OFFICE OF
INSPECTOR GENERAL
UNITED STATES POSTAL SERVICE

Oversight of Oil and Gas Mineral Rights

Audit Report

Report Number
SM-AR-16-011

September 20, 2016

OFFICE OF INSPECTOR GENERAL
UNITED STATES POSTAL SERVICE

Highlights

The Postal Service needs to improve its oversight of oil and gas mineral rights. Specifically, the Postal Service did not know which of its properties had oil and gas mineral rights and had no mechanism for tracking or maintaining properties with mineral rights.

Background

Mineral rights are the rights to resources that exist beneath the surface of a property, including oil and gas, ores and metals, or other raw materials. In some states, the surface of a property or land rights can be owned separately from the minerals underneath the land. Many mineral rights owners allow companies to explore, drill, extract, and dispose of minerals on their property or land in return for royalty income. Before conducting any surface-disturbing activities, such as drilling, a company must determine mineral rights ownership, obtain approval from the owners, and initiate a lease agreement.

The U.S. Department of the Interior (DOI) administers the mineral leasing program for about 245 million surface acres of federal land and 700 million sub-surface acres of mineral estate; and collects royalty payments, rent, bonuses, penalties, and other revenue for the program from over 2,900 organizations. In fiscal year (FY) 2015, the DOI managed 44,213 mineral leases and received over $5 billion in oil royalties and over $1.3 billion in gas royalties.

Federal law gives the DOI authority over mineral leases on federal lands and its entitlement to royalties; however, these laws do not apply to the U.S. Postal Service, which owns about 8,300 properties consisting of 20,805 acres of land.

During FY 2015, the Postal Service managed 32 properties with oil and gas leases and received royalty payments totaling $101,700. Facilities is responsible for managing the Postal Service's oil and gas leases, including collecting, tracking, and validating royalty payments.

Our objective was to assess the Postal Service's oversight of oil and gas mineral rights.

What The OIG Found

The Postal Service needs to improve its oversight of oil and gas mineral rights. Specifically, the Postal Service did not know which of its properties had oil and gas mineral rights and had no mechanism for tracking or maintaining properties with mineral rights. In addition, the Postal Service needs to improve its management of oil and gas leases and its collection, tracking, and validation of royalty payments. Further, the Postal Service did not retain mineral rights ownership or consider the value of mineral rights when selling or acquiring properties.

Based on our review of oil and gas lease documentation, we found that:

- Facilities could not provide copies of leases for five properties and was unable to determine whether four of the five properties had leases in place. It also had no established lease for one property, even though the Postal Service received royalty payments valued at $14,108 for this property in FY 2015.

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We recommended management develop a process to identify and track owned properties with mineral rights and determine if the Postal Service is entitled to royalty payments.

- Nineteen leases were not signed by one or both parties.
- Nine leases had a different lessee listed than the one in Postal Service records.
- Two leases Facilities claimed were inactive were still active. Based on our work, the Postal Service has collected $13,244 in royalty payments due since May 2013 for one of these properties and recovered a one-time lease payment in the amount of $34,343 for the other property.

Based on our review of royalty payments, we found that Facilities:

- Incorrectly recorded royalty payments of $87,592 instead of $101,700 for FY 2015.
- Did not record four royalty payment checks valued at $7,847.
- Did not validate the accuracy of royalty payments received.

These conditions occurred because the Postal Service considers the oil and gas mineral rights effort a passive revenue program and management stated they do not have the resources to identify properties with mineral rights and rely on oil and gas companies to notify them. Management also does not have a written policy for managing oil and gas leases and collecting, tracking and validating royalty payments. In addition, management stated it does not retain or consider the value of mineral rights when acquiring or disposing of properties because it is not a part of the Postal Service's mission.

