



The Secretary of Energy
Washington, D.C. 20585

June 27, 2013

The Honorable Joseph R. Biden, Jr.
President of the Senate
Washington, DC 20510

Dear Mr. President:

Enclosed please find the report entitled *U.S. Department of Energy Naval Petroleum Reserve No. 3 Disposition Decision Analysis and Timeline Report to Congress*. The report was prepared by the Department of Energy's Office of Fossil Energy and provides the Department's recommendation for disposing of this facility.

Title XXXIV of the Strom Thurmond National Defense Authorization Act for Fiscal Year 1999, Pub.L. 105-261 (October 17, 1998) appropriated funds for activities relating to the disposition of NPR-3. Section 3404 of that Act further directed the Secretary to continue to administer NPR-3 "until such time as the Secretary makes a determination to abandon oil and gas operations in Naval Petroleum Reserve Numbered 3 in accordance with commercial operating practices." Such a determination has been made by the Department per the November 2011 *Authorization of Continued Production of the Naval Petroleum Reserves Beyond April 5, 2012 Report to Congress* which proposed the development of a plan for the disposition of NPR-3.

This NPR-3 Disposition Decision Analysis and Timeline summarizes the analysis conducted. Two viable disposition options were considered and analyzed. As a result, the Department is recommending the disposition path of retaining the services of a private firm with expertise in the disposition of producing oil properties to sell the NPR-3 property under the authority of the National Defense Authorization Act of 1999 (10 USC 7420 note).

If you need additional information, please contact me or Mr. Brad Crowell, Acting Assistant Secretary for Congressional and Intergovernmental Affairs, at (202) 586-5450.

Sincerely,

A handwritten signature in blue ink, appearing to read "Ernest J. Moniz".

Ernest J. Moniz

Enclosure





The Secretary of Energy
Washington, D.C. 20585

June 27, 2013

The Honorable John Boehner
Speaker of the House of Representatives
Washington, DC 20515

Dear Mr. Speaker:

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This NPR-3 Disposition Decision Analysis and Timeline summarizes the analysis conducted. Two viable disposition options were considered and analyzed. As a result, the Department is recommending the disposition path of retaining the services of a private firm with expertise in the disposition of producing oil properties to sell the NPR-3 property under the authority of the National Defense Authorization Act of 1999 (10 USC 7420 note).

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U.S. Department of
ENERGY

Naval Petroleum Reserve No. 3 Disposition Decision Analysis and Timeline

Report to Congress
June 2013

United States Department of Energy
Washington, DC 20585

Message from the Secretary

The attached report provides a summary of the analysis supporting DOE's determination to dispose of the Naval Petroleum Reserve No. 3 (NPR-3) through sale of all right, title, and interest on the open market. NPR-3, created by Presidential order in 1915, covers approximately 9,481 acres of land in Wyoming known as the Teapot Dome oilfield. In the Naval Petroleum Reserves Production Act of 1976, Public Law 94-258 (April 5, 1976), Congress directed the Naval Petroleum Reserves to be developed and produced at their maximum efficient rates for an initial six-year period beginning in April 1976, and authorized the President to extend production in increments of up to three years after a required investigation of the necessity for continued production. The most recent *Authorization of Continued Production* was submitted to Congress by President Barack H. Obama in November 2011. The current authorized period of production will expire April 5, 2015.

NPR-3 is the only remaining Naval Petroleum Reserve administered by the Department of Energy (DOE). It consists of a small stripper well oilfield that currently produces about 200 barrels of crude oil per day. In Fiscal Year (FY) 2012, NPR-3 generated approximately \$4.8 million in revenues deposited into the U.S. Treasury, and the cost of production operations with overhead was \$3.3 million. Environmental restoration and remediation compliance costs were \$3.4 million during FY 2012. Under the current operating constraints, declining levels of production are projected to continue during the current authorization period and into the future. The most recent assessment of the proved reserves of NPR-3 is just over 400,000 barrels. Recapitalization of the productive capacity of NPR-3 has the potential to significantly increase the profitability of operations; however, it is most appropriate for the private sector to assume the risk of such an investment through lease or purchase of the property.

