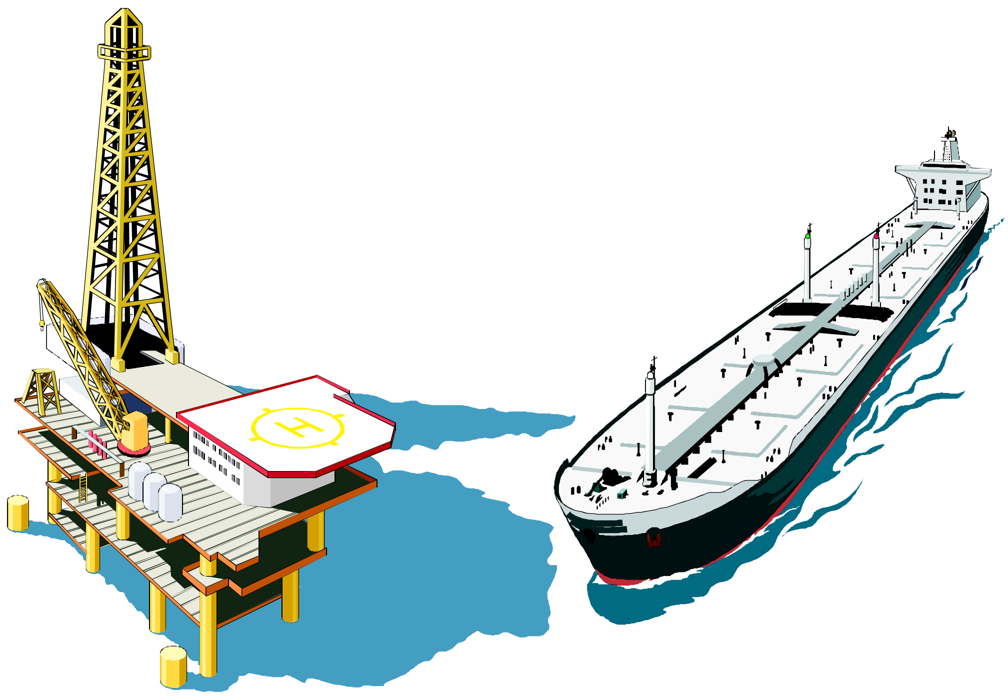
ANNUAL FINANCIAL REPORT OF FISCAL 1996 ACTIVITY



Department of the Interior
Minerals Management Service

January 1997

Preface

It is my pleasure to submit to you this Fiscal Year (FY) 1996 Annual Financial Report of the Minerals Management Service (MMS).

FY 1996 was a very productive year for the MMS. During the year we distributed about $4.7 billion in mineral revenues from leases on Indian lands, and from Federal onshore and offshore leases. We directly administered approximately 25 million acres of Federal offshore lands (active leases). Based on the latest available data, these lands supply about 25 percent of the United States' total gas production and about 15 percent of its total oil production. We also conducted 3 lease sales during the year, with high bids totaling $888 million. Since the inception of the Outer Continental Shelf (OCS) Program, 120 OCS lease sales have been conducted generating more than $113 billion in revenue to the government.

Since our inception in 1982, the MMS has made significant strides in managing the public's resources while eliminating unnecessary burdens on the industry we regulate. However, we realize that we face new challenges and opportunities today that are different from the past. In response to these challenges, we have developed an overall strategic plan to help guide our efforts and give our employees a clear sense of direction in these times of change. The numerous achievements in this report are organized to reference the goals and associated strategies we have set for our mineral revenue collection and offshore minerals management functions.

As an outgrowth of our strategic planning, we are focusing our efforts on finding ways to:

carry out our programs more efficiently and effectively;

improve our level of service both to the regulated community and the public; and

ensure that we treat our various constituencies as partners in decisions that could affect them.

If you want to know more about the MMS and our many activities, please refer to our Home Page on the World Wide Web (http://www.mms.gov).

Cynthia Quarterman
Director

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United States Department of the Interior

OFFICE OF INSPECTOR GENERAL
Washington, D.C. 20240

FEB - 7 1997

Memorandum

To: Director, Minerals Management Service

From: Robert J. Williams Robert J. Williams
Acting Assistant Inspector General for Audits

Subject: Report on Minerals Management Service Financial Statements for Fiscal Years 1995 and 1996

In accordance with the Chief Financial Officers Act of 1990, we audited the Minerals Management Service's financial statements for the fiscal years ended September 30, 1995, and 1996, as listed in the table of contents of the Service's "Annual Financial Report of Fiscal 1996 Activity." The Minerals Management Service is responsible for these financial statements, and we are responsible for expressing an opinion, based on our audit, on these financial statements.

Our audit was conducted in accordance with the "Government Auditing Standards," issued by the Comptroller General of the United States, and Office of Management and Budget Bulletin 93-06, "Audit Requirements for Federal Financial Statements," and was completed on January 17, 1997. These audit standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and notes. An audit also includes assessing the accounting principles used and significant estimates made by management. We believe that our audit provides a reasonable basis for our opinion.

We found that the financial statements and accompanying notes present fairly the Minerals Management Service's assets, liabilities, and net position; expenses, revenues, and receipts; changes in net position; and custodial activity. We also found that these financial statements are presented in conformity with the accounting standards and policies described in the notes to the financial statements. Further, the financial information in the supplemental schedules that follow the notes to the financial statements is consistent with the information presented in the financial statements.

As part of our audit, we evaluated the Service's internal control structure, tested the Service's compliance with selected provisions of laws and regulations, and reviewed the financial information presented in the Service's overview. We also reviewed the Service's most recent report required by the Federal Managers' Financial Integrity Act of 1982 and compared it with the results of our evaluation of the Service's internal control structure. However, because of inherent limitations in any system of internal controls, losses, noncompliance, or misstatements may occur and not be detected. We also caution that projecting our evaluations to future periods is subject to the risk that controls or the degree of compliance with the controls may diminish.

We found that the Service's internal control structure in effect on September 30, 1996, was sufficient to safeguard assets against loss from unauthorized use or disposition; ensure that transactions were executed in accordance with laws and regulations; ensure that transactions were properly recorded, processed, and summarized; and provide reasonable assurance that any losses, noncompliance, or misstatements that are material to the financial statements would be detected. In addition, we found that there were no material instances of noncompliance with selected provisions of laws and regulations that we tested, and nothing came to our attention during our audit work to indicate that material noncompliance with such provisions occurred. Further, we found that the financial information in the Service's overview is consistent with the information presented in the financial statements.

Our review of prior Office of Inspector General and General Accounting Office audit reports disclosed that there were no significant unresolved and unimplemented recommendations that affected the Service's financial statements.

Part 1

OVERVIEW OF MINERALS MANAGEMENT SERVICE'S OPERATIONS

Minerals Management Service
Annual Financial Report of Fiscal Year 1996 Activity

Overview

The Minerals Management Service (MMS) was established in 1982 to collect, account for, and disburse revenues from both onshore and offshore minerals production. Additionally, MMS oversees the exploration and development of America's Federal offshore natural gas, oil, and other mineral resources. By consolidating the mineral collection and offshore minerals management functions and associated personnel within a single agency, the MMS has been better able to accomplish its mission and has developed integrated processes to oversee the operation of its programs. Further, consolidation has afforded economies of scale, thus saving taxpayer dollars and providing for improved service to customers.

Although the MMS is both relatively new and relatively small, we provide major energy and fiscal benefits to the public that include:

> Administering 25 million acres of the OCS, which, based on the latest available data, supplied over 25 percent of the natural gas and 15 percent of the oil produced in the United States.
>
> Distributing about $3.6 billion in FY 1996 in royalties, rents, and bonuses from mineral leases on the OCS. This effort provided over $2.5 billion to the Federal and State treasuries; the remainder is distributed to the Land and Water Conservation Fund and the National Historic Preservation Fund.
>
> Distributing over $1 billion in FY 1996 in royalties, rents, and bonuses from onshore mineral leases, of which about $.5 billion is distributed to States, Tribes, and Indian allottees; the remainder is distributed to the Reclamation Fund and the U.S. Treasury.

The MMS's responsibilities are performed by our Offshore Minerals Management Program (OMMP) and our Royalty Management Program (RMP) organizations. The OMMP administers the outer continental shelf competitive leasing program and oversees the safe and environmentally sound exploration and production of our nation's offshore natural gas, oil and other mineral resources. The RMP meets its responsibilities by ensuring the efficient, timely and accurate collection and disbursement of revenue from mineral leasing and production due to Indian tribes and allottees, States and the U.S. Treasury.

Overview

These organizations are supported by an Office of Administration and Budget and an Office of Policy and Management Improvement. The MMS administrative financial operations are performed by the Financial Management Division in the Office of Administration and Budget. A chart of our organization is shown in illustration 1.

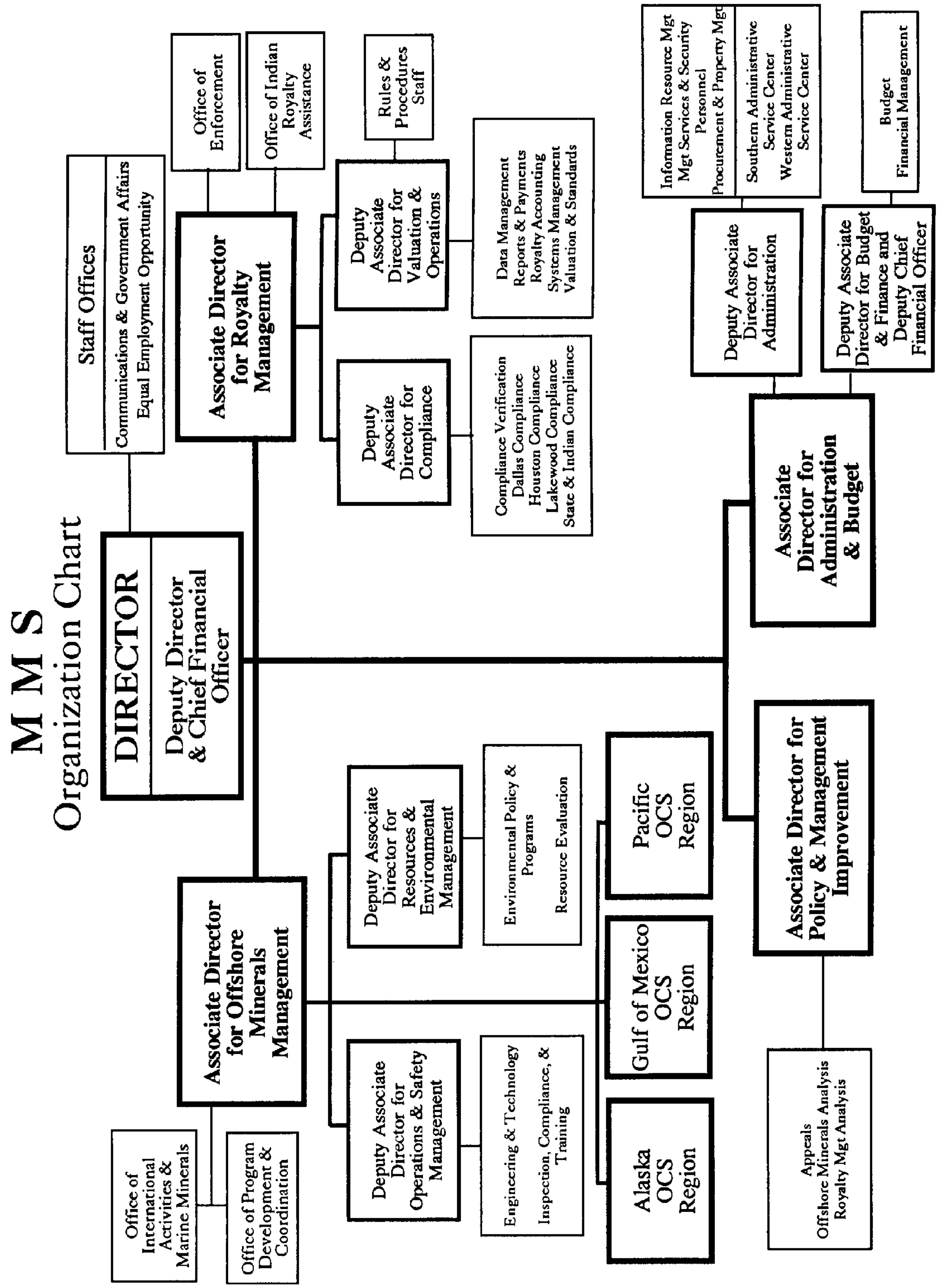
The MMS offices are located throughout the United States; including major offices in the Washington, D.C. area; Lakewood, Colorado; New Orleans, Louisiana; Camarillo, California; and Anchorage, Alaska. The MMS also has compliance (audit) offices and OMM district offices located near the centers of the minerals industry.

The MMS's operations are primarily funded from two appropriations: 1461917 and 14X8370. Additional financial resources, representing less than 8% of MMS's budget, are also obtained from offsetting collections from non-Federal sources.

