Testimony, Ak. '78 Leasing Act, 3/31/79

Mar. 13, Gregg E.

Invitation will be coming from Joe McKinnon, House Finance Comm., re leasing.

Net profits arrangements, etc.

Leg. losing confidence in Tom Cook, Beaufort sale. Junked pre-leasing regs. of Dobie.

Dobie working for Ak pipg.

Single source explors. program.

Major power proj., Susitna. Lumpy.
ISER at UA, demand projections, S. central Ak.
Gregg has $100,000 - 300,000 to study demand, + alt. supplies. -- skeptically, to support smaller alternatives.

Chatterton extended confidentiality provision

USGS gets more info. But AK can't share it.

Fed. leaning to sliding royalty.

Cook pushing cash bonus; fixed royalty ca. 30%.

Gov. committed to Dec. sale.

We have better info. bcs. working w. Feds.
But State has sale info. on 6 wells on line.

Ed Phillips doing ec. model, how much worth to State. Net profit will show higher return to State.
But based on confid. info., can't be released.

Cook gets ideas from "indy". (But does indy speak w. one voice?)

3/19

Jim Rhode

This Sat.

Malone, immed. long hrg.

1. Tech. problems. e.g. Packice

2. Quickly, what is at stake
Arguments for royalty bidding etc.

Quickly sum up args. for net proj. + royalty bidding.

Ellis, comment on jt. venture.

Dec. '19 deadline

Malone wants to drag adm. before leg. to probe how ready they are to proceed.

Exam. is toxic w. token bidding.

Wms. idea of seminar wd. be an adm. show

Committee will not pursue details, but place other options.

Free Comm. → Meskins, Bill Miles
Rem. Comm. →

Both sympathetic

Mostly sympathetic: No indy. spokesman — but maybe Chamberlain..

Gov. postponed Beckert Lease in Ct. citing problems.

Then set Dec. '79 -- but none of problems have been resolved. Gov. evidently made ~~contrib~~ commitment to indy.

La Reche under attack for slow land disposal. He has personal misgivings, but under orders from Gov.

Pattern of delay, pre-leasing investigations.

Leg. Aff. will contact - Hugle has money. Prog. Spec..

Most important point — some pay for deed loss, so money not applied to develop.

Then this loss is used to appraise A taxes

Hugh prefers net profit

Sliding scale royalty came out

Beaufort is further along than wildcat Hoffett prospect in N.C.

Confidentiality on well data, extended until sale. Previously, was only 2 yrs.

Cook is defining Leg. calcs & pub's data.

Hugh wants pub.

Jim works for Hugh, on Penn. Fund

Jim 907-465-3873
-3711

Home 586-2620
1627 Evergreen off 10th

Call Collect with TOG

L.A.G. 465-3802

Juneau, March, '79 Ideas.

1. OPEC price up again, $14.∴/bbl.
Dramatizes value of partic'n.
" " " waiting for higher prices.

2. Profits needed. As delicate as appendectomy less routine. A multi-billion $ opn.; ~~squeezing off~~ High-paid talent on other side of table. History of frauds in land sales, 200 yrs.

3. Compliance laws & programs are essential.

4. Tax on gross is much less onerous for oil & gas than other minerals, bcs. of hi-rent fluck yrs.

5. Use Prudhoe Van Poollen data to show effect of sliding royalty on timing. (It may be very small)
Add Δ fixed ~~cost~~ charge, to offset. Base fixed charge on value of ground, not value of capl. used.
Note, indy. has heavy fixed costs too. Plus fear of heavier future taxes. Big motives to take the $ & run.
Yet, once they get lease rights, they may well just sit, enjoy ΔP.
Look backwards. What does ΔP due to value in Prudhoe? How much better wd. we do w. partic'n?

6. 2dry thermal recovery, there are no deriv costs / bbl.
Sliding scale royalty presumes deriv costs, flush natural drive.

So, it is good for new acreage.
a) Shares risk
b) Collects likely rent.

But, push for SSS, Sophisticated Sliding Scale.