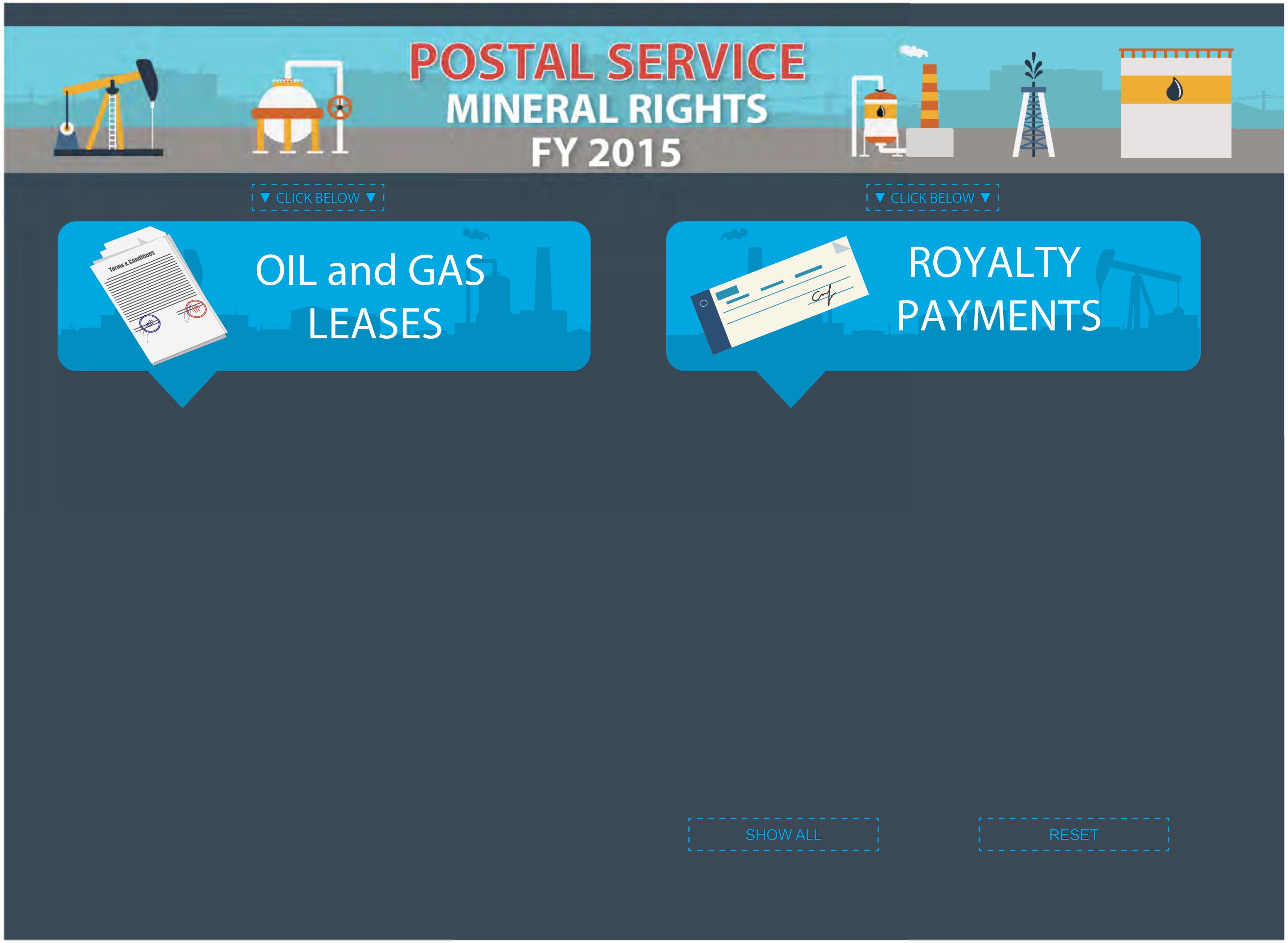
If the Postal Service does not properly manage its properties with mineral rights and does not properly collect, track, and validate royalty payments, it might not receive all entitled royalty revenue. In addition, not retaining mineral rights ownership or considering the value when acquiring or selling properties may result in the Postal Service not achieving the best price and losing potential revenue.

The DOI, through its examinations and data mining efforts, verifies data accuracy by evaluating information submitted by oil and gas companies and completes compliance reviews every 3 years to determine the reasonableness of reported revenue by oil and gas companies. By working with the DOI to identify best practices for collecting, tracking, and validating royalty payments, the Postal Service could ensure oil and gas companies are complying with lease terms and royalty payments are accurately reported and paid.

What The OIG Recommended

We recommended management develop a process to identify and track owned properties with mineral rights and determine if the Postal Service is entitled to royalty payments; and develop a policy outlining its responsibilities for overseeing mineral rights, reviewing and updating all oil and gas leases, and collaborating with the DOI to identify opportunities and best practices for collecting, tracking, and validating royalty payments.

The Postal Service needs to improve its management of oil and gas leases and its collection, tracking, and validation of royalty payments.



Transmittal Letter

OFFICE OF INSPECTOR GENERAL
UNITED STATES POSTAL SERVICE

September 20, 2016

MEMORANDUM FOR: TOM A. SAMRA
VICE PRESIDENT, FACILITIES

E-Signed by Lucine Willis
ERIFY authenticity with eSign Deskto

for

FROM: Keshia L. Trafton
Acting Deputy Assistant Inspector General
for Supply Management and Human Resources

SUBJECT: Audit Report – Oversight of Oil and Gas Mineral Rights
(Report Number SM-AR-16-011)

This report presents the results of our audit of the Oversight of Oil and Gas Mineral Rights (Project Number 15BG018SM000).

We appreciate the cooperation and courtesies provided by your staff. If you have any questions or need additional information, please contact Brian Newman, acting director, Supply Management and Facilities, or me at 703-248-2100.

Attachment

cc: Corporate Audit and Response Management

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Findings

Federal law gives the DOI authority over mineral leases on federal lands and its entitlement to royalties; however, these laws do not apply to the Postal Service, which owns about 8,300 properties consisting of 20,805 acres of land. During FY 2015, the Postal Service managed 32 properties with oil and gas leases and received royalty payments totaling $101,700.

Introduction

This report presents the results of our self-initiated audit of the U.S. Postal Service's oversight of oil and gas mineral rights (Project Number 15BG018SM000). Our objective was to assess the Postal Service's oversight of oil and gas mineral rights. See Appendix A for additional information about this audit.

Mineral rights are the rights to resources that exist beneath the surface of a property, including oil and gas, ores and metals, or other raw materials. In some states, the surface of a property or land rights can be owned separately from the minerals underneath the land. Many mineral rights owners allow companies to explore, drill, extract, and dispose of minerals on their property or land in return for royalty income. Before conducting any surface-disturbing activities, such as drilling, a company must determine mineral rights ownership, obtain approval from the owner, and initiate a lease agreement.