Our FY 1996 obligations from all funding sources and FTE were allocated as follows:

	Obligations ($000's)	Full-time Equivalent Employment
Offshore Minerals Management	$104,456	864
Royalty Management	68,929	636
General Administration	34,766	249
Total	$208,151	1,749

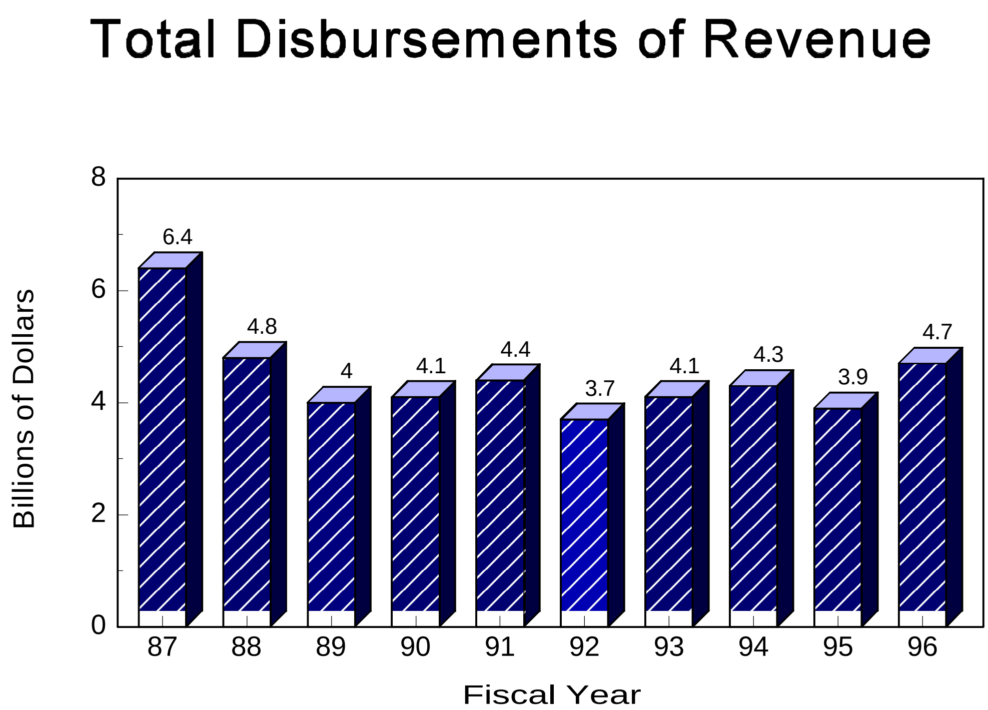
Illustration 1



Overview

The MMS collects mineral receipts from about 112,000 leases which support a broad constituency of 38 States, 42 Tribes, and about 20,000 individual Indian mineral owners.

Disbursements for the last 10 years are shown in the following chart:



Distribution of Mineral Receipts Disbursements

Recipient	Amount ($ in millions)
From OCS activities:	
U.S. Treasury	$2,428
Land & Water Conservation Fund	897
Historic Preservation Fund	150
Coastal States	90
Subtotal	*3,565*
From Onshore Federal activities:	
U.S. Treasury	174
Onshore States	457
Other Federal Agencies	371
Indian Tribes and Allottees [1]	41
Subtotal	*1,043*
Miscellaneous Disbursements	57
TOTAL	**$4,665**

[1] The $41 million disbursed to Indian Tribes and Allottees represents amounts deposited to U.S. Treasury accounts managed by the Bureau of Indian Affairs. An additional $94 million was transferred directly to Indian Tribes and agencies by royalty payors.

Overview

As of October 1, 1996, there were about 5,900 leases under supervision on the OCS encompassing approximately 25 million acres. In FY 1996, these leases supplied an estimated 5,004 trillion cubic feet of natural gas. The volume of crude oil from these leases is estimated to have exceeded 425 million barrels. Based on the latest available final data, this represents 25 percent of all the natural gas produced in the United States and about 15 percent of the Nation's output of oil.

From the OCS program's inception through FY 1996, 120 OCS lease sales have been conducted generating over $113 billion in bonus, rent, and royalty revenue to the Federal Government.

Receipts from the OCS account for the majority of funding from the Land and Water Conservation Fund (LWCF). The LWCF provides funding for the acquisition of Federal recreational lands and for acquisition and development of State and local recreational areas on a matching grant basis. The OCS receipts are the sole source of the Historic Preservation Fund (HPF), which provides grants to States and to the National Trust for Historic Preservation. Both the LWCF and HPF are administered by the National Park Service.

The FY 1996 OCS mineral receipts disbursements of $3.565 billion represent an increase of $823 million from FY 1995 disbursements (OCS receipts account for 76 percent of all MMS mineral receipts). Many factors, including oil and gas consumption, domestic production, foreign imports, world oil prices, the state of the economy, and environmental concerns affect the level of revenues collected by the MMS.

Activities of Note

Royalty Simplification and Fairness Act (RSFA).

On August 13, 1996, the President signed into law the Federal Oil and Gas Royalty Simplification and Fairness Act of 1996. This legislation provides:

> The framework for additional delegations of royalty functions to States subject to Secretarial discretion,
>
> Definitions for enforcement actions,

Certainty for royalty payors with a 7-year statute of limitations for all royalty collections with limitations on industry liability, and a 33-month limit on all administrative appeals,

Equity by requiring payment of interest on overpayments,

Assurance of cost-effective audit and collection activities that encourage continued oil and gas production from marginal properties,

Repeal of the outdated offshore refund requirements and streamlined adjustment procedures.

The MMS has developed a plan to implement the RSFA changes. Implementation will be a very complex process that in many cases will require regulation changes and a large-scale coordinated effort with States, industry, and other DOI agencies. We estimate that full implementation of the act will take 3 years.

Performance Measurement Team (PMT).

During FY 1996, a project action team was formed to advance the state of performance measurement in the MMS. The PMT's objectives are to:

Develop outcome performance measures for the MMS overall.

Develop outcome and output measures relating to RMP and OMMP.

Establish a framework that integrates performance measures with the MMS Strategic Plan and the requirements of the Government Performance and Results Act (GPRA).

Similar teams were also established within RMP and OMMP to develop measures specific to their programs. Numerous outcome and output measures have been identified by these teams and are currently being tested. Where appropriate, these measures are included in this report.

The Royalty Management Program

The MMS Royalty Management Program (RMP) employs 636 Federal staff and 250 contract support personnel. In FY 1996, its operating budget was $68.9 million. Its headquarters is in Lakewood, Colorado, with compliance offices at various major centers of the oil and gas industry.

GOAL

The MMS goal for our mineral revenue collection function is to provide timely, accurate, and cost-effective revenue collection and disbursement services to our customers. To accomplish this goal, we pursue the following strategies:

Assist and encourage royalty payors to submit royalty reports and payments correctly the first time,

Streamline and simplify royalty collection and disbursement processes whenever possible,

Use modern information management tools to improve the royalty collection and disbursement processes,

Involve stakeholders in decision making and make decisions by consensus whenever possible.

In addition to our goal for correct first time reports and payments, we focus on preventing future noncompliance. In each activity, we seek and implement improvements to increase the percentage of mineral revenue from Federal and Indian leases that is paid voluntarily.

The RMP is committed to identifying, resolving, and implementing policies or policy changes more efficiently, reaching consensus on solutions more quickly, and managing approval processes more efficiently. The RMP listens to customers, involves them in decision making, and adjusts processes to improve customer service and satisfaction.

Assisting Royalty Payors to Report and Pay Correctly the First Time.

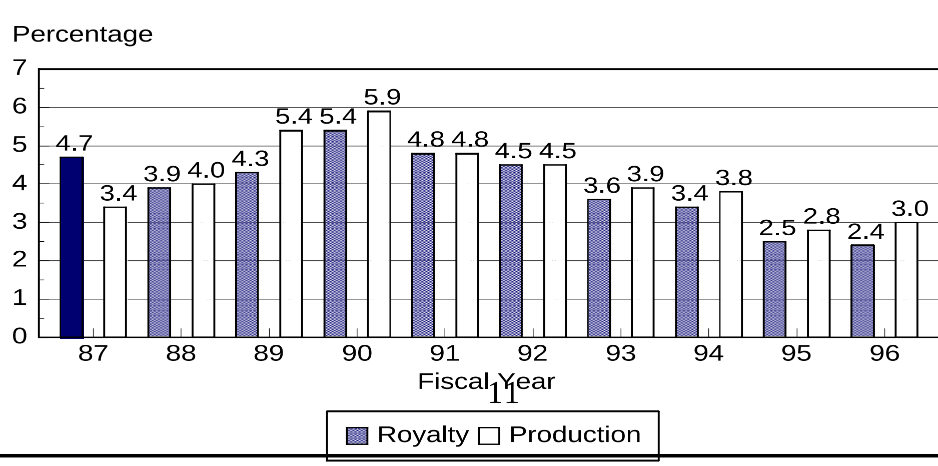
As part of the MMS's efforts to improve reporting, we provide onsite reporter training to oil, gas, and solid mineral companies in cities where their offices are located. To concentrate on reporter assistance rather than assessments, we stopped issuing bills to companies for filing royalty and production reports late or erroneously, unless the overall error rate exceeded 3 percent. The 1996 royalty and production error rates were 2.4 percent and 2.99 percent, respectively. Accordingly, we did not issue any late/erroneous assessments during 1996.

The Federal Oil and Gas Royalty Simplification and Fairness Act of 1996 (RSFA), enacted in August 1996, extended the assessment moratorium through March 1, 1998. The MMS benefits primarily through reduced error correction and assessment workloads and a reduction of approximately 35 percent of the appeals workload. The approach to stop the billing and concentrate on assisting reporters to report correctly is working to everyone's benefit.

Royalty and production reporting accuracy.

We review royalty and production report lines with a series of critical system edits. These edits ensure reported information is consistent with key lease data to permit correct disbursement of revenue. Lines rejected by critical system edits must be corrected manually before disbursement functions can resume. For example, if the reported lease number is invalid, our system rejects the line. Correct disbursement of lease revenue is impossible without a valid lease number. Lower error rates indicate reporters are better at meeting data requirements. In 1996, reporters correctly submitted 98 percent of royalty lines and 97 percent of all production lines, respectively. The chart shows the error rates for the last 10 years.

Error Rates



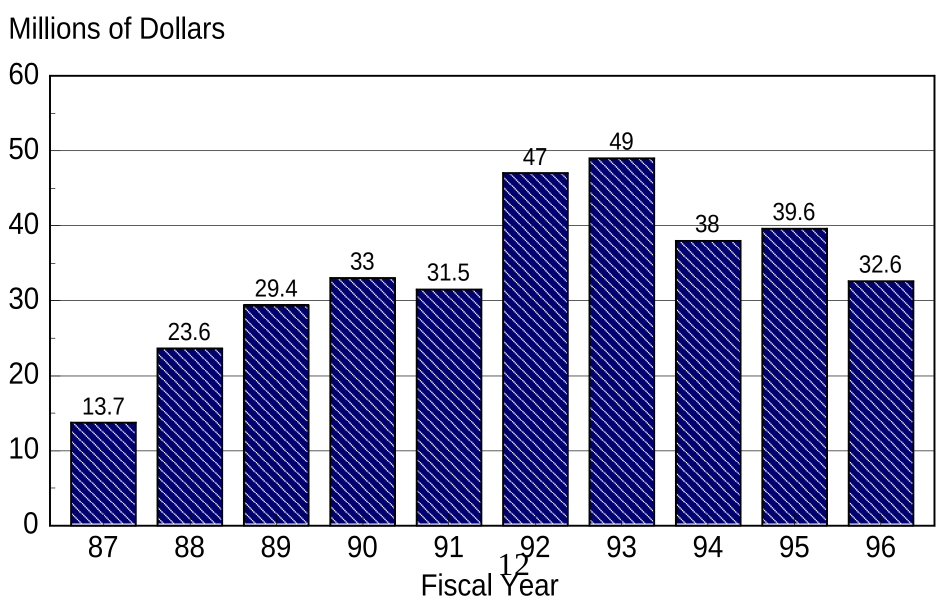
The Royalty Management Program

Compliance Verification and Audit.

An effective compliance program provides incentives for payors to “do it right the first time.” Our compliance verification and audit programs meet this need by providing reporting reviews and collections of underpayments we detect. As payors improve their first time payment and reporting, collections for these followup activities will decline.