7. DVR regs., based on $i = 0$, slow down prodn. anyway.
So, lift them, replace w. hi royalty.

8. Peculiar prodn. ecs. of O+G are what make royalty workable here, when otherwise bad.

9. Inc. tax or lease is much more sensitive to price fiddling than royalty. You can wipe out entire profit by a smaller drop in price.

Inc. base also lets you glide into in personam, start trying to deduct contract interest

Inc. base requires hi rate, butt of unfair criticism, Kelly-style.

10. Let them deduct from royalty:

a. Amortizn. of Capl. [on-site, post-lease.]
Include int. at rate below mkt.

But do this on a per unit produced. Thus offset neg. incentive of royalty.

b. Expenses.

11. To administer net proceeds approach, need:

a. Gov Acctnt. (w. minerals background) for periodic audits.

b. Gov engineer w. field experience, to judge validity of unusual reported outlays.

c. Basis for setting price.

12. Undermotivate explr. by taxing rent?

If so, can share cost of explr. Can do some ourselves, & distrib. info.

This still does not remove indiv. stands from explr., bec. it is interpn. of data where the Art is.

To be sure, they also keep tight holes, guard such drill data. State shd. require <u>as condition of lease</u> well logs, esply. at edge of lease, to evaluate new lease.

13. Oil leasing customs grew up when there were many small lessors. But etc. is one huge lessor — can reasonably explore its own land before leasing.

14. The idea of needing big motive to explore is fit for ~~offshore~~ mgnl. deps., small + scattered.
But the big finds are hard to miss. As time passes, accruing info. will lead to them, anyway.
So you can take most of surplus w. SSS, etc.

Exception wd. be where explr. is major share of total costs — where explr. is hard, but production is easy.
Remote elephants may partly fit, but at best partly.
Wellhead value is low. bcs. of long haul trucking.

15. Pipeline capacity sets pretty firm prodn. ceiling. So why lease now? When pipeline has unused capac., new oil is worth much more.

16. If anything was ever written on the wall, it is rising value of oil in ground.

Ideas

17 (#) Bonus bidding forces smaller majors into jt. ventures. Cuts down compn.

B.B. strains capl., reduces what smaller bidders have remaining to explore & develop.

B.B. increases chances of failure; over time it drives some firms out of the game, those who pay for dry land.

Here, indy. contradicts self badly. They emphasize risk, hi front-end costs. But bonus adds to these. In some cases, is now the largest of these.

Risk is as great a barrier to entry as K. State, by permitting, shares risk.

18. Effect of Δ_g compn. shd. be large, bcs. indy. is so interlocked.

Are dealing w. indy. so powerful it not only unites those on its side of table, it divides those on your side by supporting campaigns.
No partisan fight. Fanatic oil shriks finally beat them. Remains to see if democr. govt. can.

19. Target rate of return.
Means they calc. bonus bid by disc. future at hi rate.
Device of oligop. "Implicit collusion."
They come right out + tell you this.
If you disc. future at less than their target, then you do better by particip.

20. Bank connections
Big firms have 'em -- common directors.
Bus. indy. is so K-int. Finance is the game.
Banks serve to reduce compn. (in hog. mkt. eg., Katz)

21. Prohibit pol. contribns. by firms dealing w. state.

22. You have to spend money to make money.
Ask. contracting out expln. (or otherwise buying release data) is super inst.
? wdn't sell in strange mkts. w/o payg for em appraisal.

23. Royalty misses out on unrealized appreciation.
Use prop. tax to catch it on interim pd.

24. Needed: Small firm spokesman for deferred prods.
The problem is, who speaks for compn? There is not as much id compn for any competitor as there is id exclusion for the included.

25. Royalty bidding invites wild bids. This is why crop share leases are based on custom, and bidding or selection occurs on other vbles.
So, State shd. have an idea of resource; set high-ish royalty, e.g. 30%; and let bid vble be a bonus, deferred over 10 yrs.

26. "The indy." spokesmen shd. be called Bankers.
Naturally. Bankers prefer a system that gives advantage to control of cash.

27. To make profit-sharing work (or net proceeds), you need:
a. Carefully limit eligible expenses to those on site
b. Exclude R+D

c. Exclude expenses inflated by allocating bad equipment to R & D site

d. Exclude training expenses

e. " p.r. "

Read brings all this out — & he is clearly thinking of (and likes) an integrated major.

