Leasing Activities Information

MMS U.S. Department of the Interior
Minerals Management Service
Gulf of Mexico OCS Region

Royalty Suspension Provisions
Central Gulf of Mexico Oil and Gas Lease Sale 190
(Proposed Notice of Sale)

In accordance with applicable regulations at 30 CFR 260, the following royalty suspension provisions apply to Central GOM Oil and Gas Lease Sale 190:

A. The following Royalty Suspension Provisions apply to Shallow Water Deep Gas Production:

1. A lease in less than 200 meters of water where the lessee drills a new deep gas reservoir or reservoirs (15,000 feet or greater subsea) and commences production within 5 years from lease issuance, i.e., not extended by lease suspension, will receive a royalty suspension on the first 20 billion cubic feet of its deep gas production. Deep gas is defined as any gas production from a completion with the top of perforated interval 15,000 feet or greater subsea (true vertical depth below the datum at mean sea level). The lessee must notify the Regional Supervisor, Office of Production and Development, Gulf of Mexico OCS Region, in writing upon the commencement of such deep gas production. Only one royalty suspension volume is available per lease.

2. Liquid hydrocarbons (oil and condensate) which exist in liquid form at standard conditions after passing through separating facilities will be subject to royalty payments.

3. The lease will not receive the royalty suspension for a well drilled into a deep gas reservoir that has produced on any current lease.

4. Any volumes of deep gas production that are not normally royalty-bearing under the lease terms or regulations (e.g. fuel gas) do not count against royalty suspension volumes.

5. Production includes deep gas volumes allocated to a lease under an approved unit agreement.

6. The royalty suspension will continue through the end of the month in which cumulative production from deep gas reservoir(s) on the lease reaches the applicable royalty suspension volume or the

lease period ends. Lease period means the time from lease issuance until relinquishment, expiration, or termination.

7. The lessee must pay the rental fee at the end of each lease year during the period of royalty suspension. A rental fee is not due if the royalty payment during the lease year (for other lease production and under A.6. and A.8.) exceeds the rental amount.

8. The lessee must pay royalty on natural gas production that would otherwise receive royalty suspension, and such production will count towards the royalty suspension volume, in any calendar year during which the arithmetic average of the closing prices for the nearby delivery month on the New York Mercantile Exchange for natural gas exceeds the adjusted gas price threshold.

   a) The base level price threshold for natural gas is set at $5 per million British thermal units (MMBTU) in 2000. The adjusted gas price threshold in any subsequent calendar year is computed by changing the base price by the percentage by which the implicit price deflator for the gross domestic product has changed.

   b) As an example, the computation for the deflator indicates that inflation was 2.2 percent in 2001 and 1.2 percent in 2002. Then the adjusted price threshold per MMBTU was $5.11 in 2001 and $5.17 in 2002. Royalty on shallow water deep gas production in 2002 would have been due if the 2002 average NYMEX natural gas price had exceeded $5.17 per MMBTU. Since the annual average NYMEX gas price in 2002 was $3.36 per MMBTU, no royalty was due on deep gas production in 2002 from leases with deep gas royalty relief.

   c) The MMS will provide notice when this adjusted price threshold is exceeded. Also, information on price thresholds is available at the MMS website (www.mms.gov/econ).

   d) The lessee must pay the royalty due under this paragraph plus late payment interest by March 31 of the following calendar year.

9. There are no circumstances under which a single lease could receive a royalty suspension both for deep gas production and for deepwater production.

10. The proposed shallow water deep gas royalty relief rule at 68 FR 14868,published March 26, 2003, specified that lessees holding leases issued from certain lease sales may have the option to substitute the shallow water deep gas royalty relief provisions associated with the proposed rule for the applicable sale-related royalty relief (see 30 CFR 203.48 of proposed rule). This option may apply to some Sale 190 leases, and more specific information on this matter, if available, will be included in the royalty relief provisions associated with the Final Notice of Sale 190.

B. The following Royalty Suspension Provisions apply to Deepwater Oil and Gas Production. In addition, to these provisions, refer to 30 CFR 218.151 and applicable parts of 260.120-260.124 for regulations on how royalty suspensions relate to field assignment, product types, rental obligations, and supplemental royalty relief.*

1. A lease in water depths 400 meters or deeper will receive a royalty suspension as follows:

   400 meters to 799 meters: 5 million barrels of oil equivalent (BOE)
   800 meters to 1599 meters: 9 million BOE
   1600 meters and deeper: 12 million BOE

2. The lessee must pay royalty on production that would otherwise receive royalty relief under 30 CFR 260 or supplemental relief under 30 CFR 203, and such production will count towards the royalty suspension volume, in any calendar year during which the arithmetic average of the closing prices for the nearby delivery month on the NYMEX for the applicable product exceeds the adjusted product price threshold.

   a) The base level price threshold for light sweet crude oil is set at $28.00 per barrel in 1994. The adjusted oil price threshold in any subsequent calendar year is computed by changing the base price by the percentage by which the implicit price deflator for the gross domestic product has changed.

   b) The base level price threshold for natural gas is set at $3.50 per MMBTU in 1994. The adjusted gas price threshold in any subsequent calendar year is computed by changing the base price by the percentage by which the implicit price deflator for the gross domestic product has changed.

   c) As an example, the computation for the deflator indicates that inflation was 15.26% between 1994 and 2002. Then the adjusted price thresholds in year 2002 were $32.27 per barrel for oil and $4.03 MMBTU for natural gas. Royalty on deepwater oil production in 2002 would have been due if the 2002 average NYMEX oil price had exceeded $32.27 per barrel. Royalty on deepwater gas production in 2002 would have been due if the 2002 average NYMEX natural gas price had exceeded $4.03 per MMBTU. Since the annual average NYMEX oil price in 2002 was $26.10 per barrel and the annual average NYMEX gas price in 2002 was $3.36 per MMBTU, no royalty was due on deep water oil or gas production in 2002 from leases with deep water royalty relief.

   d) The MMS will provide notice when adjusted price thresholds are exceeded. Also, information on price thresholds is available at the MMS website (www.mms.gov/econ).

   e) In cases where the actual average price for the product exceeds the adjusted price threshold in any calendar year, royalties must be paid in the following calendar year. (See 30 CFR 260.122 (c) for more detail.)

3. There are no circumstances under which a single lease could receive a royalty suspension both for deep gas production and for deepwater production.

*The recent federal district court decision in a case **SantaFe, Snyder, et al. v. Norton** (U.S.D.C., W.D. La, Docket No.2:00-CV-1641) declared the regulations at 30 CFR 260.112 – 260.117 invalid. These regulations deal only with deep water leases issued in the 1996-2000 period (Eligible leases). This court decision has no effect on the royalty relief for deep water leases that will be issued in this lease sale because each lease gets its own royalty suspension volume regardless of the field to which it is eventually assigned. One provision, not mentioned in but affected by this decision, 30 CFR 260.124(b), deals with the sharing of relief on fields consisting of leases issued in the 1996-2000 period and leases issued in subsequent sales, including this one. If the district court's decision continues in force, production from leases issued in this sale may not have any bearing on the royalty suspension volume that Eligible leases may ultimately use on a field, contrary to provisions now in 30 CFR 260.124(b)(1). Moreover, your lease acquired in this sale may not produce royalty-free in excess of the suspension volume with which we issued it except as provided in 30 CFR 260.124(c).