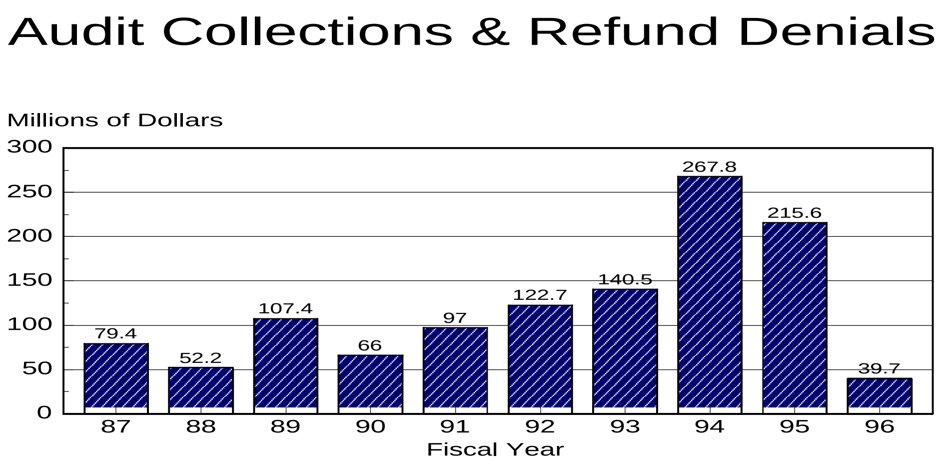
The object of compliance verification is to identify potential royalty underpayments by analyzing computer-generated exceptions and billing royalty payors for underpayments. During FY 1996, the MMS collected $18.4 million from researching 20,000 variances between production and sales volumes. We collected an additional $14.2 million through other audit activities for a total of $32.6 million from compliance verification. The following chart shows compliance verification collections for the past 10 years:

Compliance Verification Collections



The Royalty Management Program

Our auditors also conduct onsite studies of payors' accounting records for underpayment discovery. During FY 1996, RMP auditors collected $29.2 million in additional revenues and denied refund requests of $1 million. The 7 Indian Tribes and 10 States, using funded audit authority, collected an additional $9.5 million in revenues. The funds recovered go to State, Indian, and Treasury accounts. Audit collections and refund denials for the last 10 years are shown in the following chart:



The decline in FY 1996 audit collections and refund denials is caused by the conjunction of several factors including:

> FY 1996 was the first year of a three year audit of the eleven largest companies that together account for approximately 50% of total royalty revenues. Very few bills, if any, are issued during the early years of an audit. Therefore, collections resulting from audits are generally greater in the latter half of an audit cycle, or even in years following the conclusion of audits as issues appealed by the companies are resolved.
>
> A management decision, following a review of potential underpayments of royalties in California, to expand the review nationwide. This along with the California audits resulted in a substantial redirection of resources that impacted all other billing activities. It should be noted, however, that through October 1996 the California effort has resulted in the issuance of bills totaling more than $100 million.

The Royalty Management Program

Streamlining and Simplifying the Collection and Disbursement Processes

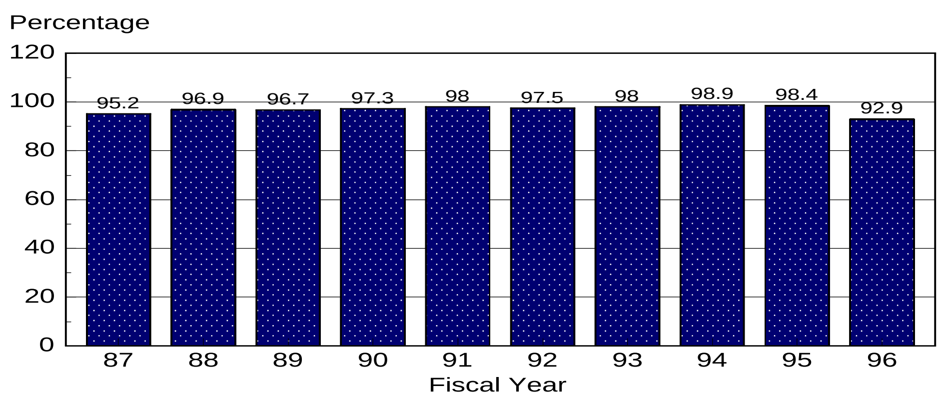
Royalty Policy Committee.

The Department formed the Royalty Policy Committee in 1995 as part of the Minerals Management Advisory Board. Its purpose is to provide advice on the Department's management of Federal and Indian mineral leases, to serve as a sounding board for new procedures and policies, and involve stakeholders in the decision making processes. During FY 1996, the Royalty and Production Reporting and Audit subcommittees submitted final reports recommending streamlined royalty and production reporting, and improved planning, scheduling and communication for audit activities. The Committee believes that implementation of these recommendations will bring about significant administrative savings by both Government and the reporting and paying industry. The MMS is considering these recommendations in our study of changes necessary to comply with RSFA.

On Time Disbursements to States.

During FY 1995, 98.4% of disbursements to States were on time. In 1996, the rate dropped to 92.9%, primarily due to the Federal Government shutdown from December 18, 1995 through January 7, 1996. During this period, payments due on the last business day of December were disbursed 10 days late. The rate of on-time payments for the last 10 years is shown on the following chart:

On-Time State Disbursements

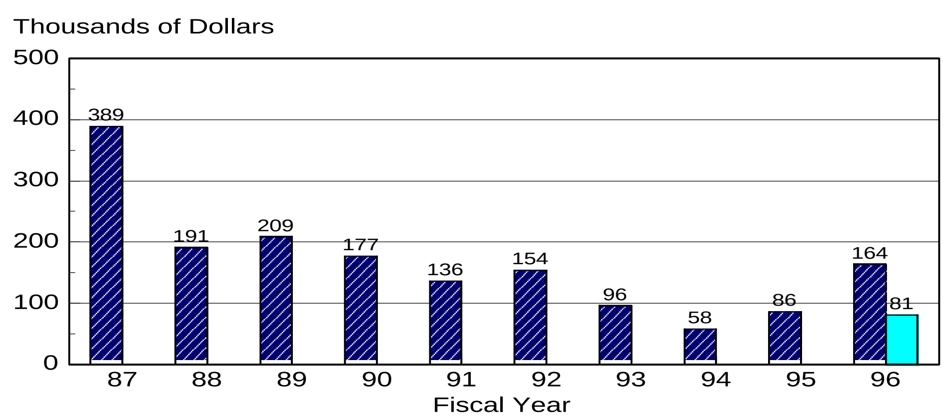


The Royalty Management Program

Interest Paid to States for Late Disbursements.

Less interest paid to States for late disbursements indicates more timely disbursements. For 1995, RMP paid $86,000 interest to States, and for 1996, $164,000. Without the Federal Government shutdown, these payments would have been $81,000. Payments for late disbursements during the last 10 years are shown in the following chart:

Interest Paid to States for Late Disbursements



(Note: in 1996 the interest paid to States would have been $81,000 without the Federal Government shutdown.)

Using Modern Information Management Tools

Electronic Commerce Technology Development and Implementation

The MMS offers various electronic reporting alternatives, including electronic data interchange, magnetic tape, diskettes, and electronic mail. Electronic reporting decreases reporting error rates, minimizes delays and eliminates manual reentry, thus increasing our ability to timely disburse revenues to recipients.

System Enhanced with More Capabilities.

Expand and Upgrade Network. We have underway a 2-year project to expand our dedicated wide-area network to States and Indian tribes with audit authority. We provide equipment, installation support, and extensive training on RMP systems and applications. Currently, most customers can access MMS E-mail, bulletin boards, and certain computer applications. In addition to electronic communication, our customers can print system reports. This provides State and Tribal auditors with faster retrieval of royalty revenue data and more complete information exchange with the rest of the RMP staff.

RMP Query System. We installed a client/server application system that greatly enhances access to and interaction with RMP data. The query system features a set of standard queries and predefined reports. The RMP staff, State, and Indian customers can access up to 6 years of mineral revenue data and all lease information residing on RMP data bases. Customers can graphically display royalty, production, or exception trends. Customers develop their own custom queries and transfer data to spreadsheets or data bases for further analysis.

Computer Output Laser Disk (COLD). The COLD and its companion Imaging and Workflow Technologies were introduced into the RMP work environment in FY 1995. The COLD system provides storage for over 300 reports generated by RMP systems. Users can view and retrieve information on selected reports from their workstations. The data can be printed, routed, or stored. The RMP is also piloting a document imaging and workflow capability which will mirror established business processes and automate the flow of companion documents between individuals and work units. These technologies have great potential to improve information access, reduce paperwork, and enhance individual productivity.

Involving Stakeholders

Participatory Rulemaking.

Federal Gas Valuation. In November 1995, the MMS proposed new regulations for natural gas valuation produced from Federal lands. These regulations were based on the recommendations of the Federal Gas Valuation Negotiated Rulemaking Committee. This Committee included representatives from industry, trade associations, States, and the MMS. The purpose of this effort was to simplify valuation and reduce the associated administrative burden on industry and the MMS. When comments on the proposed rule indicated that the consensus believed to have been reached by the Committee was opposed by several of the parties involved, the MMS reconvened the Committee for further consideration, and reopened the comment period to consider other options. A new rule proposal should be published during 1997.

Indian Gas Valuation. The MMS established the Indian Gas Valuation Negotiated Rulemaking Committee with representatives from industry, trade associations, Indian Tribes, and the MMS. The committee is working to develop a rule that will satisfy the unique requirements of Indian oil and gas lease terms in a manner that fosters timely compliance, fairness, financial certainty, and administrative ease of reporting. The rule is anticipated to rely on publicly available market indices and will retain flexibility for Tribes and individual companies to negotiate other valuation schemes.

Allowances. On February 12, 1996, the MMS published a final rule that eliminates most allowance forms filing requirements for oil, natural gas, and coal produced from Federal leases. This rule amended oil and gas and coal valuation regulations to streamline allowance forms-filing requirements and change associated penalty structures. This change eliminates a substantial reporting burden on industry.

Crude Oil Rules. On December 20, 1995, the MMS published advance notice of proposed rulemaking for Federal and Indian oil valuation regulations. We received 25 comments representing various interests including producers, refiners, States, the State and Tribal Royalty Audit Committee (STRAC), the Navajo Nation, and industry trade groups. Some companies declined to participate, because they are engaged in litigation challenging oil posted price bulletins.

Based on comments received, the RMP assembled a group with representation from the MMS, STRAC, and the Navajo Nation, to draft revised oil valuation regulations in July 1996. The group contracted with energy consultants to advise us on possible options we might consider for oil valuation. Several companies gave the group presentations on oil marketing, in addition to Platt's Oilgram, Bloomberg, and NYMEX. The group is planning on publishing a proposed rule on Federal lands by January 1997. An Indian rule will follow at a later date.

Alternative Dispute Resolution.
We use Alternative Dispute Resolution (ADR) to more efficiently resolve differences on royalty issues with royalty payors. It includes both face-to-face settlement and third-party mediation. Resolution of these disputes through ADR resolves the amount of money owed for past production and clarifies the proper payment or valuation method for particular companies. This decreases both government and industry expenses on accounting, auditing, litigation, and also may avoid

disputes in the future. In addition, we work out payment plans and other strategies for smaller companies to pay larger accrued debts. In the past 3 years, we have instituted an aggressive ADR program to resolve many old disputes. This workload should continue to increase through 1998.

Royalty Gas Marketing Pilot.

The MMS conducted a Royalty Gas Marketing Pilot from January 1, 1995, through December 31, 1995. The pilot was an innovative attempt to test a new method of streamlining natural gas royalty collection in response to recent changes in the natural gas market. During the pilot, the MMS took "in-kind" approximately 6 percent of the Federal Government's royalty share of gas produced from leases in the Gulf of Mexico and sold it to competitively selected natural gas purchasers. The pilot was an operational success, due in large part to the fact that the MMS designed the project in collaboration with industry. But we did not achieve our goal of revenue neutrality, as detailed in the pilot team's September 1996 report to the Director of MMS. We are studying the report and other relevant factors to decide whether to pursue future gas royalty-in-kind efforts.

Compliance Index.

The RMP is testing an overall royalty management outcome measure--called a compliance index--as a part of its performance measurement efforts. The index is summarized by the following formula:

$$\frac{\text{actual voluntary royalty payments}}{\text{expected royalty payments}}$$

The index will evaluate RMP progress in helping industry report and pay correctly.

We are hopeful that the compliance index, through ongoing refinement, can give important information over time on whether RMP is successfully collecting all revenue due. The RMP compliance index target is 1.00. The index was 0.951 for 1992, 0.948 for 1993, 0.950 for 1994, and 0.970 for 1995, computed on a calendar year basis. The RMP will continue to analyze, refine, and validate this measurement tool.

The Offshore Minerals Management Program

The MMS Offshore Minerals Management Program (OMMP) employs 864 staff. Its headquarters is in Washington, D.C., with major field offices in Anchorage, Alaska; Camarillo, California; and New Orleans, Louisiana. Its FY 1996 operating budget was $104.5 million.

GOAL

The MMS goal for our Offshore minerals management function is to maximize development on the outer continental shelf while ensuring fair market value and safe, environmentally sound offshore operations. To achieve this goal, we have developed the following strategies:

- Improve the decision making process through increased internal coordination and involvement of relevant staff,
- Ensure that customers have the opportunity to provide input into the decision making process,
- Recognize and respond to the public's concerns,
- Use modern information tools to ensure timely dissemination of accurate information,
- Streamline operations and simplify processes,
- Maintain a high level of scientific expertise and base decisions on high quality scientific information,
- Issue regulations that focus on results, rather than processes,
- Provide a consistently high level of customer service.

The Offshore Minerals Management Program

On Going Program Activities

In FY 1996, three lease sales were conducted, with bids received totaling about $888 million on 1,570 tracts. These sales bring the total lease sales held by the Department of the Interior to 120 and the total number of leases issued to 5,900, encompassing 25 million acres, an area the size of Texas and California combined. Over $113 billion in bonus, rent, and royalty revenue to the Federal Government has been collected from offshore leases. In FY 1996, offshore leases supplied 5,004 trillion cubic feet of natural gas and more than 425 million barrels of crude oil.