28. A less efficient co. will give a higher profit share, yet give less money. However, this is not all vs. profit sharing. Bus. the pressure to lease comes partly from developmentalists, Treasurers. They don't care for effic., or state revs. They only care for gross activity. So, just be careful what you let them deduct. Be sure to limit it to money spent in Ark. for labor. I.e., no dedn. of int. — unless at low rates. Thus nudge them toward labor, vs. K.

29. I presume DNR has carefully studied experience w. profit-share (Long B) royalty. Work-comm.

so as to benefit from their errors, & successes.

I suggest they shd. share this w. Leg.

30. ~~To avoid cost padding~~

Profit share leads to padding costs
Royalty leads to skimping on costs.
So, to cure, use royalty w. partial cost deduct., plus very close monitoring of costs.

Plus, reducing royalty where costs are high.

To prepare for this, need careful cost analysis. Volume alone not enough, e.g. for sliding scale r. List several other factors. Has DNR gotten ready for this? Will it?

31. Explain. incentive, credit in bill 85% is turning over control of state money to pvt. corps.
If State is to spend the $, it shd have a say in where

32. Profit-share wd. be hard to admin. where costs are hi, i.e. on unpvd. deposits, locus. It is a good system where costs are very low -- Wilmington.

In Beaufort, state shd. establish a hi well head price. Then, a Bft. elephant becomes hi profit.

33. As to nat. interest. Ak. guards that as much by conserving for future as by supply today.

34. Bft. Sea selection — as vs. Lower Cook, Bristol Bay, + Ak. Pen. — favors ~~biggies~~ giants, bes. remote + hi cost, no infrastr. Looks like leapfrogging.
But Dobey calls it most favorable area.
Can use present P+B. infrastr.

35. Some work commitment is ~~not bad~~ good, esply. if royalty is changed. But not as the bid vble.
(What Mead overlooks is how these biases may offset. He looks at one at a time -- partial analysis.)

36. You have to spend m to make m.
Your looking at billions in shale gold. Just foolish to skimp on staff. to keep you from being cleaned out. Don't give away the store by firing the bookkeeper.

37. Comm. must define terms. Define profit.
It's taken U.S. Tsy. many decades.
Is it in rem, or personam?

38. Pre leasing regs. needed.

39. Bonus is regressive

BEAUFORT SALE TASKS	COMPLETION DATE	RESPONSIBILITY
Memorandum of Understanding setting forth intent on sale procedures finalized between State and Department of the Interior.	3/2/78	Governor/Secretary
Call for nominations.	3/10/78	BLM - OCS/DMEM
Joint Task Force designated. Joint Task Force co-chaired by Oil and Gas Conservation Commission, Division of Minerals and Energy Management, US Geological Survey, and US Bureau of Land Management OCS Office. Joint working groups operating under the Task Force as follows:	5/78	Dept. of Interior/ Office of the Governor
(1) Legal issues (lease document, interim agreement, permitting, regulations, guidelines).		BLM/DMEM
(2) Impact analysis (DEIS/EIS, mitigating measures, presale process).		BLM/DMEM
(3) Technical problems (operating requirements, exchange of data, post sale surveillance, unitization and drainage).		USGS/O&GCC
(Each working group is co-chaired by the appropriate State and Federal agency)		
Tracts to be considered designated.	6/78	DOI/DNR
Environmental Impact Statement process initiated.	7/78	Task Force
Draft Management Plan developed by Task Force and submitted for approval by Governor/ Secretary.	7/78	Task Force
Initiation of drafting of regulations and economic analysis.	10/78	DMEM

