

(3) Transportation costs shall be authorized as allowances only when the transported byproduct is sold, delivered, or otherwise utilized by the lessee and royalties are reported and paid.

(d) Byproduct transportation allowances are subject to monitoring, review, and audit. If, after a review and/or audit, MMS determines that a lessee has improperly determined a byproduct transportation allowance authorized by this section, then the lessee shall pay any additional royalties plus interest determined in accordance with 30 CFR 218.302, or shall be entitled to a credit without interest.

(e) If byproducts produced from Federal and non-Federal leases are commingled for transportation, lessees shall not disproportionately allocate transportation costs to Federal lease production.

(f) Upon request, the lessee shall make available to authorized MMS representatives or to other authorized persons all transportation contracts and all other information as may be necessary to support a byproduct transportation allowance.

(g) Byproduct transportation allowances are to be reported as separate lines on Form MMS-2014.

§ 206.358 Determination of byproduct transportation allowances.

(a) *Arm's-length contracts.* (1) For transportation costs incurred by a lessee pursuant to an arm's-length contract, the transportation allowance shall be the reasonable, actual costs incurred by the lessee for transporting the byproducts under that contract, subject to monitoring, review, audit, and possible future adjustments. The MMS's prior approval is not required before a lessee may deduct costs incurred under an arm's-length transportation contract.

(2) In conducting reviews and audits, MMS will examine whether the contract reflects more than the consideration actually transferred either directly or indirectly from the lessee to the transporter for the transportation. If the contract reflects more than the total consideration paid, MMS may require that the byproduct transportation allowance be determined in ac-

cordance with paragraph (b) of this section.

(3) If MMS determines that the consideration paid pursuant to an arm's-length byproduct transportation contract does not reflect the reasonable value of the transportation because of misconduct by or between the contracting parties, or because the lessee otherwise has breached its duty to the lessor to market the production for the mutual benefit of the lessee and the lessor, MMS shall require that the byproduct transportation allowance be determined in accordance with paragraph (b) of this section. When MMS determines that the value of the transportation may be unreasonable, MMS will notify the lessee and give the lessee an opportunity to provide written information justifying the lessee's transportation costs.

(4) Where the lessee's payments for transportation under an arm's-length contract are not established on a dollars-per-unit basis, the lessee shall convert whatever consideration is paid to a dollar value equivalent for the purposes of this section.

(b) *Non-arm's-length or no contract.* (1) If a lessee has a non-arm's-length transportation contract or has no contract, including those situations where the lessee performs transportation services for itself, the byproduct transportation allowance shall be based upon the lessee's reasonable actual costs. All byproduct transportation allowances deducted under a non-arm's-length or no-contract situation are subject to monitoring, review, audit, and possible future adjustment. Prior MMS approval of byproduct transportation allowances is not required for non-arm's-length or no-contract situations.

(2) The byproduct transportation allowance for non-arm's-length or no-contract situations shall be based upon the lessee's actual costs for transportation during the reporting period, including operating and maintenance expenses, overhead, and either depreciation and a return on undepreciated capital investment in accordance with paragraph (b)(2)(iv)(A) of this section, or a cost equal to the capital investment in the transportation system

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multiplied by the rate of return in accordance with paragraph (b)(2)(iv)(B) of this section. Allowable capital costs are generally those for depreciable assets, including costs of delivery and installation of capital equipment, that are an integral part of the transportation system. A return on capital invested in the purchase of real estate to locate the byproduct transportation facilities may be allowed provided that the lessee demonstrates the necessity for such purchase, the purchased land is not on a Federal geothermal lease, and MMS approves the deduction; the rate of return shall be the same rate determined in paragraph (b)(2)(v) of this section.

(i) Allowable operating expenses include operations supervision and engineering, operations labor, fuel, utilities, materials, ad valorem property taxes, rent, supplies, and any other allocable and attributable operating expenses that the lessee can document.

(ii) Allowable maintenance expenses include maintenance of the transportation system, maintenance of equipment, maintenance labor, and other directly allocable and attributable maintenance expenses that the lessee can document.

(iii) Overhead attributable and allocable to the operation and maintenance of the transportation system is an allowable expense. State and Federal income taxes and severance taxes and other fees, including royalties, are not allowable expenses.

(iv) To compute costs associated with capital investment, a lessee may use either paragraph (b)(2)(iv)(A) or (b)(2)(iv)(B) of this section. After a lessee has elected to use either method for a transportation system, the lessee may not later elect to change to the other alternative without MMS approval.

(A) To compute depreciation, the lessee must use a straight-line depreciation method based on, as appropriate, either the life of equipment or the life of the geothermal project that the transportation system services. After an election is made, the lessee may not change methods. A change in ownership of a transportation system shall not alter the depreciation schedule established by the original transporter/

lessee for purposes of the allowance calculation. With or without a change in ownership, a transportation system shall be depreciated only once. Equipment shall not be depreciated below a reasonable salvage value. The rate of return used to compute the return on undepreciated capital investment shall be determined pursuant to paragraph (b)(2)(v) of this section.

(B) To compute a return on capital investment, the allowed cost shall be the amount equal to the allowable capital investment in the transportation system multiplied by the rate of return determined pursuant to paragraph (b)(2)(v) of this section. No allowance shall be provided for depreciation.

(v) The rate of return shall be Standard and Poor's industrial BBB bond rate. The rate of return shall be the monthly average rate as published in *Standard and Poor's Bond Guide* for the first month of the annual reporting period for which the allowance is applicable and shall be effective during the reporting period. The rate shall be redetermined at the beginning of each subsequent transportation allowance reporting period.

Subpart I—OCS Sulfur [Reserved]

Subpart J—Indian Coal

SOURCE: 61 FR 5481, Feb. 12, 1996, unless otherwise noted.

§ 206.450 Purpose and scope.

(a) This subpart prescribes the procedures to establish the value, for royalty purposes, of all coal from Indian Tribal and allotted leases (except leases on the Osage Indian Reservation, Osage County, Oklahoma).

(b) If the specific provisions of any statute, treaty, or settlement agreement between the Indian lessor and a lessee resulting from administrative or judicial litigation, or any coal lease subject to the requirements of this subpart, are inconsistent with any regulation in this subpart, then the statute, treaty, lease provision, or settlement shall govern to the extent of that inconsistency.

(c) All royalty payments are subject to later audit and adjustment.