In keeping the Offshore Program in balance with both energy needs and environmental concerns, the MMS conducted about 1,500 environmental reviews and 250 environmental assessments. These reviews and assessments are used to determine the environmental impact of proposed industry actions. To ensure that OCS operations are conducted in a safe and environmentally sound manner, the MMS's regulation of operations program conducted about 11,500 inspections of offshore platforms. These efforts once again have led to no fatalities from well control incidents during the year.

More than 90 oil spill plans were approved by the MMS during FY 1996. Plans are reviewed to assess the adequacy of preparedness for such accidents. Less than 1,900 oil spills actually occurred in FY 96 and none of those were spills greater than 435 barrels. A total of less than 2,700 barrels spilled was reported for the year. On average, this is only slightly more than 1.4 barrels per spill.

Performance Measurement.

During FY 1996, a project action team was formed within OMMP to develop performance measures relating to OMMP. This team is part of the overall MMS effort to develop outcome and output measures in accordance with the GPRA. The team has identified eight potential outcome measures that encompass all aspects of the offshore minerals management goal. The team is currently testing the measures to determine if the required data can be obtained, and if they are otherwise viable. Currently, data are only available for two measures that address the MMS's efforts to maximize mineral development:

The Offshore Minerals Management Program

FY 1996 OCS Production *

Oil	425 (million barrels)
Natural Gas	5,004 (trillion cubic feet)
Sulfur	2.0 (long tons)
Sand and Gravel	0.8 (million cubic yards)

* Production for July - September 1996 is estimated.

Number of Leases Drilled 286

Accomplishments.

During FY 1996, we had many accomplishments in our efforts to effectively manage the mineral resources on the outer continental shelf. Following are significant accomplishments, organized by our strategies for meeting our comprehensive goal for the offshore minerals management function, which is to maximize development on the outer continental shelf while ensuring fair market value and safe, environmentally sound offshore operations.

Improve the decision making process through increased internal coordination and involvement of relevant staff.

The concept of multi-disciplined teams to improve decision making is used frequently within the OMMP. For example, the Gulf of Mexico used teams in the determination of bid adequacy for phase 1 and phase 2 lease award procedures. The efforts of these teams resulted in the creation of a smoother, more efficient flow of data and information needed to decide on whether to accept or reject lease sale bids. In another coordinated effort, members of the Gulf of Mexico's Regional Field Names Committee, the Reserves Section staff, and other Regional supervisors combined their efforts to develop a *Field Naming Guidebook* that supports implementation of the Deep Water Royalty Relief Act of 1996 within the Gulf Region.

Ensure that customers have the opportunity to provide input into the decision making process.

The MMS published the Proposed Oil and Gas Leasing Program for 1997-2002 and draft Environmental Impact Statement (EIS) in February 1996. Over 150 comments on the proposed program and 170 comments on the draft EIS were received and considered in the preparation of the Final Program document that was issued in 1996. Comments were received from States, Federal agencies, industry, environmental groups, and the general public resulting in changes to the Proposed Program.

The MMS worked with several industry associations including the American Petroleum Institute, the Offshore Operators' Committee, the Independent Petroleum Association of America, and the National Oceans Industries Association to poll all OCS operating companies on how well they were developing and implementing the MMS Safety and Environmental Management Program (SEMP). This poll showed significant progress from similar activity in the previous year.

Four public meetings were held this past summer to provide more accurate and detailed information concerning the Federal OCS sand and gravel lease sale off New Jersey. The meetings included a public meeting of the New Jersey Beach Erosion Commission; a Congressional field hearing by Congressman James Saxton, Chair of the House Subcommittee on Fisheries, Wildlife, and Oceans; an environmental forum by Congressman Frank Pallone; and a meeting requested by Congressman Christopher Smith.

Recognize and respond to the public's concerns.

In December 1995, the MMS announced standardized procedures for handling requests for royalty relief on producing leases. This announcement was followed by the publication of detailed guidelines in June 1996. With these new guidelines, companies can determine in advance whether they are likely to qualify for royalty relief, and they can be assured that MMS is prepared to handle their requests in a more standardized, businesslike manner. The new guidelines enable a producer to compute royalties due the government using a formula based on a fixed percentage of net receipts, rather than gross receipts. In this way, the producer can take into account increased costs of production, processing, and transportation on older leases. It gives industry a straightforward set of guidelines when applying for royalty relief on marginally producing wells and provides the economic incentive to ensure continued production on older oil and gas leases and sustain profitability. The guidelines promote the recovery of oil and gas resources that otherwise may be left in the ground when a lease is relinquished.

In November 1995, President Clinton signed the OCS Deep Water Royalty Relief Act, authorizing the Secretary of the Interior to suspend royalties on certain existing and new leases in water depths of 200 meters or greater in parts of the Central and Western Gulf of Mexico planning areas. The MMS published an advance notice of proposed rulemaking in February 1996, and followed with a March 1996, workshop with interested parties soliciting recommendations and comments on rules that would implement the new authority. The MMS published an interim rule on the treatment of royalty relief for newly issued leases in the *Federal Register* on March 25, 1996. The rule was applied to deep water leases issued in the Central Gulf of Mexico Sale 157 and the Western Gulf of Mexico Sale 161. Industry responded to these initiatives by bidding on a record number of tracts in both sales.

For the past 2 years, the MMS has been actively involved with "outreach" efforts in the northwest Florida area (the Panhandle). Representatives of the Gulf of Mexico OCS Region have held meetings with local leaders and groups, participated in conferences, and made speeches, primarily to civic groups. This form of dialogue and consultation is aimed at opening lines of communication and minimizing misinformation, as well as building a degree of trust that can be used to work through new issues as they arise. To date, some 200 individuals representing 100 different organizations have been contacted by members of the Gulf of Mexico Region's Florida Panhandle Outreach Team.

Use modern information tools to ensure timely dissemination of accurate information.

The OMMP is aggressively moving towards using new technology to share information while cutting costs. During FY 1996, we made numerous technical studies and scientific information available via the Internet (see http://www.mms.gov).

Information on specific information releases is provided in the Supplemental Information Section (see page 62).

Streamline operations and simplify processes.

The MMS announced in June 1996, that it is taking steps to produce shorter, more readable EIS's. As part of the administration's call to simplify and streamline government, EIS's prepared by the MMS will be written in plain English, without jargon, describe the proposed action in simple, non-technical terms, focus on relevant environmental issues, and eliminate redundant material and unnecessary background information. These changes will result in EIS's shortened by 25 percent or more. The new procedures are expected to lead to not only smaller, but cheaper and more effective EIS's.

As part of the new EIS streamlining procedures, the MMS will publish only one EIS per 5-year period for the Central and Western Gulf of Mexico planning areas. The MMS is currently publishing a separate EIS for each annual sale.

The Offshore Minerals Management Program

Documentation of the 5-Year Pro gram for 1997-2002 was only about one-third the volume of that produced for the previous program. Early focusing and defining of the areas for leasing and extensive referencing of published material greatly reduced the size of the documentation. Streamlining the EIS also resulted in a 5-year EIS that was substantially smaller and more readable.

Maintain a high level of scientific expertise and base decisions on high-quality scientific information.

Industry is using a new technique to analyze seismic data below salt layers. This new technique, referred to as "depth migration," serves as a tool to help companies determine their bid amounts on OCS tracts. The MMS has begun to request this data from companies to help determine fair-market value. This has led to a more thorough and consistent fair-market value process based on high-quality scientific information.

In June 1996, the MMS received the *1996 Federal Environmental Quality Award* presented by the President's Council on Environmental Quality and the National Association of Environmental Professionals. The award recognizes excellence achieved through implementing the National Environmental Policy Act. The MMS award was for environmental work done in the Flower Garden Banks National Marine Sanctuary in the Gulf of Mexico offshore Texas.

The MMS has entered into a contract with Stanford University's Petroleum Reservoir Engineering Research Program. The principal objective of sponsoring the research program is to provide the MMS with timely access to important research results in the field of petroleum engineering. The MMS's specific areas of interest include the application of geostatistics to reservoir characterization, horizontal well behavior, and well test interpretation.

Issue regulations that focus on results, rather than processes.

The MMS announced revised guidelines for obtaining Suspension of Production (SOP) and Suspensions of Operations (SOO) in July 1996. These guidelines were issued in a Letter to the Lessees and Operators (LTL). The LTL provided an overview of the regulations governing SOP's and SOO's, as well as policies designed to provide flexibility to lessees and encourage the exploration and development of the OCS leases.

The Offshore Minerals Management Program

Provide a consistently high level of customer service.

Changes in industry exploration have increased the time necessary to collect and analyze data associated with drilling operations. Many operations require considerably more time, as industry is now focusing its efforts in areas such as deepwater and subsalt. The MMS proposed to increase from 90 days to 180 days the time allowed between operations for an offshore natural gas and oil lease to continue beyond its primary term. This change, proposed in April 1996, was in response to customer concerns, and gave more flexibility to lessees who are diligently exploring their leases. MMS issued the final rule and it was published in the Federal Register on October 30, 1996.

In support of, and funded by the United States Agency for International Development, the MMS continued its international training/assistance program to the former Soviet Union. The MMS conducted a workshop in Moscow, Russia, this past September on conveying offshore oil and gas exploration and development rights. The workshop was requested by Russia's Ministry of Natural Resources to provide information to Federal policymakers and members of the Russian State Duma Committee on Natural Resources.

In addition to reporting to the MMS, operators of offshore oil and natural gas platforms must file reports on all oil spills with the National Response Center, which is staffed by the U.S. Coast Guard. To reduce the reporting burden and eliminate duplicate reporting requirements, the MMS announced that effective May 31, 1996, we would no longer require operators to report to the MMS oil spills of less than a barrel. For spills of less than one barrel (which comprise 95 percent of all oil spills currently reported), the National Response Center will forward the reports to the MMS. This simple, common sense change reduces industry oil spill reporting requirements for oil spills, without compromising the MMS's environmental stewardship goals.

PART 2

FINANCIAL STATEMENTS

Introduction

The financial statements that follow were prepared to report the financial position and results of operations of the MMS, as required by the Chief Financial Officers Act of 1990. While the statements were prepared from accounting records of the MMS, they differ from financial reports prepared by the MMS pursuant to other Office of Management and Budget directives addressing MMS's use of budgetary resources. Also, these financial statements should be considered as portraying a component of a larger entity, the Federal Government.

The administrative accounting information provided in the financial statements is obtained from the MMS Advanced Budget Accounting/Control and Information System (ABACIS). The automated system provides for the recording, processing, and reporting of all MMS financial transactions in accordance with interim guidance recommended by the Federal Accounting Standards Advisory Board and agreed to by the Director of OMB and the Comptroller General. Royalty Management accounting information is obtained primarily from the RMP's Auditing and Financial System (AFS) and subsidiary records. Both the ABACIS and the AFS utilize the U.S. Government Standard General Ledger.

The Office of Inspector General (OIG) performed four prior audits of MMS annual financial statements, covering fiscal years 1995 (Report No. 96-I-631), 1994 (Report No. 95-I-405), 1993 and 1992 (Report No. 94-I-715), and 1991 (Report No. 93-I-369 -- Combined Statement of Financial Position only). For all four audits, the OIG issued unqualified opinions that the financial statements were fairly presented. The audits also concluded that the MMS internal control structure met established internal control objectives, and that it complied in all material respects with applicable laws and regulations.

DEPARTMENT OF THE INTERIOR
MINERALS MANAGMENTMENT SERVICE

COMBINED STATEMENT OF FINANCIAL POSITION

AS OF SEPTEMBER 30, 1996 AND 1995

	1996	**1995**
ASSETS		
Custodial Assets *(managed on behalf of the Federal Government, not available for use in the internal operations*)		
Fund Balance with Treasury - Royalty Collections (Note 3)	$389,965,816	$124,172,167
Accounts Receivable, Net (Note 5)	244,262,857	275,203,029
Escrow Investments (Note 4)	1,537,531,160	1,406,664,648
Total Custodial Assets	2,171,759,833	1,806,039,844
Operating Assets *(relating to internal operations, funded by Congressional appropriations)*		
Current Assets		
Fund Balance with Treasury (Note 3)	81,745,881	79,532,845
Cash and Other Monetary Assets	48,712	49,250
Accounts Receivable: (Note 5)		
Public	1,663,372	107,681
Due from Federal Agencies	153,471	94,287
Total Current Assets	83,611,436	79,783,963
Property, Plant and Equipment (Note 6)	13,251,104	12,421,781
Total Operating Assets	96,862,540	92,205,744
TOTAL ASSETS	$2,268,622,373	$1,898,245,588
LIABILITIES AND NET POSITION		
LIABILITIES		
Custodial Liabilities *(offsets Custodial Assets)*		
Pending Transfers (Note 7)		
Royalty Distributions	$ 634,228,673	$ 399,375,196
Distribution of Escrow Investments	1,537,531,160	1,406,664,648
Total Custodial Liabilities	$2,171,759,833	$1,806,039,844

DEPARTMENT OF THE INTERIOR
MINERALS MANAGMENTMENT SERVICE

COMBINED STATEMENT OF FINANCIAL POSITION

AS OF SEPTEMBER 30, 1996 AND 1995

	1996	**1995**
Operating Liabilities *(relating to internal operations)*		
Liabilities Covered by Budgetary Resources		
Liabilities to the Public:		
Accounts Payable to the Public	$5,380,022	$3,063,559
Accrued Payroll and Benefits (Note 7)	4,534,329	4,005,477
Total Liabilities to the Public	9,914,351	7,069,036
Liabilities to Federal Agencies:		
Accounts Payable	5,556,350	5,143,229
Receipts Transferable to Treasury	48,712	49,250
Total Liabilities to Federal Agencies	5,605,062	5,192,479
Total Liabilities Covered by Budgetary Resources	15,519,413	12,261,515
Liabilities Not Covered by Budgetary Resources		
Unfunded Payroll Costs (Note 7)	8,725,294	8,161,453
Total Liabilities Not Covered by Budgetary Resources	8,725,294	8,161,453
Total Operating Liabilities	24,244,707	20,422,968
Total Liabilities	$2,196,004,540	$1,826,462,812
Net Position		
Unexpended Appropriations (Note 8)	68,092,023	67,522,448
Cumulative Results of Operations (Note 8)	4,525,810	4,260,328
Total Net Position	72,617,833	71,782,776
TOTAL LIABILITIES AND NET POSITION	$2,268,622,373	$1,898,245,588

The accompanying notes are an integral part of these statements.

