

Negotiated Rulemaking Committee Meeting 4/3/2013

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The last in this series of “open to the public meetings” of the Osage Negotiated Rulemaking Committee started promptly at 9:00 AM as scheduled. There were probably at least 100 in the audience at opening, and more chairs were brought out several times throughout the day to provide seating for more Producers, Land- owners, and Shareholders attending.

After opening ceremonies, they immediately started through the proposed changes to the CFR’s from page one, for the last time. The object was for each of the full committee to have an opportunity to ask questions about the language and to try to reach a consensus of agreement for the language on each subject. The process moved along quickly until the issue of bonding for plugging abandoned wells and site remediation was reached. This has been a sticking point for the committee each time it has been discussed. The most recent version of a change to this language had the bonding set at \$10,000 per well, with a 20 well cap for each producer. A change to \$5,000 per well with a 25 well cap was pending. Also, a solution they called a “revolving well plugging fund” had been proposed and they spent about 20 minutes discussing this method and how it could be implemented, and it was brought up a couple more times later in the meeting. No final consensus was reached today, but the language was temporarily changed to \$5,000 for 25 wells, at least until they work out the details for the revolving fund method for further consideration. This issue will likely be re-visited several times before the NRC recommendations to the BIA are finalized.

The price we Shareholders will receive for royalty barrels was discussed at length again, and although 2 of the 5 man Osage caucus opposed using NYMEX, this seems to be the method that will be recommended by this NRC.

Also it was decided, at the request of, and with the agreement of the Producers; to change the proposed primary rental rate for the first 24 months of a lease from \$10 per month per acre for an oil or gas only lease to \$3 per month per acre; and, to change the proposed primary rental rate for an oil & gas combination lease from \$20 per month per acre to \$6 per month per acre.

The fines and penalties for non-compliance of regulations in these currently proposed CFR changes were the subject of much concern by the Producers and the Minerals Council. Each was discussed in some detail and the amount for many was lowered to better reflect the rate of inflation incurred from 1978 until 2013.

Immediately following a lunch break, verbal comments from the public were heard. There were Shareholders, Producers, and Landowners voicing opinions and offering suggestions for improvements. About 1 hour was allocated to these comments, and each speaker was allowed 4 minutes to present their point of view.

Some time was then spent responding to comments and questions posed. After a couple of typo's were corrected and several other "housekeeping" chores attended to, and after a short break for team caucuses, a recommendation for acceptance or rejection from the Chairman of each caucus was called for. The Federal team reported that they had reached a unanimous consensus to accept the proposed CFR changes. The Osage team reported that they had a 3 to 2 consensus to accept the proposed CFR changes.

After accepting the proposed changes to the CFR's, and after a couple of speeches by some of the Council, the meeting began winding down to a close.

IN MY OPINION:

The red-line version of the CFR revisions flowing from the March 14 meetings can be found at: <http://www.bia.gov/osageregnet> . The April 2 meeting changes will be posted there in like manner within a few days. If anyone was of the opinion in the beginning that these CFR's didn't need to be updated, just open this document and see all the red ink. Much of the modern technology now used in exploration and development for our minerals was not available 20 years ago when this was last updated, and inflation has made many of the numbers obsolete. When the final version of the CFR's are approved, the BIA will once again have the proper tools necessary to manage our Mineral Estate and the teeth to enforce the regulations. I don't personally agree with every change, nor do I agree with a couple of the things in the original document that were left unchanged, but overall, I think this is a very good set of recommendations. The Producers will be taking a pretty hard hit, since it has been 20 years since the last updates were done, but I guess it can't be helped. And let's don't forget, the BIA/DOI makes the final decisions on everything!

Bonding for plugging current and pre-existing abandoned wells and site remediation has historically been the most neglected segment of Osage oil field operations. For many years, leasees' have accepted the responsibility to plug and remediate all abandoned wells and facility sites, but there has never been a time certain established to plug even 1 "orphan" well. It is reported that at least 3,500 of these orphan wells currently exist in the Osage, and there are countless numbers of abandoned facility sites to clean up. None of that has been done either, except a few sites done by the OERB. When a current lessee decides to sell or assign a lease to someone else, this plugging responsibility passes on to the succeeding lessee, and this can continue forever, thus, no wells are ever plugged. The "revolving well plugging plan" recently submitted and being considered, is a way for plugging and remediation to get started, using the funds formerly paid to insurance companies by the Producers as premiums for a revenue base to finance the operations. No further formal bonding would be required except in extreme high risk situations. The initial proposal asks the value of 2 barrels of oil per year for each active well in the control of a lessee. This plan, and other possible methods available to get this work done will be considered in later discussions between the BIA and the Minerals Council.

I'm still not convinced that using NYMEX pricing for oil would be so terrible for the Producers, but neither am I sure that it is a fair way to set the price for royalty oil. The purchasers seem to delight in keeping exactly how the current HPP price is calculated a big mystery. As far as I know, they just set it, and that's what everyone gets. At least Cushing NYMEX could be depended upon to reflect the price of oil each day, as determined by the world market. Maybe a set percentage of the Cushing NYMEX price could be used to cut the extra 30 or 40 cents per barrel cost to the producer. For example, 99.5% of Cushing NYMEX.

I have no problem with the \$3 and \$6 rental rates. It could have been a little higher, but there were much more important things to be resolved by the NRC than to get hung up on this issue. They came down from \$10 & \$20, at the request of the Producers. That was a big step, but it still works for me.

Adjusting the fines and penalties downward somewhat is also OK, but the very best way to avoid any fines and penalties at all would be to stay in compliance with the regulations in the first place. Nearly every one of these penalties can be waived by the BIA Supt., if the Minerals Council agrees.

The Producers had made heavy objections to inserting some of the onshore orders of the Bureau of Land Management. In fact, some of the BLM onshore orders have been used, including most of the section pertaining to the very deadly H₂S contained in some of the Mississippi Lime gas. Other inclusions of BLM language were made in other places, but mostly on a line by line basis. The BLM has dealt with H₂S on a major scale for many years and, although its presence has been known here for a long time, it has appeared only in isolated instances until recently. If certain things in the BLM regulations are found that don't apply here in the Osage, they can be omitted; or, if certain things need to be added, that can be easily done, also. But, there's no need to re-invent the entire wheel here. Too many important things could be overlooked. This H₂S is really bad stuff.

This was the last NRC meeting allowing public comment. There will likely be further negotiations on specific issues with the BIA before the CFR's are completed and forwarded to the Department of Interior for final approval. I am told that once the DOI approves a final version, it will be published in the Federal Register for a 30 day period, where final comments from the public will be taken. The DOI will consider these final comments, and then the final, final, final version of the new CFR 226, Title 25, Chapter 1, Part 226, for the Osage Mineral Estate will emerge and be published. You will have to ask someone who knows, just when this might be expected. I'll be waiting, too.

Ray McClain, Osage Shareholder