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MMS Reports Successes, Challenges in Royalty-in-Kind Projects

Internal Minerals Management Service (MMS) reports finalized today conclude that two “Royalty-in-Kind” (RIK) pilot projects conducted with the states of Wyoming and Texas resulted in increased revenues of nearly 3 percent and 1 percent respectively, and improved administrative efficiencies. According to the MMS, the bureau is now also looking into developing better performance measures to further advance RIK business activity.

“The Royalty-in-Kind program is providing solid benefits to American taxpayers and the nation,” said MMS Director Johnnie Burton, “yet more work remains to be done to fully assess the revenue impacts of the program. We intend to pursue program improvements to achieve consistent results.”

During the past decade, MMS has conducted several feasibility studies and pilot projects to determine if taking royalty-in-kind (in the form of product) as opposed to royalty-in-value (cash payments) is in the nation’s best interests. Based on these projects, including the joint sales with the states of Wyoming and Texas, MMS has determined that RIK will be an integral part of its approach to manage mineral royalties, to be used in tandem with royalties in value.

Among the objectives of the effort are to return fair value on the public’s royalty assets, reduce regulatory costs and reporting requirements, shorten the compliance cycle, and improve overall business efficiencies. In addition, taking royalties in-kind in the form of product simplifies audits and can potentially reduce the number of audits performed of royalty-in-value cash payments. In the past, that auditing process for royalty payments could take several years to complete, which is one reason the oil and gas industry generally supports the government’s RIK efforts.

The Wyoming report concludes that the RIK program reduced the period of time that it takes MMS to ensure it has received all royalties due from years to months; that RIK royalty receipts exceeded comparable in-value royalties by approximately \$810,000; and that the process established a foundation for administrative savings for MMS and industry in the future.

The Texas report examined all of the Texas offshore section 8(g) leases participating in the RIK pilot. It found royalty receipts exhibited an uplift of approximately \$997,000, or 1 percent over what would have been collected through royalty-in-value.

Director Burton stressed that the MMS expects to do as well as any other party selling gas and oil at market centers under industry standard contract terms. “Our goal is to get fair market value from RIK sales,” Burton said. She noted that assessments of the RIK program to date indicate that efficiencies are being realized, transaction cycle times are being reduced, and that MMS can expect some RIK revenue uplifts from negotiating favorable transportation and gas processing arrangements because of the size of the Federal royalty portfolio.

The selected use of RIK sales, combined with taking royalty-in-value payments when economics indicate that is the best approach, will help ensure taxpayers receive fair value, Burton noted.

With an eye toward the future, MMS awarded a contract in January 2003 to independent management consulting company Lukens Energy Group of Houston, Texas, to commercially assess the RIK program; recommend improvements, particularly in performance measurement tools and metrics; and make recommendations for future strategic planning. The Lukens’ report was completed in December 2003.

Acting on Lukens’ recommendations, MMS is preparing a five-year RIK Business Plan which is expected to be finalized in May 2004. That plan will include strategic direction, goals, objectives and specific management actions to advance the permanent RIK business activity in the 2004-2008 timeframe.

Copies of the internal RIK pilot reports that have been finalized are available on the MMS web page at: www.mms.gov, under the Royalty-In-Kind section.

Relevant Web Sites:

Minerals Revenue Management royalty-in-kind home page (reports available here)

<http://www.mrm.mms.gov/rikweb/Default.htm>

MMS Home Page

<http://www.mms.gov/>

MMS is the federal agency in the U.S. Department of the Interior that manages the nation's oil, natural gas, and other mineral resources on the Outer Continental Shelf in Federal offshore waters. The agency also collects, accounts for, and disburses mineral revenues from Federal and American Indian lands. Between 1982 and 2003, MMS distributed more than \$135 billion in revenues from onshore and offshore lands, an average of more than \$6 billion per year, to the Nation, States and American Indians. Nearly \$1 billion from those revenues go into the Land and Water Conservation Fund annually for the development of State and Federal park and recreation lands.