DEPARTMENT OF THE INTERIOR
MINERALS MANAGEMENT SERVICE

STATEMENT OF NET COST FROM OPERATIONS

FOR THE YEARS ENDED SEPTEMBER 30, 1996 AND 1995

	1996	1995
Expenses		
Operating Expenses (Note 11)	$202,120,336	$193,904,266
Other Expenses		
Depreciation	1,770,674	1,783,737
Interest Expense	164,777	86,264
Other Expense	63,841	262,239
Total Other Expenses	1,999,292	2,132,240
Total Expenses	204,119,628	196,036,506
Revenues/Receipts		
Other Revenues		
Reimbursement from other Federal Agencies	2,972,976	1,490,437
Other Revenue	15,400,000	8,800,000
Total Revenues/Receipts	18,372,976	10,290,437
Net Cost of Operations	$186,246,652	$185,746,069

The accompanying notes are an integral part of these statements.

DEPARTMENT OF THE INTERIOR
MINERALS MANAGEMENT SERVICE

STATEMENT OF CHANGES IN NET POSITION

FOR THE YEARS ENDED SEPTEMBER 30, 1996 AND 1995

	1996	1995
Change in Net Position		
Net Cost of Operations	($186,246,652)	($185,746,069)
Appropriation Expensed	186,286,079	191,356,140
Net Results of Operations	39,427	5,610,071
Net Change from Operations	39,427	5,610,071
Other Changes in Net Position		
Increase (Decrease) in Appropriated Capital	(33,693)	1,002,530
Increase (Decrease) in Invested Capital	829,323	(531,774)
Net Other Changes in Net Position	795,630	470,756
Net Change in Net Position	835,057	6,080,827
Net Position - Beginning of Year	71,782,776	65,701,949
Net Position - End of Year	$72,617,833	$71,782,776

The accompanying notes are an integral part of these statements.

MINERALS MANAGEMENT SERVICE

STATEMENT OF CUSTODIAL ACTIVITY

FOR THE PERIOD ENDING SEPTEMBER 30, 1996 AND 1995

Collections on Behalf of the Federal Government	1996	1995
Mineral Lease Collections		
Rents and Royalties	$4,264,540,018	$3,254,586,205
Offshore Lease Sales	714,763,998	$371,731,175
Other	1,078,040	$3,303,871
Total Mineral Lease Collections	4,980,382,056	$3,629,621,251
Earnings on Escrow Investments		
Amortized Discount (Note 9)	39,970,138	$44,563,255
Interest, Federal	41,044,133	$32,195,712
Total Investment Earnings	81,014,271	$76,758,967
Total Collections	5,061,396,327	$3,706,380,218
Less: Transfers on Behalf of the Federal Government (Note 11)	(4,664,736,165)	($3,862,704,982)
Untransferred Collections	(396,660,162)	$156,324,764
Total Transferred & Untransferred Collections	(5,061,396,327)	($3,706,380,218)
Excess of Collections over Transfers	$0	$0

The accompanying notes are an integral part of these statements.

PART 3

NOTES TO FINANCIAL STATEMENTS

Note 1. Significant Accounting Policies

Basis of Presentation

These financial statements were prepared to report the financial position and results of operations of the Minerals Management Service (MMS), as required by the Chief Financial Officers Act of 1990. They were prepared primarily from the accounting records of the MMS in accordance with the form and content for entity financial statements specified by the Office of Management and Budget (OMB) in OMB Bulletin No. 94-01, and also, as appropriate, with the OMB Statement of Federal Financial Accounting Concepts Number 2, "Entity and Display." The net position information in the Statement of Financial Position is based partly on Treasury Department reports.

Significant MMS accounting policies are summarized in this Note. These financial statements differ from the financial reports prepared by the MMS pursuant to other OMB directives that are used to monitor and control MMS's use of budgetary resources.

Reporting Entity

The MMS was created on January 19, 1982, by Secretarial Order No. 3071, under authority of Section 2 of Reorganization Plan No. 3 of 1950 (64 Stat. 1262). On May 10, 1982, by Secretarial Order No. 3071, Amendment No. 1, all Outer Continental Shelf leasing responsibilities of the Department of the Interior were consolidated within MMS under Section 2 of Reorganization Plan No. 3 of 1950. Amendment No. 2, dated May 26, 1982, set forth the basic organizational structure for the MMS and provided for the transfer of administrative functions. Secretarial Order No. 3087, dated December 3, 1982, and Amendment No. 1, dated February 7, 1983, provided for the transfer of royalty and mineral revenue management functions, including collection and distribution performed by the Bureau of Land Management, to the MMS.

The MMS has principal responsibility for the offshore leasing program, leasing management, and resource evaluation and classification functions, the environmental review of leasing activities, regulation of operations and lease management, inspection and enforcement programs, and leasing and related public liaison and planning functions on Outer Continental Shelf lands. In addition, the MMS is responsible for the prevention of fraud and theft and for the prompt, full, and complete collection of monies and certain other forms of royalty due the Federal Government, states, and Indian lessors under contractual agreements with lessees.

Basis of Accounting

The accounting principles and standards applied in preparing the financial statements and described in this note are in accordance with the following hierarchy of accounting principles:

> Statements of Federal Financial Accounting Standards (SFFAS). These statements reflect the accounting principles, standards, and requirements recommended by the Federal Accounting Standards Advisory Board and approved by the Comptroller General of the United States, the Director of OMB, and the Secretary of the Treasury.
>
> Form and content requirements for financial statements, as presented in OMB Bulletin No. 94-01 (Form and Content of Agency Financial Statements), and OMB Statement of Federal Financial Concepts No. 2 (Entity and Display).
>
> The accounting principles and standards contained in Departmental and Bureau accounting policy and procedures manuals, and related guidance.
>
> Accounting principles published by authoritative standard-setting bodies and other authoritative sources, in the absence of other guidance in the first three parts of this hierarchy.

The statements are presented on a combination of the cash and accrual bases of accounting. The accrual basis of accounting recognizes the significance and accountable aspects of transactions as they occur. Billed but uncollected mineral lease royalties (receivables) are not recognized as collections because these receivables are subject to significant adjustments prior to collection, and the actual collections resulting from these receivables cannot be reliably estimated. Accordingly, conservative accounting principles require royalty collections to be disclosed on the cash basis instead of the accrual basis of accounting on the Statement of Custodial Activity. However, the balance of billed receivables relating to royalty collections is disclosed on the Statement of Financial Position as a liability (with an offsetting receivable) because of the significant value of the liability. Lack of disclosure of this information would significantly distort the potential liability of MMS to recipients of royalty collections. Because of the different accounting basis for royalty collections, the Statement of Financial Position and the Statement of Custodial Activity do not reconcile.

Certain MMS financial activities interact with and depend on the financial activities of the centralized management functions of the Federal Government. These activities are performed for the benefit of the whole Federal Government, and include public debt and employee retirement, life insurance, and health benefit programs. The MMS financial statements do not contain the results of these centralized financial decisions and activities.

Other Financing Sources and Revenues

The primary financing source for the operation of the MMS is its annual Congressional appropriation. For FY 1996, the principal MMS appropriation account was 1461917. Funds for specific purposes were also appropriated in accounts 146/71917, 14X1917, 14X8370, 14X5003, 14X5243, and 14X5248. Appropriated funds are used for operating and capital expenditures of the MMS. Additional amounts are obtained through reimbursements for services performed for other Federal Agencies. Appropriations are recognized as revenues at the time they are used to pay program or administrative expenses. Appropriations expended for capitalized property and equipment are recognized as expenses as the assets are consumed in operations.

The MMS's FY 1996 appropriation allows for the retention of revenues, in an amount not to exceed $15.4 million dollars, to be used for the development of the Technical Information Management System (TIMS). The TIMS is a comprehensive ADP system for evaluating OCS resources. The revenues result from additions to receipts caused by increased rental rates for offshore leases, rate increases to fee collections for OCS administrative activities, and additional fees for OCS administrative activities established after September 30, 1993. The revenues are credited to the appropriation and remain available until expended.

The MMS Royalty Management Program (RMP) collects bonuses, rents, royalties and other receipts from Federal and Indian Leases, and distributes all proceeds to the U.S. Treasury, other Federal Agencies, States, Indian Tribes, and Indian Allottees, in accordance with legislated allocation formulas. The amounts collected, not including billed receivables (see Basis of Accounting discussion in this Note), are disclosed in the Statement of Custodial Activity as Collections on Behalf of the Federal Government. Corresponding amounts are also disclosed as Transfers on Behalf of the Federal Government. None of the royalties and other receipts collected by the MMS are retained for use by the MMS.

Fund Balances With the U.S. Treasury and Cash

U.S. Government cash is administered on an overall consolidated basis by the U.S. Department of the Treasury. The "Fund Balance with Treasury" line in the Entity Assets Section of the Statement of Financial Position represents the right to draw on the U.S. Treasury for allowable expenditures relating to the MMS appropriation. The "Cash and Other Monetary Assets" line represents the aggregate corpus of MMS imprest funds. The "Fund Balance with Treasury" line in the Custodial Assets Section represents royalty collections received by MMS but not yet disbursed to recipients.

Investments in Federal Securities

The MMS investments in Federal securities are nonmarketable - market based, and are reported at cost net of amortized premiums or discounts. Additional information on MMS investments is provided in Note 4.

Property, Plant and Equipment

Property, plant and equipment are valued at historical cost. Property, plant and equipment are capitalized if the initial acquisition cost is $5,000 or more and the estimated useful life is 2 years or greater (excluding ADP software). Depreciation is recorded using the straight-line method based on useful lives ranging from 5 to 36 years. During FY 1996, adjustments were made to equipment balances reflecting changes to equipment cost bases resulting from reclassifications, upgrades, and revaluations of existing equipment (see Note 12). Additional information on MMS property, plant and equipment is found in Note 6.

Operating Materials and Supplies

The MMS operating materials and supplies primarily consist of office supplies, library materials, and fuel charges. It is assumed that all operating materials and supplies purchased during the year were consumed during the year. Accordingly, no net value is applicable to these items.

Liabilities

Operating Liabilities of the MMS represent amounts likely to be paid by the MMS as a result of transactions or events that have already occurred. However, no liabilities relating to MMS operations can be paid absent an appropriation. Liabilities for which an appropriation has not been enacted are classified as unfunded liabilities and there is no certainty that the appropriation will be enacted. MMS liabilities arising from other than contracts can be abrogated by the Government acting in its sovereign capacity.

The MMS also recognizes custodial liabilities for Pending Transfers of Royalty Collections and Receivables and Pending Transfers of Escrow Investments. Pending Transfers of

Royalty Collections and Receivables represent amounts owed to royalty recipients, and correspond to the total of the asset accounts: “Fund Balance with Treasury - Royalty Collections” and “Accounts Receivable.” Pending Transfers of Escrow Investments primarily represent amounts relating to disputed leases held in escrow pending resolution of the disputes. They correspond to amounts included in the asset account: “Escrow Investments.” Additional information on MMS liabilities is provided in the Basis of Accounting section of this Note and in Note 7.

Contingencies

The MMS is party to a lawsuit where monetary amounts are being sought from the Federal Government. The plaintiffs claim that enactment of the Outer Banks Protection Act in 1990 constiuted a material breach of leases they held in North Carolina pursuant to the Outer Continental Shelf Lands Act, and are seeking damages of $160 million. The court has ruled in favor of the plaintiffs on the breach of contract claims, however, the Government intends to appeal this ruling. The court has not yet made a ruling regarding damages and the damages trial is set to commence in the Spring of 1997. The MMS can make no estimate at this time as to the final disposition of the appeal or as to any ultimate settlement that may be required. Amounts awarded to the plaintiffs, if any, will be paid by the Judgment Fund administered by the Department of Justice and so will not be paid from MMS operating funds.

The MMS has a number of other claims and lawsuits pending against it. In the opinion of management and the Office of the Solicitor, Department of the Interior, the resolution of these claims and lawsuits will not materially affect MMS's financial position or operations. Therefore, no provision for these claims and lawsuits has been made in the accompanying statements.

