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James M. Davis
President

October 15, 1997

Mr. David S. Guzy
Chief, Rules and Procedures Staff
Minerals Management Service
Royalty Management Program
Rules and Procedures Staff
P.O. Box 25165, MS 3101
Denver, Colorado 80255-0165

Re: MMS Proposed Rulemaking - Crude Oil Royalty Valuation

Dear Mr. Guzy:

ARCO Western Energy (AWE) is an oil and gas production company located in the state of California. We produce crude oil from three Federal leases located in Kern County and two Federal leases located in Los Angeles County, California. We have reviewed the request for comment in the Federal Register dated September 22, 1997 and welcome the opportunity to provide comments. We understand that at this time MMS is interested in comments only relating to three specific alternatives; 1) benchmarking, 2) differential and 3) index pricing.

Benchmarks

Alternative 1 considers allowing a company to base production not sold at arm's length on prices it receives for outright sales of crude in a particular market area or region. Such a program is called a bid-out or tendering program. This type program may be applicable to some operators but, under the current definition of "arm's length" sales, we do not know if we would be able to use such a program. We understand the proposal to allow "arm's length" sales only to those (or their affiliates) who do not purchase crude oil. ARCO Western Energy is a unit of the Atlantic Richfield Company, a company that buys, sells and refines crude oil. However, ARCO Western Energy does not supply crude oil for refining to any ARCO company. As such, we operate like many independent, "non-integrated" companies. Irrespective of our actual operations, we question whether we would be able to participate in a tendering program if the definition of "outright sales" is tied to the current definition of "arm's length" sales.

Alternative 2 considers other benchmarks. The only part of this alternative that seems feasible is a published price by MMS based on RIK sales. This alternative is also only feasible if the RIK sales are from the same field or general area. Using RIK information from other areas has the same inherent problems as using a netback methodology from the nearest market center or aggregation point.

Geographic Benchmarking

Alternative 3 proposes to establish value based on geographic indexing using MMS "system data". We find it extremely difficult to imagine how market prices would be established if posted prices are to be excluded from the system data. Any market price has as it's genesis a posted price which is determined through established market forces. It is ARCO Western Energy's opinion that the use of a posted price is the best methodology to employ. In selling our crude, ARCO Western Energy relies almost exclusively on the use of posted prices - prices over which ARCO has no influence. We do not post and are totally dependent upon the market for the price we receive for our oil. In addition, the use of ANS prices for California crudes fails to take into consideration market and economic forces that currently establish the difference in price for these crudes.

Differentials

Alternative 4 considers the use of a differential to establish the price per barrel for different regions or areas. We are unsure how the differential methodology would work for California. We have significant concerns about using ANS as a base crude compared to the heavy crude oil produced in the San Joaquin Valley. We also have concerns about a transportation differential established for SJV crudes because of existing pipeline capacity constraints and the effect that the All American Pipeline has on the incremental barrel which, in effect, competes with mid-continent production.

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Alternative 5 suggests the use of published spot prices instead of NYMEX. We believe that this method may provide a workable alternative as those that publish the spot prices have no vested interest in the process. Using information published by Platts, Reuters and/or Telerate could provide the basis from which to determine equitable royalty. This is a workable solution because the prices quoted are based on sales at the lease site or at a marketing sales point, such as Monterey Resources Station 31 here in the San Joaquin Valley.

We thank you for the opportunity to provide comments during the proposed rulemaking process. We also support MMS for holding a workshop in Bakersfield to address California producers and request that if future workshops are necessary in the development of this rule that a west coast location be considered.

If you have any questions or need additional information, please don't hesitate to contact me at (805) 321-4000.

Sincerely,

James M. Davis
President

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