took place at the wellhead. With the articulation of FERC Order 636, a change in the gas transportation and marketing has occurred. This does not, however, automatically require a change in effect in the lease terms of tribal oil and gas leases. Nevertheless, for many years

MMS has imposed on tribal and allotted oil and gas leases a deduction permitted to the producer for transportation. Given the Secretary of Interior's trust responsibility and the fact that no such allowance or deduction is expressly permitted in the standard Indian oil and gas lease, any amounts permitted as a deduction or allowance for transportation should be scrupulously examined and limited to the minimum amount necessary in the economic best interest of the lessor. Therefore, consideration being given to permit the lessee to use a FERC approved tariff presumptively for one's transportation allowance is not acceptable. It is fairly common knowledge that FERC approved tariffs are not, in fact, the actual and reasonable cost of transportation that are paid by the producer. Therefore, the fact that a FERC tariff has been approved and that companies must go through comprehensive filing procedures does not answer the underlying question of whether any particular amount has been paid by the lessee. Nor does the fact of a FERC approved tariff, which includes a number of component elements which are not narrowly for the purpose of moving gas to the point of sale, allow for a reasonable basis upon which a FERC approved tariff can be utilized for purposes of allowing a deduction from royalties otherwise due to the tribal lessor. The Secretary of Interior should examine each and every component cost item that is claimed to have been paid as a necessary element of transportation and make an independent determination of whether such cost element is actual, reasonable, and necessary to move the gas from the wellhead to the point of sale. In the absence of a satisfactory basis to establish the foregoing, claims for transportation allowance should be presumptively rejected.

In addition, under the existing MMS transportation allowance regulations, there is a fifty percent (50%) transportation ceiling. There is a provision in the proposed transportation allowance regulation that would allow the lessee to exceed fifty percent (50%) as an allowance for transportation. There should not be any circumstances under which such an excessive allowance is permitted because the presumption ought to be that the valuation occurs at the wellhead. In addition, however, the proposed regulations that permit a lessee to apply for a transportation allowance greater than fifty percent (50%) are devoid of any meaningful test that such an application be demonstrated to be in the economic best interest of the lessor tribe. Without tying the application for excessive transportation allowance to the economic best interest of the Tribe and to the maximization of revenue of the Tribe, the Secretary of Interior's trust responsibilities under the Bureau of Indian Affairs ("BIA") standard oil and gas lease form, as interpreted by the Supron court, would be violated. The obvious kinds of justification that may be rational on behalf of the lessee may have no economic benefit to the lessor. The Department of Interior's duties and hence, the regulations with respect to transportation, should be limited to those which benefit the lessor tribe and not the lessee. In contrast, for reasons mentioned above, having the origin in the different lease terms, such excessive transportation allowance may be permissible under a federal oil and gas lease. Hence, the recommendation as a general proposition that separate transportation allowance regulations for Indian leases be considered.

Under the provisions of the proposed transportation allowance regulation that deal with firm service and charges that are paid for such reserved capacity, the MMS procedures currently in place are inadequate to monitor reductions and firm demand charge used to calculate transportation allowances on the MMS form 2014. If MMS is going to consider permitting firm demand charges to be utilized as a transportation allowance basis, it must have in place systems to timely review and audit, if necessary, the actual amount ultimately paid. The justification used in the MMS analysis that because FERC allows certain costs in the basic pipeline transportation rates, MMS considers these actual costs of transportation under existing regulations remains a fantasy in light of numerous examples that have been discussed in the recent past between tribal representatives and MMS staff that clearly demonstrate that the FERC allowed costs were not paid. It is therefore important in the proposed regulations that this fiction not be continued. In examining the MMS so-called economic impact analysis, this fantasy continues to be presented as if it were a rational explanation for permitting continued inclusion in the overall transportation allowance of certain specific FERC included cost elements. The gas research institute fee, for example, has nothing to do with transportation. Simply because MMS has allowed this fee to be included in the transportation allowance in the past and simply because FERC has allowed it does not address the question of whether such a fee has anything to do with the actual transportation of gas. In fact, it does not and should not be permitted to be used as a deduction from amounts due as royalties to tribes.

Similarly, MMS proposes to continue actual or theoretical losses that are permitted under certain circumstances under existing regulations. The rationale for continuing this policy is nothing more than that is the way MMS has treated it in the past and therefore, there should be no substantive change in existing rules. Such an explanation is hardly an economic evaluation as required by the Secretarial Order 3175 as now incorporated into the Departmental Manual requiring an economic impact analysis prior to decisions of the Department of Interior which may have an impact on tribal resources. Without going into each and every element as articulated in MMS' economic impact analysis suffice it to say that this same deficiency of "economic best interest of the tribe finding" combined with an explanation that this is the way that the particular matter is currently treated, suggests very strongly that the obligations of the Department of Interior to ensure that tribal non-renewable resources receive the maximum revenue for their disposition has not been taken seriously by the MMS. Rather, there appears to be a desire for uniformity of regulations so that the administrative tasks are minimized. The conclusion that is reached by the Department of Interior to the effect that a publication of the proposed rule will meet MMS' goal of providing certainty, clarity, and consistency on royalty issues so that royalties are reported right the first time is, by itself, not an adequate basis to reduce tribal royalties by allowing the inclusion of inappropriate elements of transportation allowances. The only mention made in the conclusion to the economic impact analysis is that "the rule will likely have a neutral or beneficial impact on Indian royalties." The narrative which precedes this conclusion is devoid of any real economic demonstration of favorable impact to tribal lessors by virtue of these new proposed transportation allowances.

It is, therefore, respectfully suggested that the Department of Interior has not complied with the substantive requirements of Part 512, Chapter 2 of the Departmental Manual and the larger responsibilities of the Department of Interior, as articulated by the Supron court, in these proposed transportation regulations. It is therefore recommended that MMS exclude tribal leases from the existing proposed transportation allowances as published in recognition of the differential and underlying leases as well as the different legal obligations of the Secretary of Interior, as expressed above. These differences are of primary importance when the allowances go towards directly reducing otherwise due tribal royalties to the extent they are permitted. The separate valuation regulations for Indian gas and the likelihood that separate valuation regulations for Indian oil will be forthcoming, MMS should recognize the propriety of treating federal oil and gas leases differently from tribal oil and gas leases. The narrower permissibility of transportation allowances that should be permitted, if at all, under tribal oil and gas leases are not reflected in the proposed transportation allowance regulations.

For all these reasons, the Jicarilla Apache Tribe strongly recommends to the Director of the Minerals Management Service and Secretary of Interior that separate transportation allowance regulations for Indian oil and gas leases be considered that more accurately reflect the nature of the Secretary of Interior's obligation under Indian oil and gas leases as interpreted by the Supron court.

Respectfully yours,

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