The U.S. Department of the Interior (DOI) administers the mineral leasing program for about 245 million surface acres of federal land and 700 million sub-surface acres of mineral estate; and collects royalty payments, rent, bonuses, penalties, and other revenue for the program from over 2,900 organizations. In fiscal year (FY) 2015, the DOI managed 44,213 mineral leases and received over $5 billion in oil royalties and over $1.3 billion in gas royalties.

Federal law gives the DOI authority over mineral leases on federal lands and its entitlement to royalties; however, these laws do not apply to the Postal Service, which owns about 8,300 properties consisting of 20,805 acres of land. During FY 2015, the Postal Service managed 32 properties with oil and gas leases and received royalty payments totaling $101,700. Facilities is responsible for managing the Postal Service's oil and gas leases, including collecting, tracking, and validating royalty payments.

Summary

The Postal Service needs to improve its oversight of oil and gas mineral rights. Specifically, the Postal Service did not know which of its properties had oil and gas mineral rights and had no mechanism for tracking or maintaining properties with mineral rights. In addition, the Postal Service needs to improve its management of oil and gas leases and its collection, tracking, and validation of royalty payments. Further, the Postal Service did not retain mineral rights ownership or consider the value of mineral rights when acquiring or selling properties.

Based on our review of oil and gas lease documentation, we found that:

- Facilities could not provide copies of leases for five properties. The group was unable to determine if four of the five properties had leases in place. It also had no established lease for one property, even though the Postal Service received royalty payments valued at $14,108 for this property in FY 2015.
- Nineteen leases were not signed by one or both parties.
- Nine leases had a different lessee listed than the one in Postal Service records.
- Two leases that Facilities claimed to be inactive were still active. Based on our work, the Postal Service has collected $13,244 in royalty payments due since May 2013 for one of these properties and recovered a one-time lease payment in the amount of $34,343 for the other property.

The Postal Service needs to expand its knowledge of properties with oil and gas mineral rights, improve its management of oil and gas leases and associated royalty payments, and retain or consider the value of mineral rights when acquiring or selling properties.

Based on our review of royalty payments, we found that Facilities:

- Incorrectly recorded royalty payments of $87,592 instead of $101,700 for FY 2015.
- Did not record four royalty payments checks valued at $7,847.
- Did not validate the accuracy of royalty payments received.

These conditions occurred because the Postal Service considers the oil and gas mineral rights effort a passive revenue program. Management stated they do not have the resources to identify properties with mineral rights and rely on oil and gas companies to notify them. In addition, management does not have a written policy for managing oil and gas leases and collecting, tracking and validating royalty payments. In addition, management does not retain or consider the value mineral rights when acquiring or disposing of properties because it is not a part of the Postal Service's mission.

If the Postal Service does not properly manage its properties with mineral rights and does not properly collect, track, and validate royalty payments, it might not receive all entitled royalty revenue. In addition, not retaining mineral rights ownership or considering the value when acquiring or selling properties may result in the Postal Service not achieving the best price and losing potential revenue.

The DOI, through its examinations and data mining efforts, verifies data accuracy by evaluating information submitted by oil and gas companies. In addition, the DOI completes compliance reviews every 3 years to determine the reasonableness of oil and gas companies' reported revenue. By working with the DOI to identify best practices for collecting, tracking, and validating royalty payments, the Postal Service could ensure oil and gas companies are complying with lease terms and royalty payments are accurately reported and paid.

Oversight of Oil and Gas Mineral Rights

The Postal Service needs to expand its knowledge of properties with oil and gas mineral rights, improve its management of oil and gas leases and associated royalty payments, and retain or consider the value of mineral rights when acquiring or selling properties.

Properties with Oil and Gas Mineral Rights

The Postal Service did not know which of its properties had oil and gas mineral rights because it did not have a mechanism for tracking or maintaining properties with mineral rights. It also considers the oil and gas mineral rights effort a passive revenue program. Management stated they do not have the resources to identify properties with mineral rights and rely on oil and gas companies to notify them.