Public Law 101-510 requires the MMS to cancel its appropriations 5 years after the expiration of the appropria- tions. Any required disbursements against those appropriations after they are canceled must be made out of the current year's appropriation. As of September 30, 1996, the MMS had a balance of $3,575,095 in unliquidated obligations against canceled approp- riations that represents potential liabilities against current year appropriations.

Annual, Sick and Other Leave

Annual leave earned but not taken is accrued in the accounting system and presented in the financial statements. Each year, the balance in the accrued annual leave account is adjusted to reflect current pay rates. Sick leave and other types of leave are expended when used but are not accrued when earned. To the extent current or prior year appropriations are not available to fund unused earned annual leave, funding will be obtained from future financing sources.

Pension and Retirement Plans

Employees of the MMS participate in the Civil Service Retirement System (CSRS) or the Federal Employees' Retirement System (FERS), to which the MMS makes matching contributions. These statements do not report CSRS or FERS assets, accumulated plan benefits, or unfunded liabilities, if any, applicable to MMS employees, since these data are only reported in total by the Office of Personnel Management. On January 1, 1987, FERS went into effect pursuant to Public Law 99-335. Employees hired after December 31, 1983, are automatically covered by FERS, while employees hired prior to that date could elect either FERS or CSRS coverage. One of the primary differences between FERS and CSRS is that FERS offers a savings plan to which MMS is required to contribute 1 percent of pay and match employee contributions up to an additional 4 percent of basic pay. The MMS's contributions for FY 1996 to CSRS and FERS were $4,407,242 and $3,147,300 respectively.

Note 2. Significant Accounting Policies Relating to the Royalty Management Program

Section 8g Settlement

The Outer Continental Shelf (OCS) Lands Act Amendment of 1985 (85 Amendment), provided for the settlement of OCS lease ownership disputes between the Federal Government and various coastal States. The 85 Amendment required annual payments over the next fifteen years to the affected States. The payments are made before April 15 each year. The 85 Amendment stated the payments are funded from revenues derived from OCS leases.

The annual settlement payments for FY96 and FY95 were $45.5 million each year. As of the end of FY 95, the outstanding liability to the States was $325 million.

The remaining schedule of payments is as follows:

Fiscal Year	Amount ($ in millions)
1997	65.0
1998	65.0
1999	65.0
2000	65.0
2001	65.0

Accounting for the Royalty-in-Kind (RIK) Program

Federal and Indian oil and gas leases are issued with a provision that the lessor may elect to receive the royalty amount in product rather than in value. The RMP currently has thirteen RIK contracts (three onshore and ten offshore) for Federal leases. One offshore RIK contract was terminated as of July 30, 1996. These contracts were established in accordance with Federal law (most notably, the Mineral Leasing Act of 1920; the OCS Lands Act of 1953; and the Emergency Petroleum Allocation Act of 1973) to provide small refiners a constant source of product to continue their operations. Operators are required to report the entitled amount of product to be delivered to these designated refiners and RMP then issue bills to the refiners for the payments. In FY 1996, refiners were billed $537.4 million for RIK transactions. Contracts with the refiners allow assessing an administrative fee to cover RMP's cost of managing the RIK program. In FY 1996, RMP billed $919,768 in administrative fees. The $373,768 increase in administrative fee billing is due the first time inclusion of indirect cost for executive direction and administrative support. In addition to paying administrative fees, refiners post both a 30-day cash surety and a surety drawn against a financial institution (i.e., a bond or letter of credit) in an amount equal to 99 days' entitlement for their contract. These sureties are posted at the time of contract execution and are reviewed/adjusted monthly to ensure adequacy of coverage. Cash surety as of September 30, 1996, totaled $39.8 million for the fourteen contracts, while coverage for one bond and thirteen letters of credit totaled $154.2 million. An additional letter of credit in the amount of $2.4 million is being held for an appealed RIK related billing issue.

Sureties for Orders to Perform

As of the fiscal year end September 30, 1996, the RMP no longer holds sureties for Orders to Perform. During FY 1996, RMP released the 111 Order to Perform sureties to comply with 30 CFR 243.

Indian Nonstandard Lease Responsibilities.

The MMS accepted responsibility in March 1988 to account for Indian leases issued per the provisions of the Indian Mineral Development Act of 1982 (25 U.S.C. 2101 et seq.). These leases are negotiated directly between individual Indian Tribes and industry. The Indian leases also contain unique terms or conditions that have to be accounted for manually. The MMS classifies Indian nonstandard leases into three major groups:

> Joint Venture Leases—Leases with another party to share in the development costs and revenues of a property or group of properties;

Net Profit Share Leases—Leases with another party to share in the revenues of a property or properties, usually after deducting operating expenses;

Royalty Leases with unusual terms or conditions—Leases with variable or conditional royalty rates, bonus or penalty payment terms, alternative methods or reporting frequencies.

OCS Refund Requests.

Refund requests from payors, presumably due to previous overpayments on OCS leases, total $146.6 million. These requests must be verified by MMS and then for- warded to Congress for 30 days for review. If no objection is raised, the refund or recoupment is automatically approved.

Alabama Escrow.

A judgement against the MMS was issued May 18, 1994, by the U.S. District Court for the Southern District of Alabama, Southern Division. The judgement directed MMS to pay to the Court Registry the Federal portion of royalties for natural gas production from OCS Block 823. During FY 1996, RMP paid the Court Registry $17.2 million.

The Court's Order was vacated on August 20, 1996, and the original lawsuit was dismissed as of August 27, 1996. A total of about $36.7 million had been paid to the Court Registry. The Justice Department is preparing motions to have the Court Registry return the monies along with the approximately $1.6 million of interest earnings.

Note 3. Fund Balances with Treasury

Fund Balances with Treasury	Obligated	Unobligated		Total
		Available	Restricted	
Appropriated Funds	$71,213,370	$6,595,782	$3,936,729	$81,745,881
Royalty Collections		389,965,816		389,965,816
Total Funds with Treasury	$71,213,370	$396,561,598	$3,936,729	$471,711,697

Note 4. Investments

	Cost	Market Value	Amortization Method	Amortized (Premium) Discount	Net Investment
Escrow Investments	$1,497,561,022	N/A	Straight	$39,970,138	$1,537,531,160

Section 7 of the Outer Continental (OCS) Lands Act allows for receipts from OCS leases having boundary disputes to be invested in Government securities. The current investment amount is due to an ongoing boundary dispute with the State of Alaska dating back to 1979. The principal portion of the Alaska investment is $434 million and the earned interest is $990 million. The funds are continually reinvested and will be disbursed when the boundary dispute is resolved. The Special Master assigned to the U.S. vs. Alaska No. 84 Original, the lawsuit addressing Federal/State boundary questions, issued his recommended decision this year to the Supreme Court.

The Special Master agreed with the U.S. on all but three issues. The U.S. is taking exception to one of the issues. That issue involves the question of who owns the submerged lands under and within the boundaries of the Arctic National Wildlife Refuge. The Special Master ruled that the State of Alaska owns the title and the State has expressed an interest in leasing the lands for oil and gas development.

The State of Alaska has taken exception to all issues on which they did not prevail before the Special Master.

The Solicitor General's Office expects oral arguments before the Supreme Court to occur in early December, 1996. There are two additional briefings before the Supreme Court remaining before the final determination of the lawsuit. The Solicitor General's Office expects the Supreme Court to rule on the case by June, 1997.

Also, the MMS is required by regulation to invest the 1/5 OCS bid amounts from the apparent high bidders for all OCS lease sales. The 1/5 bid investment represents less than 5 percent of the total investment amount. Should any of the apparent high bids be later rejected, the 1/5 bid and actual interest earned are returned to the bidder. The interest earned on accepted bids reverts to the Treasury when the bids are accepted.

Note 5. Accounts Receivable

General Operations.

Accounts receivable relating to general operations consist primarily of amounts due to MMS from other agencies in connection with various interagency agreements, travel advances to MMS employees, and refunds due from MMS vendors.

Royalty Management.

The Federal Oil and Gas Royalty Management Act of 1982 requires reports and payments of royalties by the end of the month following the month in which products are sold. The RMP receivables represent RMP issued royalty-related invoices and any deferred bonus amounts. The amount of RMP receivables is also included in Pending Transfers in the Custodial Liabilities Section of the Statement of Financial Position. As explained in Note 1, accounts receivable relating to royalty collections are not disclosed in the Statement of Custodial Activity.

Recognition of Delinquent Accounts Receivable.
Approximately $122 million of the $244 million RMP net receivables as of September 30, 1996, are considered delinquent. Of the $122 million, about $115 million is in adjudication and the amount collectible is uncertain. Delinquent receivables comprise bills issued for:

Late payment of royalty reports - payments received after due date;

Late payment of bills - payments received after due date;

Nonpayment of royalty reports - payments not received; and

Various types of assessments, e.g. erroneous reporting or valuation issues.

Interest is calculated at statutory rates tied to the Internal Revenue Code by the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA). Generally, the outstanding billed receivables, accumulated interest and one additional year of interest are covered by certificates of deposit, bonds, or letters of credit until all appeal processes allowed by Federal law, are exhausted.

The current surety value is $195 million; $100 million covering invoice values and $95 million covering the potential interest value on the invoices. Some of the amounts owed are shareable with various states and Indian Tribes and Indian allottees, with the remainder owed to miscellaneous receipt funds.

Allowance for Amounts to be Written Off.

The amounts to be written off for royalty payments is based on the most recent fiscal year's experience in collecting accounts receivable. Since RMP has no appropriation or other account to actually offset the uncollectible receivables, RMP's method for offsetting these amounts is to credit the same receivable.

During FY 1996, the allowance for amounts to be written off decreased from $848,049 to $115,000. The $733,049 decrease is due to the implementation and completion of a more streamlined write-off policy, procedural changes and a more aggressive review and cleanup of the oldest open receivables in FY 1995. Receivables scheduled for write-off generally represent only a small fraction of total receivables because of the great majority of receivables are backed by sureties. In addition to the amounts written off, other adjustments of various amounts are made to correct errors and to reflect settlement adjustments. Detailed information on these adjustments are not disclosed due to the proprietary nature of the settlements.

Summary of Accounts Receivable as of September 30, 1996

Type of Receivable	RoyaltyMgmnt	Operations	Total
Custodial Receivables			
Governmental	$244,377,857		$244,377,857
Allowance for Amounts to be Written off	(115,000)		(115,000)
Net Custodial Receivables	$244,262,857		$244,262,857
Operating Receivables			
Public		$1,663,372	$1,663,372
Governmental		153,471	153,471
Net Operating Receivables		1,816,843	1,816,843
Net Receivables	$244,262,857	$1,816,843	$246,079,700

Note 6. Property, Plant and Equipment

Class of Fixed Assets	Depreciation Method	Service Life	Acquisitn Value	Accum Deprec	Net Book Value
Vehicles	Straight-Line	5-10 Years	$ 460,113	$ 231,178	$ 228,935
Office Equipment	Straight-Line	5-36 Years	4,877,318	1,576,395	3,300,923
ADP	Straight-Line	5-20 Years	16,990,922	7,875,741	9,115,181
Other Fixed Assets	Straight-Line	5-20 Years	829,621	223,556	606,065
Totals			$23,157,974	$9,906,870	$ 13,251,104

Note 7. Other Liabilities

	General Operations		Royalty Management		Total	
	Current	Noncurrent	Current	Noncurrent	Current	Noncurrent
Liabs Coverd - Budgtry Resources						
Governmental: Accrued Payroll	$4,534,329				$ 4,534,329	
Liabs Not Covrd-Bdgetry Resrces						
Pending Royalty Distributions			$ 618,624,859	$15,603,814	618,624,859	$15,603,814
Escrow Investments [1]			1,537,531,160		1,537,531,160	
Govrnmntl: Unfunded Annl Leave	8,725,294				8,725,294	
TOTALS	$13,259,623		$2,156,156,019	$15,603,814	$2,169,415,642	$15,603,814

[1] The settlement date of the boundary dispute for which 99 percent of the escrow investment was established (see Note 4) is not determinable. Accordingly, the entire investment is considered current.

Note 8. Net Position

	FY 1996	FY 1995
Unexpended Appropriations		
Unobligated		
Available	$ 6,547,070	$ 5,572,372
Unavailable	3,936,731	5,481,372
Undelivered Orders	57,608,222	56,468,704
Total Unexpended Appropriations	68,092,023	67,522,448
Invested Capital	13,251,104	12,421,781
Future Funding Requirements	(8,725,294)	(8,161,453)
Cumulative Results of Operations	4,525,810	4,260,328
Total Net Position	$72,617,833	$76,043,104

Note 9. Other Revenues and Financing Sources

Collectns on Behalf of Federal Government	FY 1996	FY 1995
Mineral Lease Collections		
Rents and Royalties	$4,264,540,018	$3,254,586,205
Offshore Lease Sales	714,763,998	371,731,175
Miscellaneous Collections	1,078,040	3,303,871
Total Royalties Collected	4,980,382,056	3,629,621,251
Redeemed Earnings of Escrow Investments	39,970,138	32,195,712
Amortized Discount	41,044,133	44,563,255
Total Earnings on Escrow Investments	81,014,271	76,758,967
Total Collections	$5,061,396,327	$3,706,380,218

Royalty Collections and Escrow amounts are not available for use by the MMS. Mineral lease rents and royalties represent amounts paid by mineral lessees per the terms of the lease. Royalties are to be paid monthly for the prior month's production and sales of the minerals. Rents are paid once a year at the beginning of the lease year until production begins or the lease is terminated.