BEAUFORT SALE TASKS (Continued)	COMPLETION DATE	RESPONSIBILITY
Revised Leasing and Nomination Map issued.	1/79	BLM/DNR
Management Plan approved by Governor/Secretary.	1/79	Governor/Secretary
Tract evaluation team designated.	1/79	USGS/DGGS/DMEM
Draft Environmental Impact Statement completed and submitted for field review.	2/9/79	BLM/DMEM
Field review of DEIS completed.	3/2/79	DOI/State Agencies
Meeting of Agency Advisory Committee on Leasing to develop procedures and assignments.	3/7/79	AACL
DEIS issued.	3/30/79	BLM/DMEM
Legal notice for leasing regulations published; draft regulations distributed for public comment. Draft of new leasing form released for public comment concurrently.	4/7/79	DMEM
Copies of DEIS taken directly to Barrow, Kaktovik, and Nuiqsuit by State representatives to explain DEIS/EIS process and to notify of upcoming hearings.	4/4/79 - 4/7/79	BLM/DMEM
Current seismic operations completed.	5/79	Private Contractors
Evaluation of seismic and well data.	4/79 - Sale date	USGS/DMEM/DGGS
Hearings in Fairbanks, Kaktovik, Nuiqsuit, and Barrow on DEIS.	5/79 - 6/7/79	BLM/DMEM

BEAUFORT SALE TASKS (Continued)	COMPLETION DATE	RESPONSIBILITY
Hearings on State Leasing Regulations	5/79 - 6/7/79	DMEM
Public comments considered, leasing regulations adopted and filed with Lieutenant Governor. New leasing form finalized.	6/79	DMEM/Law
State leasing regulations become effective.	7/79	DNR
Field review and drafting of final EIS. EIS includes general operating requirements, conditions, and limitations.	6/7/79 - 7/15/79	Task Force
Trial computer runs on economic model.	5/20/79 - 8/79	BLM/DMEM
Field geologic survey, ANWR, sampling for potential reservoir and source rock characteristics.	Summer, 1979	USGS/DGGS
Lawsuit on disputed lands initiated.	7/79	DOI/Law
Federal State agreement on lease terms	7/79	Task Force
Recommendation by Task Force on basic terms of sale, bidding methodology, length of lease, etc., to decisionmakers (Commissioner/Governor and Secretary), including economic analysis of bidding systems.	7/79	Task Force
Recommendations on unitization of State/Federal lands submitted to decisionmakers by Task Force.	7/79	Task Force
Final Enviornmental Impact Statement released.	8/79	BLM/DMEM

BEAUFORT SALE TASKS	COMPLETION DATE	RESPONSIBILITY
Preliminary geologic model completed, to include estimated reservoir characteristics, thickness, trap sizes, and probability for oil and gas occurrence and amounts. Computer runs on economic model, which includes factors such as resource values, assumptions of oil prices, discount rates, transportation economics, timing of discoveries, risk factors, costs of development, forecast market conditions.	8/79 - Post sale analysis	BLM/USGS/DGGS/DMEM
Recommended course of action in the form of proposed Secretarial Issues Document (SID) sent to Commissioner/Governor and Secretary by Joint Task Force. Must go to Secretary within 30 days after EIS finalized.	9/79	Task Force
Interim Agreement on disputed lands completed.	9/79	DOI/Law
Announcement of decision by Governor/Secretary on sale, bidding terms, terms of sale, lease term, etc.	10/79	Governor/Secretary
Legal notice of sale issued. Includes description of tracts, publication of sale map, breakdown of bid methods and terms by tract, etc. Application of mitigating measures to tracts.	11/79	Task Force
Joint State/Federal lease sale held.	12/17/79	DOI/DNR
Initiation of post sale evaluation. Additional computer runthroughs. Evaluation of bids by US Department of Energy, Federal Trade Commission, US Department of Justice, Congress (oversight), State of Alaska.	12/79 - 2/80	
Post sale evaluation completed. Bids accepted/rejected and awards made.	2/~~79~~ 80	DOI/DNR
Post award processes initiated/completed. Includes approval of plans of operations, compliance inspections, accounting for revenues, permitting procedures for off-lease facilities and activities, other detailed implementation.	1980 - end of lease terms or production	DOI/DNR/Joint Committee
Standardized unit agreement document finalized.	12/80	USGS/DMEM/DOI/Law

Alaska State Legislature

House of Representatives

Committee on Resources

Official Business

Pouch V
State Capitol
Juneau, Alaska 99811

JOINT HOUSE RESOURCES-HOUSE FINANCE
BEAUFORT LEASE HEARING

Saturday, March 31
Courtroom A, Court Bldg.
To begin as soon as House session ends