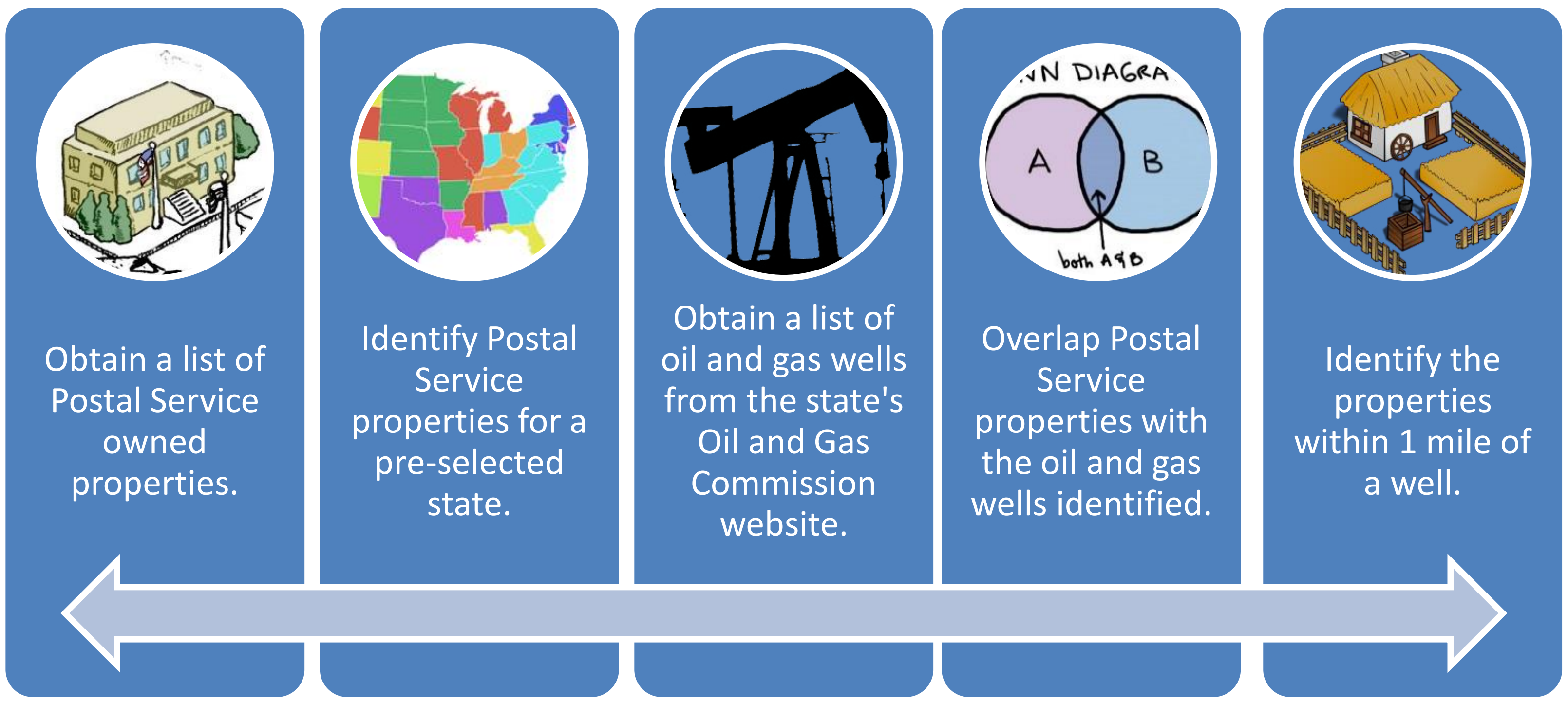
The Postal Service owns 8,314 properties and received oil and gas royalty payments for 31 of them (.004 percent) in FY 2015.[1] Although not all 8,314 properties are in states with an oil and gas presence, without tracking mineral rights, the Postal Service may be missing out on royalty revenue. In addition, according to the DOI, drilling wells without approval has been an increasing problem, with many of these incidents originating on privately owned surfaces.

1 The Postal Service managed 33 properties with oil and gas minerals rights; however, one of the properties did not require a lease or royalty payments as it was a one-time survey. An additional property did not receive payments during FY 2015 as the Postal Service was renegotiating the lease.

For example, the U.S. Postal Service Office of Inspector General's (OIG) Office of Investigations identified a property in ND for which the Postal Service owns the mineral rights and should have received royalty payments, as minerals were extracted from its land.[2] A lease for this property was signed in November 1996; however, Facilities did not have records for this location and did not receive royalty payments from 2006 to 2015, as ownership of the well changed several times. Based on this investigation, Facilities identified the current oil and gas company and received a $911 royalty payment for this property in FY 2016. However, due to multiple changes in well ownership, Facilities could not verify the accuracy of this payment.

To identify owned properties that could potentially have mineral rights, the Postal Service could use a target-based approach by focusing on states with a high oil and gas drilling presence like TX[3] — one of five states that supplied more than 80 percent of crude oil and 67 percent of natural gas produced in the U.S. Using the process depicted in Figure 1, the Postal Service could identify properties located within 1 mile of an oil or gas well in the selected state.

