

or at the geothermal use facility, the byproduct transportation allowance is authorized for the total byproduct that is transported to a point of sale off the lease, unit, or participating area. You must express byproduct transportation allowances as a cost per unit of byproduct transported.

(3) You may deduct transportation costs only when you sell, deliver, or otherwise utilize the transported byproduct and report and pay royalties on the byproduct.

(d) *Reporting requirements.* (1) You must use a discrete field on Form MMS-2014 to notify ONRR of a transportation allowance.

(2) In conducting reviews and audits, ONRR may require you to submit arm's-length transportation contracts, production agreements, operating agreements, and related documents. You must comply with any such requirements within the time ONRR specifies. Recordkeeping requirements are found at part 1212 of this chapter.

(e) Byproduct transportation allowances are subject to monitoring, review, and audit. If, after a review or audit, ONRR determines that you have improperly determined a byproduct transportation allowance, you must pay any additional royalties due (plus interest computed under §1218.302 of this chapter). You are entitled to a credit for or refund of any overpaid royalties.

(f) If you commingled byproducts produced from Federal and non-Federal leases for transportation, you may not disproportionately allocate transportation costs to Federal lease production.

**§ 1206.359 How do I determine byproduct transportation allowances?**

(a) For transportation costs you incur under an arm's-length contract, the transportation allowance will be the reasonable, actual costs you incurred for transporting the byproducts under that contract.

(1) In conducting reviews and audits, ONRR will examine whether the contract reflects more than the consideration actually transferred either directly or indirectly from you to the transporter for the transportation. If the contract reflects more than the

total consideration you paid, ONRR may require you to determine the byproduct transportation allowance under paragraph (b) of this section.

(2) If ONRR determines that the consideration you paid under 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 you otherwise have breached your duty to the lessor to market the production for the mutual benefit of the lessee and the lessor, ONRR will require you to determine the byproduct transportation allowance under paragraph (b) of this section. When ONRR determines that the value of the transportation may be unreasonable, ONRR will notify you and give you an opportunity to provide written information justifying your transportation costs.

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

(b) If you transport the byproduct yourself or under a non-arm's-length transportation arrangement, the byproduct transportation allowance is your reasonable actual costs for transportation during the reporting period, including:

(1) Operating and maintenance expenses under paragraphs (d) and (e) of this section;

(2) Overhead under paragraph (f) of this section; and either

(3) Depreciation under paragraphs (g) and (h) of this section and a return on undepreciated capital investment under paragraphs (g) and (i) of this section; or

(4) A return on capital investment in the transportation system under paragraphs (g) and (j) of this section.

(c)(1) Allowable capital costs under paragraph (b) of this section are generally those for depreciable fixed assets (including costs of delivery and installation of capital equipment) that are an integral part of the transportation system.

(2)(i) You may include a return on capital you invested in the purchase of

real estate to locate the byproduct transportation facilities if:

- (A) The purchase is necessary; and
- (B) The surface is not part of a Federal lease.

(ii) The rate of return will be the same rate determined in paragraph (k) of this section.

(3) You may not deduct the costs of gathering systems and other production-related facilities.

(d) Allowable operating expenses include:

- (1) Operations supervision and engineering;
- (2) Operations labor;
- (3) Fuel;
- (4) Utilities;
- (5) Materials;
- (6) Ad valorem property taxes;
- (7) Rent;
- (8) Supplies; and
- (9) Any other directly allocable and attributable operating expense that you can document.

(e) Allowable maintenance expenses include:

- (1) Maintenance of the transportation system;
- (2) Maintenance of equipment;
- (3) Maintenance labor; and
- (4) Other directly allocable and attributable maintenance expenses that you can document.

(f) Overhead directly 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.

(g) To compute costs associated with capital investment, a lessee may use either paragraphs (h) and (i) or paragraph (j) 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 ONRR approval.

(h)(1) To compute depreciation, you must use a straight-line depreciation method based on either the life of the equipment or the life of the geothermal project which the transportation system services. After you choose the basis for depreciation, you may not change that basis without ONRR approval. You may not depreciate equipment below a reasonable salvage value.

(2) A change in ownership of a transportation system does not alter the depreciation schedule established by the original lessee-owner for purposes of computing transportation costs.

(3) With or without a change in ownership, you may depreciate a transportation system only once.

(i) To calculate a return on undepreciated capital investment, multiply the remaining undepreciated capital balance as of the beginning of the period for which you are calculating the transportation allowance by the rate of return provided in paragraph (k) of this section.

(j) To compute a return on capital investment in the transportation system, the allowed cost will be the amount equal to the allowable capital investment in the transportation system multiplied by the rate of return determined pursuant to paragraph (k) of this section. There is no allowance for depreciation.

(k) The rate of return must be the industrial rate associated with Standard & Poor's BBB rating. The BBB rate must be the monthly average rate as published in Standard & Poor's Bond Guide for the first month for which the allowance is applicable. You must re-determine the rate at the beginning of each subsequent calendar year.

(1)(1) For new transportation facilities or arrangements, base your initial deduction on estimates of allowable byproduct transportation costs for the applicable period. Use the most recently available operations data for the transportation system or, if such data are not available, use estimates based on data for similar transportation systems.

(2) When actual cost information is available, you must amend your prior Form MMS-2014 reports to reflect actual byproduct transportation cost deductions for each month for which you reported and paid based on estimated byproduct transportation costs. You must pay any additional royalties due (together with interest computed under §1218.302 of this chapter). You are entitled to a credit for or a refund of any overpaid royalties.