OVERVIEW
Greg Erickson and Kay Brown, Legislative Research Agency

ENVIRONMENTAL AND TECHNOLOGICAL CONSIDERATIONS
Eben Hobson, North Slope Borough
Don Clocksin, Alaska Legal Services (representing Villages of Kaktovik and Nuiqaut, City of Barrow, Herman Rexford, and Ralph Ahkivgak)
Chuck Evans, Arctic Environmental Information and Data Center
B. Sackinger and Tom Ostercamp, Geophysical Institute, University of Alaska

DISPUTED LANDS
Tom Koester, Assistant Attorney General, Department of Law

WEST COAST OIL GLUT
Arlon Tussing, Economic Consultant

ALTERNATE METHODS OF DEVELOPMENT
Mason Gaffney, Professor of Economics, University of California

DEPARTMENT OF REVENUE
Tom Williams, Director, Petroleum Revenue Division

DEPARTMENT OF NATURAL RESOURCES
Robert LeResche, Commissioner
Tom Cook, Director, Division of Minerals and Energy Management

ADDITIONAL TESTIMONY

Don Langston, EXXON
Sam Del Piaz, Alaska Conservation Society & Alaska Center for the Environment
John Carson, Chevron USA
Phil Holdsworth, Resource Development Council
OMAR

I, A. Bonus bidding, attractive side.

B. Problems w. Bonus Bidding.

1. Front-end barrier

a. Hi conc. Top 8 corps. have 64% acreage (competitive, net)
They have more than 200,000 acres each.

b. Reduced compn.

i. The more the giants get, the lesser base there is for others. ~~(This cd. be partly deliberate, preclusive.)~~

ii. Medium + small firms forced into joint bidding ventures.
→ Same as collusion. If they sold this way, violate Sherman Act. Shd. prohibit joint bidding --- but bonus system gives it a rationale.
Damps compet. edge of bidding. Mead + Norgaard both showed this, indep. studies.

iii. Fncl. power of accum. wealth becomes dominant (conc)

c. Reduced local entrepreneurship; more absenteeism.
Big capl. is outside capl.
More leakage of ec. base

d. Reduced employmt.
Larger firms do everything in more K-int. ways.
My Agr. has data on this.

e. Excessive premium on pre-leasing explr. More front-money needed.
(Not much helped by incentive credits in present law, which only help winners, thus ↓ risk. - + keep info. from State.)

factor in bidding. This nearly means Efficiency moves down the scale as a factor. The most Effic. firm, that cd. pay the most over time, is not the one who can pay most up front. (That's why rich investors rent farms to tenants, etc.) This principle is the beginning of wisdom in resource ecs. W/o it, never understand why the world isn't perfect.

iv. Effect of anything that can Δ compn. cd. be very high, bus. we are dealing w. a united, interlocked oligopoly, w. a century of experience at restraining compn. But there is a large fringe of potential competitors, yearning to break in.

Could cure above problems by defining bonus. But not below.

2. Large Δ in risk. Creates a system where most will lose, so a few can win big ~~most will lose~~

"Gambler's ruin" for some become more likely.

Cuts down willingness of small firms to bid, as the ~~it~~ ante grows large rel. to their wealth. Cuts down success ratio, overall.

They wd. bid much more, DCF =ut, if they cd. pay over time, and contingent on success.

Indy. says as much - it's the high risk that requires hi target rates of return, and reserves the game for a few giants.

In response ~~Well~~, let's reduce the risk, hence reduce the required return.

The State may often be an active party to gambler's ruin by knowingly selling dry acreage. This is using inside info. to practice fraud, and sets or legitimizes a low moral tone ~~tone~~ under which pvt. firms do the same.

3. Is inconsistent w. State's strong fncl. position.

Bonuses are for paupers; for guileless ~~natives~~ primitives who are too easily dazzled by the flash of money, who undervalue the future. Like sale of Manhattan for $24.

State has a surplus. Best invt. is to participate in future revs.

Corps. claim their target is 20%. I.e., they tell you they calculate bids by disc. at 20%. If you'd like to inv. at 20%, participate.