Figure 1. Process for Identifying Properties With Potential Mineral Rights

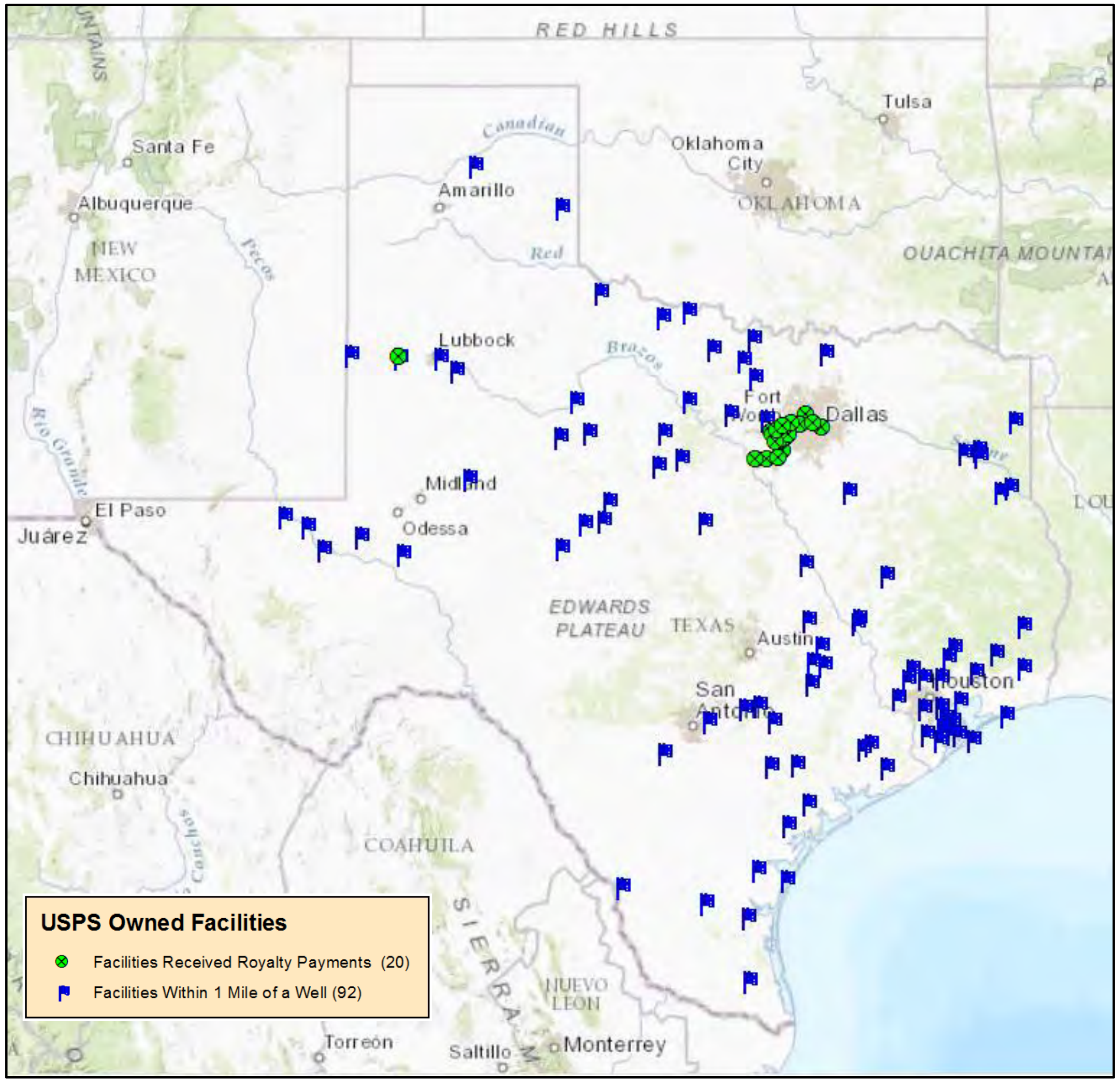


Source: OIG-developed process.

The Postal Service owns 603 properties in TX and, in FY 2015, it received oil and gas royalty payments totaling $80,630 for 20 of these properties. We obtained a list of 132,082 active oil and gas wells in TX, compared this list with the 603 properties, and identified 92 properties within 1 mile of a well, including the 20 properties that received royalty payments during FY 2015 (see Figure 2).

2 Although there is no drilling equipment on the Postal Service property, directional drilling occurred within 1.5 miles of this property. Directional drilling usually refers to drilling at non-vertical angles, including horizontally. It allows oil and gas well operators to approach a potentially productive area without the need for a well to be drilled directly above that area.
3 In 2013, TX, ND, CA, AK, and OK, and federal submerged lands in the Gulf of Mexico supplied more than 80 percent of the crude oil produced in the U.S. TX, PA, LA, WY, and OK produced 67 percent of total dry natural gas in the U.S.

Figure 2. Texas Postal Service Properties Within 1 Mile of an Oil or Gas Well



Source: OIG Facilities Risk Model and Railroad Commission of Texas.
Note: Due to the size of the map and the properties' close proximity, not all 20 properties that received royalty payments are visible.

Management of Oil and Gas Leases

The Postal Service needs to improve its management of oil and gas mineral rights leases. Based on our review of oil and gas lease documentation for the 32 properties, we found that:

- Facilities could not provide copies of leases for five properties. The group was unable to determine if a lease was in place for four of the five properties. It also had no established lease for one property, even though the Postal Service received royalty payments valued at $14,108 for this property in FY 2015. Because there was no established lease for one facility, its royalty checks had not been deposited and were held by Facilities. Facilities personnel are working with the oil and gas company to sign a lease for this property in FY 2016, and trying to determine whether the Postal Service is due any additional royalty payments for this location.

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Based on our work, the Postal Service received $13,244 in royalties due since May 2013 for one property and recovered a one-time lease payment in the amount of $34,343 for another property.

- Nineteen leases were not signed by one or both parties. When leases are not signed, neither party can enforce the terms of the contract against the other, which is particularly problematic in the event of a dispute about the terms of the agreement.

- Nine leases had a company listed as a lessee (tenant) that was different than the one in Postal Service records. Leases should be modified to reflect the correct company name. If the new name is due to a merger or acquisition, the lease is likely not enforceable against the new company absent assignment.[4]

- Facilities provided an additional 13 leases claimed to be inactive;[5] however, during our review, management contacted the oil and gas companies for these leases and determined that two were still active. The Postal Service has received $13,244 in royalties due since May 2013 for one of these properties and recovered a one-time lease payment in the amount of $34,343 for the other property.[6]

Facilities confirmed with the oil and gas companies that leases for seven of the 13 properties mentioned above were expired or had dry wells and were terminated. As of March 2016, Facilities was unable to confirm whether the remaining four leases were active or inactive. Facilities personnel stated they will follow up regularly with the companies but anticipate terminating the leases.

