

Hyla Hurst
Regulatory Specialist
Office of Natural Resource Revenue
PO Box 25165
MS 61013C
Denver, CO 80225



RE: Office of Natural Resources Revenue Advance Notice of Proposed Rulemaking: Federal Oil and Gas Valuation (RIN) 1012-AA01

July 26, 2011

Dear Ms. Hurst,

Taxpayers for Common Sense (TCS), is a national, non-partisan budget watchdog organization. Our mission is to achieve a government that spends taxpayer dollars responsibly and operates within its means.

Since 1995 TCS has actively worked to ensure that taxpayers receive a fair return on resources extracted from federal lands and waters. Royalties and fees collected from resource development represent a valuable source of income for the federal government and should be managed and accounted for in a fair and accurate manner. As the rightful owners, taxpayers have the right to fair market compensation for the resources extracted from our lands and waters, as would any private landowner.

In response to the Office of Natural Resources Revenue's (ONRR) Advance Notice of Proposed Rulemaking (ANPR), Taxpayers for Common Sense would like to submit the following comments for the record.

Oil and gas companies compensate federal resource owners (taxpayers) for resources they extract from public lands and waters in the form of royalties. Generally, this payment is a percentage of the total value of the minerals extracted. More recently other energy resources, such as wind, are also being leased on federal lands and waters, and royalties are being paid to federal taxpayers.

Revenues from the collection of royalties represent one of the largest non-tax income sources for the federal government. Fair and accurate collection is necessary to ensure taxpayers are receiving what they are rightfully owed. In the recent past, the oil and gas royalty collection system has rightfully received serious criticism. The problems within the system have lead to a lack of accountability, transparency and accuracy in charging, collecting, and auditing payments to the federal treasury. It is from this perspective that we would like to comment on the ANPR.

We are pleased to see the ONRR evaluating its royalty collection system, and we urge that any change adopted for federal oil and gas valuation should be designed to recover royalties based on market value with a minimum of lease-specific calculations and adjustments. There is always a tension between simplicity and fairness in valuation, but past practice has gone too far in the direction of site-by-site and lease-by-lease adjustments, each of which creates opportunities for error and must be subjected to later audit and compliance review. These site- and lease-specific adjustments for transportation and processing have created too many opportunities for fraud and required too many resources devoted to lease-by-lease compliance auditing. Simpler valuation

regulations can produce fairness while eliminating opportunities for error and some of the expense of the current five-year post hoc audit cycle.

Thus, wherever possible, value should be calculated based on the simplest estimate of market value without transportation and processing. Obviously, the arm's length contracts used in the past as a primary valuation mechanism are a strong indicator of market value. However, even such contracts require review and audit in order to ensure that they are true arm's length transactions involving no joint interest or collusion. A simpler approach should rely on established market indexes as the primary valuation mechanism.

Recognizing that market indexes do not exist for some areas of federal resource production, surrogates must be found. Arm's length contracts would be the next best measure of value. In cases where there is no arm's length contract, ONRR should establish simple, market-based calculations to be used across the board for valuation from all leases. For example, a general per-mile deduction for transportation costs to the market index point would provide sufficient lease-specific valuation while eliminating many avenues of collusion or fraud that require detailed audit review (i.e., ONRR would still audit the distance calculation but not the actual transportation charges for each month).

ONRR has suggested that the proposed rulemaking is meant to be revenue-neutral, but we urge ONRR to consider whether past royalty calculations have in fact yielded fair return to the Treasury. Numerous outside reviews have suggested that ONRR's valuation methodology has under-valued federal resources, and a simpler methodology should also seek to ensure full return of royalties due. In addition, simpler royalty valuation should require less federal investment in audit and compliance reviews; once current royalties get through the audit process, there should be additional savings for the taxpayer in gradually declining audit costs through the next five years.

Instituting a fair and transparent royalty collection system should be a top priority of the ONRR. Federal taxpayers depend on the important revenues earned from the extraction of our federally owned resources. We look forward to working with the ONRR to ensure this goal is met.

Thank you for your consideration.

Sincerely,

A handwritten signature in dark ink, appearing to read "A. Ry Alexander". The signature is fluid and cursive, with the first name "A. Ry" and the last name "Alexander" clearly distinguishable.

Ryan Alexander
President