4. Bonus reduces K available to explore + dev. lands.

5. Bonus leaves many kinds of risks
~~Future~~ qns. of ~~the~~ unknown future parameters:
Gen'l. infln.
Oil infln. (If anything was ever written on the wall, it's more of this.)
Amt of reserves
Cost of lifting
" " x ptg.
W. coast mkts
Fed. price regs.
Gas sales
Envr. regs
Title to land. State or Fed. subject to state taxes.
Future Fed. pmts to state in lieu of taxes.

No one can handle all these + bid correctly.
Even if one knew exactly what was underground,
other unknowns are huge.

✓ Prudent man today wd. be a bull on future of oil; and bear on future of money. to participate.

6. Bonus inequitable, in same sense a regressive tax is inequitable. Falls the same on lucky winners + unlucky losers.

Only worse, bec. it is gambler's luck that goes free, more than skill + work.

Lesser points

7. Bonus irreversible, if Kachemak Bay situation occurs.

9. If small firm does win, may be under excessive pressure to produce too fast, to recover K.

Bec. of these problems, State Leg. sought alts. 1978 Leasing Act gives two, (+ some combos) High royalty; high net profit royalty.

In hist. of disposal of U.S. public lands, solved by saddling lands w. prop. taxes. Minerals + petrol. too. So I suggested AVC, same idea in lease terms. Still hope. (Alta. has used this.) But now are faced w. implementing Act of '78, let's see what this entails.

Other jurisdns. leasing lands are mostly nations, who can hit w. high inc. taxes. We must use leasing devices.

II. High royalty.

Defers + shares. ~~But~~ Is in wide use. In farming, ~~[illegible]~~ ~~[illegible]~~ is common to lease land on 50% share or even 60% to lessor.

But there are problems to offset.

A. No commitment by lessee.

1. a. Wild bids possible. But our law, § 854, has no royalty bid except on drainage sales. High fixed royalty, no problem. I like bonus as bid vble., bec. is familiar. But Δ royalty.

2. b. Tie up acreage cheap. To prevent:

a. Limit acreage any one can hold this way. This is what landlords dealing w. share tenants always do.

b. Write a work-commitment into lease.

~~iii. Couple w. profit share royalty, as law allows.~~

✓ iv. Use delay rental; [or bonus, ~~bid~~ deferred pay.]

d. Enforce 5-yr. diligence rule

B. ~~a~~. Marginal effort is made subeconomic.

1. ii. Impose royalty ~~Bee~~ at ↑ rate only during flush years. The peculiar prodn. patterns of oil recs. make this feasible. Easy to avoid early shut-down.

The marg.-effort argument is derived from hard-rock mining, where it really tells. But oil well flows can be neatly divided into flush yrs. + marg. years. Our law allows this. ~~Bee~~ It will take some expert staff work,

and I trust this is being done. But it is doable.

~~For~~

Law doesn't allow sliding scale or step royalty. But lets you start at any level and work down as costs warrant it.

2. ~~II~~. Combine w. net profit royalty.

There are many variations. E.g.

Take top 20%, then, say ¼ of the net profit after that.

Or, levy 20% on all, less deduction of half of costs.
Or, deduct all costs, but w/o int. on capl.
Etc.

Which is best? Calls for deep staff work by DNR. Again, I trust this is being done.

3. ~~III~~. Require certain things be done, by regs. Like done w/in. rules of B.C.F.S. Or w/n. injections, gas injection, etc. We already do this anyway.

4. ~~IV~~. Lower royalty after big invts. made. Very recovery, an obvious & common step. Alts. lower royalty on deeper wells.

Again, calls for expert profnl. staff work, & I trust this is being done.

5. Adopt a fixed charge like GVC

E. ~~e.~~ Lessee doesn't pay you at first, as his wealth increases. But in return, later, he pays you as his wealth declines, no deductions for depln.

C. ~~c.~~ You don't get all the rent, on low-cost deposits.

Solve in part by raising rate, & going to net profit in part, as law allows.