These conditions occurred because the Postal Service does not have a written policy in place outlining the responsibilities for managing oil and gas leases.

Management of Oil and Gas Royalty Payments

The Postal Service needs to improve its collection, tracking, and validation of oil and gas royalty payments. Facilities personnel recorded royalty payments using an Excel spreadsheet and relied on this spreadsheet as the sole mechanism for tracking royalty payments. This condition occurred because the Postal Service does not have a written policy in place outlining the responsibilities for collecting, tracking, and validating royalty payments.

Based on our review of royalty payments, we found that Facilities:

- Incorrectly recorded royalty payments of $87,592 in an Excel spreadsheet instead of $101,700, for FY 2015.[7] Incorrectly recording royalty payments will result in Facilities reporting inaccurate revenue.

- Did not record four royalty payments checks valued at $7,847 for FY 2015.

- Did not validate the accuracy of royalty payments received. We judgmentally selected 13 properties included in the royalty payment spreadsheet that received 63 royalty payments valued at $69,839; however, we could not validate the accuracy of the payments. Verification includes decimal interest[8], unit price, gross volume, taxes and withholdings, processing, transportation,

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4 A lease assignment is a legal transfer of the rights under the lease from one contracting party to another pursuant to the terms of the lease. In order to ensure that the contract is legally enforceable against the new entity, the lease must be assigned to it.
5 Typically, a lease is inactive either because the well is not producing or the lease has expired.
6 A check was initially issued to the Postal Service in 2010 for a 3-year paid upfront lease (for 2010 through 2013) but was not deposited. It was eventually reissued and deposited in February 2016.
7 This amount does not include royalty payments identified during our audit that Facilities did not track.
8 The decimal interest represents the ownership interest expressed as a decimal. It is calculated with the land tract size (land Postal Service owns), mineral interest percentage, lease royalty fraction, and the size of the producing unit.

Although mineral rights retention is not part of the Postal Service's mission, the Postal Service may not achieve the best purchase or sales price by not considering the value of mineral rights ownership when acquiring or selling properties, thereby resulting in a loss of potential revenue.

and gathering costs[9]. Although we could verify the decimal interest for two properties and the gross volume amounts for six properties, we were unable to obtain and verify the remaining elements. For example, we were not able to obtain unit price, as this is a confidential marketing contract executed between the pipeline and working interest owners and the Postal Service does not have access to this information.

The DOI collects and disburses royalty payments for federal properties but not for the Postal Service. The DOI, through its examinations and data mining efforts, verifies data accuracy by evaluating information submitted by oil and gas companies and ensuring necessary adjustments are made. It also processes royalty payments and matches them to the receivables. By exploring opportunities with the DOI to develop best practices in the payment validation processes, the Postal Service could ensure oil and gas companies are complying with lease terms and royalty payments are accurately reported and paid.

Retention and Value of Mineral Rights

The Postal Service did not retain mineral rights ownership or consider the value of mineral rights attached to a property when acquiring or selling properties. The Postal Service does not verify mineral rights ownership prior to a sale, but sells the property outright, including the mineral rights. Management stated they do not evaluate mineral rights when acquiring or disposing of properties because it is not part of the Postal Service's mission. According to a General Services Administration official, mineral rights should be valued and accounted for and the value of these rights should be recouped, retained or possibly sold separately.

Although mineral rights retention is not part of the Postal Service's mission, the Postal Service may not achieve the best purchase or sales price by not considering the value of mineral rights ownership when acquiring or selling properties, thereby resulting in a loss of potential revenue.

9 Gathering costs are charges for pipeline gathering of a product to a common sales point.

Recommendations

We recommend the vice president, Facilities:

1. Develop a process to identify and track owned properties with mineral rights and determine if the Postal Service is entitled to royalty payments.

2. Develop a policy that outlines the responsibilities for overseeing mineral rights, including managing oil and gas leases; collecting, tracking and validating royalty payments; and evaluating whether to acquire or dispose of mineral rights before buying or selling a property.

3. Review and update all oil and gas leases, including signatures and current tenant information.

4. Collaborate with the Department of the Interior to identify opportunities and best practices for collecting, tracking, and validating royalty payments.

Management's Comments

Management agreed with our findings and recommendations. Management also agreed that the Postal Service received $47,587 in royalty and lease payments but disagreed with the OIG classifying this monetary impact amount as a revenue loss.

Regarding recommendation 1, management stated they will develop a process to identify and track owned properties with mineral rights and determine if the Postal Service is entitled to royalties. The target implementation date is September 30, 2017.

Regarding recommendation 2, management will meet with the DOI to identify an efficient process to validate royalty payments. Management also agreed to the importance of evaluating whether to acquire or dispose of mineral rights prior to buying or selling a property and will address this in the new policy. The target implementation date is September 30, 2017.

Regarding recommendation 3, management agreed to review and update all oil and gas leases within 180 days. The target implementation date is March 31, 2017.