Offshore lease sales are the amounts collected from the bonus and first year rental on Outer Continental Shelf leases. Miscellaneous collections result from money received in error from mineral industry payors.

The almost doubling of the Offshore Lease Sale amounts resulted mainly from the Deep Water Royalty Relief regulations spurring interest in the Central Gulf of Mexico. The 902 leases awarded in the Central Gulf sale were the largest number of leases let in any OCS sale. There was also an OCS sale in the Beaufort Sea area of Alaska. This was the first Alaska OCS sale since 1991.

The increase in the Rents and Royalties amount is the result of increase oil and gas prices and the fact that FY 1996 did not end on a weekend. In FY 1995 the last day of September was a weekend and the regulations allow the payors to remit their monies the next business day.

Note 10. Interest

The MMS incurs interest expense primarily for delayed disbursements of royalties to states. The FOGRMA, as interpreted by the solicitor and various courts, requires RMP to disburse all shareable monies the month following receipt of the funds. Any monies not disbursed within the prescribed time frame accrue interest until disbursement is made.

The MMS paid $163,520 in interest payment in FY 1996 and $85,896 in interest payment in FY 1995. Most interest results from incorrect reporting from industry. The $77,624 difference between FY 1995 and FY 1996 resulted mainly from the Federal Employee's furlough during December, 1995 and January, 1996.

The MMS also pays a small amount of interest in the form of late payment penalties to vendors required under the Prompt Payment Act. Late payment penalties totaling $1,257 and $368 were paid in FY96 and FY95 respectively.

Note 11: Detail of Operating Expenses

Operating Expenses by Object Classification

	FY 1996	FY 1995
Personnel Compensation and Benefits	$111,943,265	$109,849,374
Travel and Transportation	2,798,192	3,811,279
Rents, Communications, and Utilities	12,001,634	12,200,146
Printing and Reproduction	487,278	399,685
Contractual Services [1]	63,445,263	60,968,946
Supplies and Materials	3,875,822	2,595,020
Noncapitalized Equipment	7,568,882	4,079,816
Unfunded Expenses	563,841	262,239
Interest Expense	164,777	86,264
Depreciation	1,770,674	1,783,737
Total Expenses by Object Class	$204,619,628	$196,036,506

1 The major portion of contractual services consists of operation and maintenance contracts for RMP computer systems, and contracts for various environmental assessment studies.

Transfers of Royalty Collections by Recipient:

	FY 1996	FY 1995
U.S. Treasury General Fund	$2,601,616,467	$1,792,725,295
National Park Service	1,046,905,734	1,046,987,237
State Shares of Mineral Receipts	546,891,866	552,248,836
Bureau of Reclamation	350,264,141	367,284,063
Indian Tribes and Agencies	41,217,842	32,537,652
Other Federal Agencies	35,974,102	22,753,898
Other Transfers	41,866,013	48,168,001
Total Transfers on Behalf of the Federal Government	$4,664,736,165	$3,862,704,982

Note 12. Non-Operating Changes

	FY 1996	FY 1995
Increases:		
Transfers In:		
Warrants	$182,312,000	$187,995,903
Restorations	6,400,000	6,440,000
Equipment Additions	2,358,363	2,358,647
Total Increases	191,070,363	196,794,550
Decreases:		
Transfers Out		
Accrued Expenditures	185,592,506	191,931,050
Withdrawals	3,153,187	1,502,323
Equipment:		
Depreciation	1,770,674	1,783,737
Disposals	462,748	517,072
Total Decreases	190,979,115	195,734,182
Other Adjustments:		
Equipment Adjustment, Net [1]	704,382	(589,612)
Net Non-Operating Changes	$ 795,630	$ 470,756

1 Equipment adjustments reflect changes to equipment cost bases resulting from reclassifications, upgrades, and revaluations of existing equipment.

PART 4

SUPPLEMENTAL SCHEDULES

Schedule 1

Department of the Interior
Minerals Management Service
Report of Budgetary Resources
for the years ended September 30, 1996 and 1995
(Unaudited)

Budgetary Resources Made Available	**1996**	**1995**
Budget Authority	$188,712,000	$195,134,903
Unobligated Balances - Beginning of Period	9,643,907	10,845,424
Reimbursements and Other Income	20,877,524	11,506,222
Adjustments	(578,945)	(688,924)
Total, Budgetary Resources Made Available	$218,654,486	$216,797,625
Status of Budgetary Resources:		
Obligations Incurred (gross)	$208,170,685	$206,454,718
Unobligated Balances - End of Period	6,547,070	5,506,243
Unobligated Balances - Not Available	3,936,731	4,137,664
Total, Status of Budgetary Resources	$218,654,486	$216,098,625
Outlays:		
Obligations Incurred, Net	$184,718,919	$194,135,097
Obligated Balance Transferred	0	0
Obligated Balance - Beginning of Period	69,888,937	61,036,113
Less: Obligated Balance - End of Period	71,262,080	69,888,936
Total, Outlays	$183,345,776	$185,282,274

Schedule 2

Minerals Management Service
FY 1996 Obligations by Budget Activity/Subactivity and Major Expense Category
$ (000)

PROGRAM	Salaries & Benefits	Travel	Services	Equip	All Other	Total
OCS LANDS (OCS)						
Leasing & Env. Program	12,707	404	14,026	156	387	27,680
Resource Evaluation	13,823	325	4,509	121	178	18,956
Regulatory Program	17,422	458	9,936	80	244	28,140
Information Mgmt Program	3,498	117	4,677	3,603	1,909	13,804
Offshore Managment	7,078	243	1,132	624	612	9,689
TOTAL OCS LANDS	54,528	1,547	34,280	4,584	3,330	98,269
ROYALTY MANAGEMENT (RMP)						
Mineral Revenue Valuation & Ops.	16,952	365	13,952	2,124	1,274	34,667
Mineral Revenue Compliance	23,190	820	8,551	918	605	34,084
Interest on Late Disbursements					178	178
TOTAL ROYALTY MANAGEMENT	40,142	1,185	22,503	3,042	2,057	68,929
GENERAL ADMIN (GA)						
Executive Direction	2,652	77	225	212	105	3,271
Policy & Mgmt Improvement	3,251	103	105	97	41	3,597
Admin Operations	9,770	135	2,623	821	361	13,710
General Support Services	457	3	2,316	138	11,274	14,188
TOTAL GENERAL ADMINISTRATION	16,130	318	5,269	1,268	11,781	34,766
TOTAL RMP, OCS, GA (ROMM)	110,800	3,050	62,052	8,894	17,168	201,964
Oil Spill Research	1,332	42	4,717	12	84	6,187
TOTAL MMS	112,132	3,092	66,769	8,906	17,252	208,151

Schedule 3

MINERALS MANAGEMENT SERVICE
SUMMARY OF ROYALTY TRANSFERS TO OTHER FEDERAL AGENCIES
THOUSANDS OF DOLLARS

AGENCY	1996	1995
U.S. TREASURY	$2,601,616	$1,792,725
NATIONAL PARK SERVICE	1,046,906	1,046,987
BUREAU OF RECLAMATION	350,264	367,284
U.S. FOREST SERVICE	15,649	18,676
U.S. FISH & WILDLIFE SERVICE	4,102	2,453
BUREAU OF LAND MANAGEMENT	823	1,625
TOTAL	$4,019,360	$3,229,750

Schedule 4

MINERALS MANAGEMENT SERVICE
SUMMARY OF ROYALTY DISBURSEMENTS TO STATES
THOUSANDS OF DOLLARS

STATE	1996	1995
ALABAMA	$11,010	$7,766
ALASKA	14,177	14,007
ARIZONA	17	87
ARKANSAS	920	831
CALIFORNIA	50,945	50,811
COLORADO	34,481	35,489
FLORIDA	37	98
GEORGIA	0	0
IDAHO	2,144	2,351
ILLINOIS	80	95
INDIANA	0	0
KANSAS	1,094	871
KENTUCKY	112	72
LOUISIANA	24,066	15,765
MICHIGAN	702	885
MINNESOTA	6	17
MISSISSIPPI	1,097	823
MISSOURI	1,206	1,013
MONTANA	20,258	24,612
NEBRASKA	14	14
NEVADA	5,751	8,119
NEW MEXICO	118,309	118,904
NORTH CAROLINA	0	1
NORTH DAKOTA	2,370	2,489
OHIO	166	243
OKLAHOMA	1,716	1,834
OREGON	63	43
PENNSYLVANIA	21	23
SOUTH CAROLINA	0	2
SOUTH DAKOTA	633	800
TENNESSEE	0	0
TEXAS	21,532	18,467
UTAH	34,090	31,084
VIRGINIA	90	89
WASHINGTON	469	371
WEST VIRGINIA	197	197
WISCONSIN	1	1
WYOMING	199,118	213,975
TOTAL	$546,892	$552,249

Note: Disbursements include both Mineral Leasing Act payments to onshore States and 8g payments to coastal States.

Schedule 5

ROYALTY COLLECTIONS TRANSFERRED TO
BUREAU OF INDIAN AFFAIRS
FOR DISTRIBUTION TO INDIAN TRIBES
THOUSANDS OF DOLLARS

TRIBE NAME	1996	1995
Alabama-Coushatta	$3,887	$1,584
Assiniboine-Sioux	393	387
Blackfeet	20	25
Cherokee Tribe	0	1
Cherokee,Choctaw,Chickasaw	298	276
Cheyenne-Arapaho	322	293
Chickasaw,Choctaw	194	193
Chilocco Indian School	3	4
Chipewa-Cree	142	156
Choctaw	45	82
Creek	21	10
Creek-Thlopthlocco (1936 Act)	13	13
Crow	59	50
Jicarilla Apache	22	78
Navajo	19	61
Pawnee	2	2
Sac & Fox	4	6
Seminole	6	1
Shoshone and Arapaho	8,673	7,025
Southern Ute	33	199
Ute (Northern Ute)	5,740	4,534
Ute Mountain Ute	1,908	2,207
Wichita, Caddo, Delaware	2	2
TOTAL TRIBAL AMOUNTS	$21,806	$17,189

Schedule 6

ROYALTY COLLECTIONS TRANSFERRED TO
BUREAU OF INDIAN AFFAIRS
FOR DISTRIBUTION TO INDIAN AGENCIES
THOUSANDS OF DOLLARS

ALLOTTEE NAME	1996	1995
Anadarko	$4,144	$3,929
Blackfeet	44	44
Cheyenne River	11	10
Concho	3,777	3,438
Crow	48	44
Ft. Belknap	56	174
Ft. Berthold	268	342
Ft. Peck	1,102	1,036
Michigan	2	1
Muskogee	2,295	1,521
Muskogee (Cherokee)	13	10
Navajo	2,390	1,945
Pawnee	327	326
Shawnee	1,166	621
Southern Ute	657	254
Turtle Mountain	10	11
Uintah and Ouray	1,966	1,440
Unidentified	918	0
Wind River	206	192
Wind River (Amoco)	2	10
TOTAL ALLOTTED	$19,402	$15,348

Schedule 7

OTHER ROYALTY MANAGEMENT PROGRAM ACCOMPLISHMENTS and INITIATIVES

SUPPLEMENTAL INFORMATION

California Undervaluation.

The Assistant Secretary of the Department of Interior commissioned an interagency team, including assistance from the Departments of Energy and Commerce, to investigate charges of royalty underpayments. This team, with access to previously court-sealed documents, detailed possible underpayment information in a May 1996 report. The team concluded that companies often received gross proceeds higher than the amount on which royalties were based, and that royalties may have been substantially underpaid. In July 1996, the MMS took a series of actions to collect unpaid royalty in California. For Federal crude oil produced in and offshore California, the potential underpayment for the period 1980 to 1995 has been estimated at approximately $440 million, including interest.

Most bills for the 1980-1988 period will be issued by January 1997. Bills for later periods will be issued by July 1997, provided that subpoena actions for records are successful. In addition, we initiated actions to review crude oil royalty payments in other States, in cooperation with States and Indian Tribes with which we have audit agreements.

Contract Settlements.

During the past 10 years, many gas (and a few coal) purchasers, particularly pipeline companies, negotiated with mineral producers to rescind, terminate, limit, or otherwise modify sales contracts containing unrealistic purchase prices and/or volumes. In return, mineral producers frequently received monies in settlement of the contractual obligations. Since mineral producers receive additional proceeds under these settlements, audit determinations are necessary to verify that, to the extent the payments were attributable to production, appropriate royalties are paid by the Federal and Indian leaseholders.

Supplemental Information.

In August 1996, a three judge panel of the U.S. Court of Appeals for the District of Columbia Circuit ruled against DOI in a contract settlement case. Concluding our current policy on settlements is inconsistent with the regulatory position on take or pay payments established in 1988, the panel held that we are precluded from collecting royalties on settlement payments unless they are expressly recoupable. Although the court refused to consider the ruling, we continue to believe the payments in question are distinct from take or pay payments, were in fact linked to production, and should be subject to royalty. In October 1996, the Government requested the entire U.S. Court of Appeals to reconsider and that court rejected the request. Without a reversal of the August ruling, our lease recipients could lose hundreds of millions of dollars in royalties. MMS will continue to pursue this approach.