D. ~~d.~~ Incentive to defer produn, to save costs. Wider well spacing than opt.

~~Omit~~

i. Can regulate well spacing

ii. Defend may well ↓ PVR, as oil prices rise, so not such a bad thing.

iii. Defend is advocated anyway, for MER. use royalty instead, get $

iv. Defend effect is weaker than I once thought. Bcs. as you produce, decline in value of leasehold (value of depletion change) is reduced by royalty %. I.e., you only own 60% of what is depleted, so this cost is automatically shared w. lessor.

Omit

III. High Profit-share (again, I won't make it the bid vble - promises are too cheap)

Step 1 here is to define profit. '78 Act leaves this to Comm. Wide latitude. I trust this is being done. Rather, has been done bcs. until you define profit, you can't implement anything.

Some basic qns.

A. Are offsite expenses deductible?

Out-state expenses?

I urge limiting to onsite expenses. Make it ~~be~~ like a Net Proceeds tax, a la Nevada + R. Marshall. Otherwise, open selves up to be had.

(Note encouragement to "local hire." But don't say that's (over)

But this calls for an on-site, in rem approach which cannot simply borrow Corp. Inc. Tax data, which are in personam. Is Comm. ready?

It's not impossibly hard to administer. Marshall says you need an ~~auditor~~ acctnt. to audit spending; and an engineer w. field experience to pass on reasonableness. But you definitely need more than inc. tax data. Or probably less ... but definitely different.

B. How deduct Capl. over time?

1. With interest? I urge yes, but at only 6% or so, to avoid goldplating. But this is just my opinion. Important qu. now is, how will DNR handle, and why.

2. Per bbl., or over life?

I wd. save it for 10 yrs. let him deduct later when produ. becoming unecl. and credit is needed. On a per bbl. basis, offset royalty effects.

Or, deduct up front. Simple + effective. I like this.

the purpose. Say it's a net proceeds royalty.)

Requires Accounts; for auditing Eng's to judge validity of our keys. Complicance rules, penalties for cheating.

C. How avoid padding, chiseling?

Mead's list of chisels. To prevent, we must:

1. ~~Allocate~~ Exclude offsite expenses
2. Exclude R + D
3. " Δ expenses due to allocating bad equipment to the site.
4. " training expenses
5. " p.r. "

1. i.e. avoid underestating price. Profit is highly sensitive. Calls for extra care, monitoring field price. Could call for drastic measures e.g. a state mktg. agency.

Other chisels + ~~other~~ counter measures.

2. Goldplating, a-j. Effect.
   Allow recovery of K w. int., but only 6%.
   Focus auditing on flush producers.
   Only allow front-end recovery of K_0, i.e. K sunk before flush producer confirmed.
3. Stay away from areas of low profit. If Reasn. is low, shd it be there.
4. ~~Hold~~ Combine net profit share w. royalty.

General Countermeasure

Net result is to make lease terms resemble an inc. tax where costs are only partly deductible. Thus, by combining and balancing the working principles of the diff. systems, mixing in common sense, profnl. expertise, and dedication to the public interest, will get a good, workable system.

Conclusion

This will cost some money. OK.
You have to spend money to make money.
~~Yes~~ We're looking at tens of billions of $ in assets.
Admin + leasing public lands is as delicate an operation as an appendectomy, and much less routine.
There were across the table are pros, out for the best deal they can get, and they have scored some real hidies in the past, dealing w. disorganized, confused, unsophisticated ~~naive~~ people --- people a lot ~~sensitive~~ like us.
We need pros on our side.

I am frankly concerned DNR hasn't been back here beating on up. doors for more staff, (over)

Too complex? A lease is no more complex than the standard deal between a movie distrib. + a theatre owner. Bus. is used to working w. complex contracts, sharing risks. It is we, the general public who are tempted to throw up our hands + quit, grab a little money + run. That is the worst mistake we cd. make.

Most big land lessors are nations, which levy 50% corp. inc. tax, use this in tandem w. leases. We have to do much more of it via leasing. Calls for special attn.

and more powers. (e.g. to change royalties rates for different conditions.) (Compliance regs + penalties, re deductibles)

Bonus bidding

Another problem –

The unit bid is much affected by s.t. rate of lease sales. Sell too fast, + prices drop.