Regarding recommendation 4, management reached out to the DOI to determine the agency's interest in working with the Postal Service to identify opportunities and best practices for collecting, tracking, and validating royalty payments. Management will evaluate the DOI's suggestions or recommendations on a cost/benefit basis and determine if they are in the best interest of the Postal Service. The target implementation date is September 30, 2017.

See Appendix B for management's comments in their entirety.

Evaluation of Management's Comments

The OIG considers management's comments responsive to the recommendations in the report.

We classified royalty and lease payments the Postal Service received as a revenue loss because the Postal Service did not timely receive the funds due to the absence of mineral rights policies and procedures. Further, the Postal Service only received this revenue as a result of our audit.

All recommendations require OIG concurrence before closure. Consequently, the OIG requests written confirmation when corrective actions are completed. None of the recommendations should be closed in the Postal Service's follow-up tracking system until the OIG provides written confirmation that the recommendations can be closed.

Appendices

Click on the appendix title to the right to navigate to the section content.

Appendix A: Additional Information

Background

The U.S. is a world leader in producing natural resources, including oil, gas, coal, renewable energy, and non-energy minerals. Five states — TX, ND, CA, AK, and OK — and federal submerged lands in the Gulf of Mexico supply more than 80 percent of the crude oil produced in the U.S. Additionally, five states — TX, PA, LA, WY, and OK — produce 67 percent of the total dry natural gas in the country.

The DOI has administered the mineral leasing program for federal and American Indian lands for over a century. The DOI's Bureau of Land Management (BLM) is responsible for issuing and managing all leases for oil and gas exploration and development on lands owned or controlled by the federal government. BLM manages more federal land than any other agency — about 245 million surface acres of federal land and 700 million sub-surface acres of mineral estate. BLM manages split estate federal minerals, including non-federal surface, which is managed by the state, local governments, or private surface ownership overlying federal minerals.

The DOI's Office of Natural Resources Revenue (ONRR) collects royalty payments, rent, bonuses, penalties, and other revenue from over 2,900 organizations. ONRR's mission is to collect, disburse, and verify federal and Indian energy and other natural resource revenues on behalf of all Americans. They ensure that companies timely comply with laws, regulations, and lease terms; and pay every dollar due. They also ensure that states, tribes, Indian mineral owners, and other entities receive timely and accurate revenues and data.

Federal law gives the DOI authority over mineral leases on federal lands and its entitlement to royalties; however, these laws do not apply to the Postal Service, which owns about 8,300 properties consisting of 20,805 acres of land. During FY 2015, the Postal Service managed 32 properties with oil and gas leases and received royalty payments totaling $101,700. Facilities is responsible for managing the Postal Service's oil and gas leases, including collecting, tracking, and validating royalty payments.

Objective, Scope, and Methodology

Our objective was to assess the Postal Service's oversight of oil and gas mineral rights.

To accomplish our objective we:

- Interviewed Postal Service Facilities personnel to understand policies and procedures pertaining to managing oil and gas leases and royalty payments.
- Met with DOI officials to understand policies and procedures used to manage federal mineral rights leases and royalty payments.
- Analyzed royalty payments the Postal Service received in FY 2015.
- Determined whether an oil and gas lease was in place for each Postal Service property that received royalty payments in FY 2015.
- Reviewed active and inactive mineral rights leases managed by the Postal Service.

- Judgmentally selected a sample of 63 royalty payment checks received by the Postal Service in FY 2015 to determine if payments were accurate.

- Compared Postal Service-owned properties and well data to identify all such properties located within 1 mile of an oil and gas well.

We conducted this performance audit from August 2015 through September 2016, in accordance with generally accepted government auditing standards and included such tests of internal controls as we considered necessary under the circumstances. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. We discussed our observations and conclusions with management on August 9, 2016, and included their comments where appropriate.

We assessed the reliability of Postal Service-owned properties data by comparing the properties' locations listed in the electronic Facilities Management System[10] to the locations found in online records. We determined that the data were sufficiently reliable for the purposes of this report.

Prior Audit Coverage

The OIG did not identify any prior audits or reviews related to the objective of this audit.

10 The official Postal Service record for real property inventory and management.

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Appendix B: Management's Comments

TOM A. SAMRA
VICE PRESIDENT, FACILITIES

UNITED STATES
POSTAL SERVICE

August 30, 2016

SHERRY FULLWOOD
DIRECTOR, AUDIT OPERATIONS (A)

SUBJECT: Draft Audit Oversight of Oil and Gas Mineral Rights (Report Number SM-AR-16 DRAFT)

Thank you for the opportunity to review, and comment on the above referenced Draft Audit. Management does agree with most of the findings, and recommendations regarding the current oil, and gas mineral rights leases. Management disagrees with the monetary impacts identified, and have cited reasons set forth below.

FINDINGS

Finding #1:
Facilities could not provide copies of leases for five properties.