CUSTOMER SERVICES

Farmington Laboratory Summary.

The Department of the Interior, under the Vice President's National Performance Review initiative, studied how to improve the processes which provide mineral and other related services to individual Indian land owners at the Farmington Indian Minerals Office. This office, a tri-agency effort established during 1992 to coordinate the activities of the BIA, Bureau of Land Management (BLM) and MMS, offers one-stop shopping for Indian mineral owners. The Indian Minerals Steering Committee has endorsed most of the recommendations for a 2-3 year pilot program. During the pilot, the employees of the Farmington office will operate under a single line of management and supervision. The recommendations also included the consolidation of minerals management functions currently performed in other locations into the local Four Corners office to make use of their knowledge of local conditions.

Indian Services.

All three Office of Indian Royalty Assistance field offices (Farmington, Northern and Oklahoma City) enhanced customer outreach and consultation by implementing a regular schedule for meeting with individual Indian minerals owners.

Our staff also actively participated in an educational project initiated by the Indian Mineral Steering Committee. The BIA, BLM, and MMS formed a training cadre to develop educational materials to better educate the individual Indian mineral owners.

The BIA and MMS, in a cooperative effort to improve customer service, have staff working together in the BIA's Muskogee Area mineral section.

OTHER OFFSHORE MINERALS MANAGEMENT PROGRAM ACCOMPLISHMENTS and INITIATIVES

Supplemental Information.

During FY 1996, the OMMP had many accomplishments in our efforts to effectively manage the mineral resources on the outer continental shelf. Following are significant accomplishments not included in the Overview of this report. These accomplishments, like those in the Overview section, are listed under the major strategic plan objectives.

Ensure that customers have the opportunity to provide input into the decision making process.

The Alaska Regional Stakeholders Task Force continued to participate in the development of the 5-year program during FY 1996. Following the release of the draft proposed program, the Task Force confirmed that the program was consistent with the Task Force's original recommendations Membership on the Task Force was modified after the draft proposed program was issued in order to assure the most appropriate representation of affected interests for the five Alaska planning areas Following the public comment period, the Task Force made three additional recommendations which were incorporated into the final program decision process. The Task Force provided a unique opportunity for local stakeholders to participate early in the planning process and before any program decisions were made.

The MMS's three Coastal Marine Institutes (CMI's) - Alaska, California and Louisiana - were developed as part of an initiative to cultivate new State-Federal research partnerships on environmental and socioeconomic issues of mutual concern. FY 1996 marked the fourth full year of operation. Thirty-one projects have been initiated to date with a 1-to-1 match of Federal funds with State funds. This year has been highlighted by the receipt of the first two final reports for CMI projects.

Public hearings were held on the Draft EIS for the proposed 5-Year Oil and Gas Leasing Program for 1997 - 2002 in March/April 1996 to obtain public input in the development of the final program for 1997-2002. These meetings were held in Houston, Texas; New Orleans, Louisiana; Mobile, Alabama; and in the Alaska locations of Barrow, Homer, Yakutat, Anchorage, and Kivalina. Information received from these meetings was also considered in the preparation of the Final Program.

Recognize and respond to the public's concerns.

Last May the MMS published a Request for Information (RFIN) in the Federal Register in response to a request to hold a competitive lease sale for Federal OCS sand and gravel resources off the coast of New Jersey. MMS extended the comment period in response to requests from citizens and elected officials for local meetings to explain the leasing proposal in more detail to the public. Extending the comment period allows for inclusion of statements from the public and any additional written comments.

Supplemental Information.

P.L. 103-426 authorized the Secretary to negotiate agreements with States, local governments, or other federal entities, allowing access to OCS Federal sand and gravel resources for public benefit without going through a competitive lease sale process. During FY 1996 one negotiated lease was concluded and one other is under review.

In MMS's Pacific Region the Regional Director has initiated a forum for public discussion of seismic activities on the OCS offshore Southern California. A High Energy Seismic Team consisting of representatives from MMS, other Federal agencies, California State and local agencies, environmental groups, and the natural gas and oil industry meets on a periodic basis to review the process of authorizing seismic survey activities under prelease permits and exploration and development plans under leases. Outside participation has led to more understanding of the technical nature of seismic surveys and the approval process involved on the Federal, State and local levels.

MMS participated in a study entitled: *California Offshore Oil and Gas Energy Resources (COOGER): A Joint Study of the Development Scenarios and Onshore Constraints in the Tri-county Areas of San Luis Obispo, Santa Barbara, and Ventura, California* designed to move the Offshore program into a more proactive relationship with its many customers. By having state and local government representatives working with oil and gas industry representatives and MMS, we have helped to facilitate better understanding of the issues and concerns that affect our diverse and often competing customers. To further enhance meeting our customers' needs, representatives of the business and environmental communities were added to the Steering Committee. Regular monthly mailings on the status of the study were initiated. The mailing list of approximately 200 names includes a range of elected officials, Federal, state, and local agencies, industry, environmental groups, and interested private parties.

MMS's Technology Assessment and Research program developed:

a process to reduce nitrogen oxide emissions from gas turbines and diesels operating on the OCS which adversely affect air quality;

improved deepwater well control procedures to detect and/or control shallow gas releases;

new methodologies to assess the integrity of aging platforms and pipelines.

Supplemental Information.

Use modern information tools to ensure timely dissemination of accurate information.

The Offshore program is aggressively moving towards using new technology to share information while cutting costs. We've emphasized the use of good science in the making of sound resource decisions. During FY 1996 we have released the following information via the Internet (http://www.mms.gov):

> The Environmental Studies Program Information System (ESPIS) makes the results of over $600 million worth of biological, sociological, chemical, and oceanographic research available. This system allows for full text searching capabilities of over 700 technical summaries of its research. More than 20 years of data are accessible on the Internet. This initiative is helping to ensure that MMS provides States and local communities with the information they need concerning the exploration for and development of offshore resources while also ensuring that the academic and scientific community has efficient access of MMS-sponsored research.
>
> The National Resource Assessment is a collection of information on the natural gas and oil resources believed to underlie various Federal offshore areas. In June of 1996 MMS announced the availability of *An Assessment of the Undiscovered Hydrocarbon Potential of the Nation's Outer Continental Shelf*, which presents the results of a multi-year study by MMS to estimate the amounts of undiscovered natural gas and crude oil resources that may exist on the Nation's OCS. Compared to previous versions of this resource assessment, MMS was able to make this version available to a wider audience by publishing it on the MMS Internet.
>
> In a similar vein, MMS also published the first results of the *Offshore Gulf of Mexico Atlas Project* on the home page. The MMS maintains extensive geologic and reservoir engineering files, including all well logs, all available paleontological reports, and complete history of natural gas and oil production. This data has now been organized into a Gulf-wide geologic framework in the Atlas, with the goal of assisting exploration geologists, as will as academia and state professionals, in identifying areas of greatest resource potential. In the Atlas more than 10,000 productive sands from about 1,100 fields have been placed into one of 91 producing hydrocarbon plays. A second volume, for Plio-Pleistocene plays, is due for publication in April 1997. (The Atlases are a joint effort between the MMS and several State and Federal entities).

Other information made available on the Internet by MMS includes: the summary results of the OCS assessment, associated price-supply curves, pool size distributions, and descriptions of the economic results for the various geologic provinces for Alaska; advance notice of proposed rulemaking and the interim rules on the treatment of royalty relief for newly issued leases and for providing suspensions of royalty payments on deep water leases, and the guidelines for deep water royalty relief applications. Also included are Gulf of Mexico's Field Names Guidebook, the Quarterly Field Names Masterlist and reserves data for 899 proved fields. Home Pages have been developed for all Offshore Regional Offices and can be accessed through the MMS Home Page.

Supplemental Information.

The decision documents for the Proposed and Final Oil and Gas Leasing Program for 1997-2002 documents were made available to members of Congress and other constituents in diskette form. These documents were later made available via Internet for all of our customers. Internal to the organization, comments on the proposed program were scanned and transmitted to offices via e-mail, eliminating the extensive use of paper copies that had been generated for previous programs.

Streamline operations and simplify processes.

In an effort to streamline the multiple inspection requirements placed on pipeline operators by several regulatory agencies, MMS has sponsored the Pipeline Inspection Quality Improvement Team (PIQIT) which has developed a consensus-based decisionmaking process to provide user agencies with an analytical framework for assessing the present condition and inspection needs of offshore pipelines. This process, known as the Offshore California Pipeline Inspection Survey(OCPIS) plan, will permit pipeline operators to develop inspection strategies that are tailored to the needs of individual pipelines based on the actual condition of the pipeline.

The Gulf of Mexico Region initiated a change in bid adequacy procedures to eliminate the 3-bid rule used in the acceptance of wildcat and confirmed tracts for lease sales in the Phase 1 evaluation process. The objective of this change was to prevent the awarding of leases on tracts simply because they received three bids. This rule was initially established to incorporate market forces in the evaluation process, but it allowed for prospects with significant potential to be accepted without the detailed analysis given to tracts passed to Phase 2 evaluation. Results were that tracts with potential receiving three or more bids were automatically passed to Phase 2 where they received a detailed analysis, ensuring that fair-market value was achieved.

Supplemental Information.

Maintain a high level of scientific expertise and base decisions on high quality scientific information.

The Gulf of Mexico Region helped compile and publish a Gulf of Mexico natural gas and oil resource database of geophysical, geological, reservoir performance, and production information and analyses for more than 1,100 fields and 22,000 reservoirs. This Atlas is useful to MMS for tract evaluation and fair-market value determinations and to researchers, academics, and industry to more efficiently discover and develop hydrocarbon resources in the Northern Gulf of Mexico.

Gulf of Mexico personnel conducted extensive training on seismic interpretations at computer workstations. Geoscientists within the region used the methodology and technology for interpretations of 2-D and 3-D seismic data for use in making fair market value determinations.

The United States Geological Survey (USGS) and MMS continued their interaction and cooperation on environmental studies. The goal is to utilize the USGS expertise to conduct studies when the required capabilities exist and when it is cost effective for the Federal government. MMS provided USGS with the FY 1996-1997 Studies Strategic Plans and invited USGS to attend meetings of the Scientific Committee. The USGS, in turn, informed MMS of its planned research to facilitate the possibility for additional partnerships when appropriate. The two Bureaus continue to work towards the goal of identifying geographic areas and subject areas where common needs can form the basis for these collaborative efforts.

The Pacific OCS Region successfully completed the California Monitoring Program (CAMP) Phase III study. The study, started in 1986, investigated changes in the marine communities surrounding three major oil and gas platforms in the Point Arguello area of California. Numerous environmental factors were measured during the ten years of the program. Although changes in several of many species of animals on hard rock substrata were observed during the installation and drilling of the platforms and wells, the changes could not be clearly attributed to the platforms and all changes were within natural variation ranges observed over the ten years of the study.

A new 5-year contract to maintain the National Oil Spill Response Test Facility (Ohmsett) was awarded. A full season of tests and evaluations of the effectiveness of oil spill response equipment and procedures was carried out. There has been a dramatic increase in the utilization of Ohmsett over the last two years. In FY 1996 Ohmsett was used as a research center by the U.S. Navy and U.S. Coast Guard to conduct training in oil spill response.

Supplemental Information.

Issue regulations that focus on results, rather than processes.

The MMS has been a leader within the Department of the Interior for efforts to write regulations and similar documents more clearly. This "Plain English" initiative has been so successful that MMS received the Vice President's National Performance Review Hammer Award on March 12, 1996. The Vice President's Hammer Award recognizes teams that dramatically improve the way the government does business.

In June 1996, MMS proposed rules to revise requirements governing unitization of leases. The revision put the rule into plain English and significantly shortened the regulation. MMS expects to issue these as final rules during the first quarter of FY 1997.

MMS is rewriting the regulations at 30 CFR 250.200 (Subpart N), to clarify and simplify assessing and collecting OCS civil penalties. Subpart N will be modified to clarify the administrative process implementing the MMS OCS Civil Penalty Program using the new questions-and-answer format.

Provide a consistently high level of customer service.

At the request of the Department of State, the MMS has participated on several Federal working groups tasked in the drafting of voluntary Arctic offshore oil and gas guidelines and voluntary environmental impact assessment guidelines. The MMS has worked closely with the State Department, NOAA, EPA, the U.S. Coast Guard, and the State of Alaska on both efforts. Both sets of draft guidelines will be reviewed by the Arctic Environmental Protection Strategy, a forum comprised of the eight Arctic nations.

The Reserves Inventory Program Improvement Team (RIPIT) within the Gulf of Mexico Region conducted a total of 9 surveys distributed to 625 internal and external customers. Responses were received from 280 customers representing a 45 per cent response rate. The team identified 49 problems and developed 73 recommendations to improve the products and processes of the Reserves Inventory Program in the Gulf of Mexico based partially on information gathered from the surveys and interviews.

Other MMS accomplishments can be found in the MMS Home Page on the Internet (HTTP://WWW.MMS.GOV). Specific documents that highlight our many accomplishments are:

> Reinventing MMS: A Year of Progress & Accomplishments, 09/96 (look under the "What's New" section)
>
> MMS Today, Spring 1996 (look under the "Reading Room" section)
>
> MMS Innovation Announcements (look for them in the "Reading Room" section, MMS News Releases ("innovation practices")