Management agrees with this finding. Management has taken actions to obtain leases as applicable for the five properties. The specifics of the actions are listed below:

1. Fort Smith, AR – Currently operated by Chesapeake, and royalties are being paid notwithstanding the fact that the lease document is missing. Management requested a copy of the lease from Chesapeake in 1/2016, and they responded that they were unable to locate a copy. Management contacted previous owners, and the O&G Records Clerk in AR, and none could find a copy of the lease. As a result, Management will request that Chesapeake enter into a new lease document, and will work to have this in place in the next 90 days.
2. Levelland, TX - Currently operated by Occidental Permian, and royalties are being paid. Management attempted to get a copy of this lease from Occidental Permian in 2011, but that attempt was unsuccessful. Management has made another request, and with the cooperation of Occidental Permian, if no copy is found, Facilities will work to have a new lease in place in the next 90 days.
3. Wilburton, OK - No lease required. Per letter on file from 1988, the State of OK provided certification of royalty interest in lieu of a Lease. (letter attached)
4. McCurtain, OK - No lease required. Per letter on file from 1990, the USPS holds royalty interest in a pooling order in lieu of a Lease. (letter attached)
5. Weld County, CO - Management is working to have a new lease in place with the OG Company in the next 90 days.

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WASHINGTON, DC 20260-1861
WWW.USPS.COM

Finding #2:
Nineteen leases were not signed by one or both parties.

Management agrees with this finding. Management is working to get fully executed leases for these sites within 180 days. Management points out that notwithstanding the fact that the leases were not fully executed, the parties to the leases are performing in accordance with the same.

Finding #3:
Nine leases had a different lessee listed than the one in Postal Service records.

Management agrees with this finding. It is difficult for the Postal Service to learn of the mergers, and acquisitions of oil, and gas exploration companies as these are frequent. Instead, Management relies upon the tenants to provide notice of change of ownership. When so notified, Management agrees to make changes to the names of the tenants in the eFMS system. Management notes that the changes in names of tenants has not impaired or delayed the payment of royalties to the Postal Service. Future leases will have provisions requiring notice of change of ownership.

Finding #4:
Two leases Facilities claimed were inactive were still active, and based on our work, the Postal Service collected $13,244 in royalty payments due since May 2013 for one of these properties.

Management agrees with this finding. Management has corrected the data entry error.

Finding #5:
Incorrectly recorded royalty payments of $87,592 instead of $101,700 for FY 2015.

Management agrees with this finding. The Postal Service has received the $101,700 royalty payments. Management has corrected the data entry error. .

Finding #6:
Did not record four royalty payments checks valued at $7,847.

Management agrees with this finding, and has corrected the data entry error. Management notes that the royalty checks were processed by the Postal Service, and the funds deposited.

Finding #7:
Did not validate the accuracy of royalty payments received.

Management agrees with this finding, however, Management believes that such validation would be extremely difficult for the Postal Service to achieve. As the OIG notes in its audit report,

> *"We judgmentally selected 13 properties included in the royalty payment spreadsheet that received 63 royalty payments valued at $69,839: However we could not validate the accuracy of the payments. Verification includes decimal interest, unit price, gross volume, taxes and withholdings, processing , transportation and gathering costs. Although we could verify the decimal interest for two properties and the gross amounts for six properties, we were unable to obtain and verify the remaining elements. For example, we were not able to obtain unit price, as this is confidential marketing contract*

executed between the pipeline and working interest owners and the Postal Service does not have access to this information.".

Management does not believe it would be any more successful than the OIG in such validation given the lack of information necessary to validate.

Finding #8:
Management does not have a written policy for managing oil, and gas leases, and collecting, tracking and validating royalty payments.

Management agrees with this finding. Management will issue a written policy within the next 30 days.

RECOMMENDATIONS

Recommendation #1:
Develop a process to identify and track owned properties with mineral rights, and determine if the postal service is entitled to royalty payments

Management Response
Management agrees with this recommendation subject to being able to work with the Department of Interior to see if there is a practical way to identify, and track mineral rights, and determine if the Postal Service is entitled to royalties.

Recommendation #2:
Develop a policy that outlines the responsibilities for overseeing mineral rights including managing oil and gas leases: collecting, tracking, and validating royalty payments: and evaluating whether to acquire or dispose of mineral rights before buying or selling a property

Management Response
Management agrees with the recommendation. With respect to properly validating royalty payments, Management will meet with the Department of Interior to learn if there is a practical way to validate. Management agrees that evaluating whether to sell or acquire mineral rights in sales, and acquisition of Postal Service property is important, and this evaluation will be addressed in the written policy.

Recommendation #3:
Review and update all oil, and gas leases, including signatures, and current tenant information

Management Response
Management agrees with this recommendation, and will work to review, and update existing oil and gas leases within 180 days.

Target Implementation Date: March 2017

Recommendation #4:
Collaborate with the department of the Interior to identify opportunities, and best practices for collecting, tracking, and validating royalty payments.

Management Response

Management agrees with this recommendation. Management has reached out to the Department of Interior to determine the agency's interest in working with Management to identify opportunities and best practices for collecting, tracking, and validating royalty payments. Management is awaiting a response. It is important to note that whatever suggestions or recommendations are proposed by the Department of Interior, if any, will need to be evaluated on a cost/benefit basis by Management to determine whether such suggestions or recommendations are in the best interest of the Postal Service.

MONETARY IMPACTS

Management agrees that the Postal Service did receive the $47,587 in royalties, and therefore, Management does not agree with the characterization of this amount as a "Revenue Loss."

In conclusion, Management appreciates the OIG's efforts in reviewing the oil, and gas leases, and Management's responses do not contain information that management believes may be exempt from disclosure under the FOIA.

Tom A. Samra

CC: Sally K. Haring, Manager CARM via email (CARMManager@USPS.GOV)

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