Co-located with NPR-3 is the Rocky Mountain Oilfield Testing Center (RMOTC). RMOTC was established in 1994 to utilize NPR-3's resources and facilities in order to assist the U.S. oil and gas industry, researchers, and academia in the field validation of new technologies through cost-shared arrangements. Recently, efforts have been made to make RMOTC a self-sustaining entity not dependent on appropriated funding. Beginning in FY 2011 cost-sharing was discontinued and all testing has been performed through 100 percent funds-in arrangements. While certain aspects of RMOTC may contribute to the marketability of the NPR-3 property as a whole, continued operation of RMOTC through 100 percent funds-in arrangements is unlikely to be in the best interest of a potential lessee or purchaser.

Section 3416 of the National Defense Authorization Act for FY 1996, Pub. L. 104-106 (February 10, 1996), required the Secretary of Energy (Secretary) to conduct a study regarding the naval petroleum reserves that "would maximize the value of the reserves to the United States." Title XXXIV of the Strom Thurmond National Defense Authorization Act for Fiscal Year 1999, Pub. L. 105-261 (October 17, 1998) (NDAA 99), authorized the disposition of NPR-3. Section 3404 of NDAA 99, entitled *Disposal of Naval Petroleum Reserve Numbered 3*, further directed the Secretary to continue to administer NPR-3 "until such time as the Secretary makes a determination to abandon oil and gas operations in *Naval Petroleum Reserve Numbered 3* in accordance with commercial operating practices." Additionally, section 3404(b) provided the following:

After oil and gas operations are abandoned in *Naval Petroleum Reserve Numbered 3*, the Secretary of Energy may dispose of the reserve as provided in this subsection. Subject to section 3406 [providing that any disposal of property at NPR-3 shall be subject to existing contracts or leases], the Secretary shall carry out any such disposal of the reserve by sale or lease or by transfer to another Federal agency. Any sale or lease shall provide for the disposal of all right, title, and interest of the United States in the property to be conveyed and shall be conducted in accordance with competitive procedures consistent with commercial practices, as established by the Secretary.

Section 3406(e) of NDAA 99 states that the consultation requirements of 10 U.S.C. 7431 are not applicable to the disposal of NPR-3. 10 U.S.C. 7431 requires the Secretary of Energy to consult with Congress and obtain the President's approval prior to contracting to "alienate from the United States the use, control, or possession of any part of the naval petroleum reserves" would not apply to the disposal of property under NDAA 99.

This report will satisfy several purposes. Both the Senate and the House requested information in the FY 2012 Energy and Water Development Appropriations report language which will be addressed by this report. The Senate Committee report language requests the Department "provide a report on the Department's obligations related to the reserves and a time-line for exiting from responsibility for the reserves." The House Committee directs the Department "to develop a long-term management plan for the RMOTC that includes a transition to a self-sustaining facility." Additionally, the President's FY 2012 Budget Request proposed the development of a plan for the disposition of NPR-3, and specified that the Department would analyze options and recommend a disposition path for NPR-3.

I am pleased to enclose a copy of the Naval Petroleum Reserve No. 3 Disposition Decision Analysis and Timeline. This report provides information on the Department's obligations related to the reserves, assesses the long-term sustainability of RMOTC, and summarizes the analysis of options conducted by DOE which are the basis of the recommended disposition path. Two primary disposition options were considered and analyzed: transfer to the Department of the Interior for leasing and sale of all right, title and interest on the open market. DOE has concluded that retaining the services of a private firm with expertise in the disposition of oil producing tracts is the best option for disposing of the NPR-3 property (including RMOTC) while maximizing the value of the property for the benefit of the US Treasury. This disposition process can be accomplished expeditiously, is expected to provide a positive net present value, and will minimize risks associated with long term environmental liabilities.

Pursuant to protocols, this report is being provided to the following Members of Congress:

- **The Honorable Joseph R. Biden, Jr.**
President of the Senate
- **The Honorable John Boehner**
Speaker of the House of Representatives

- **The Honorable Ron Wyden**
Chairman, Senate Committee on Energy and Natural Resources
- **The Honorable Lisa Murkowski**
Ranking Member, Senate Committee on Energy and Natural Resources
- **The Honorable Barbara Mikulski**
Chairwoman, Senate Committee on Appropriations
- **The Honorable Richard Shelby**
Ranking Member, Senate Committee on Appropriations
- **The Honorable Carl Levin**
Chairman, Senate Committee on Armed Services
- **The Honorable James Inhofe**
Ranking Member, Senate Committee on Armed Services
- **The Honorable Dianne Feinstein**
Chairman, Subcommittee on Energy and Water Development
Senate Committee on Appropriations
- **The Honorable Lamar Alexander**
Ranking Member, Subcommittee on Energy and Water Development
Senate Committee on Appropriations
- **The Honorable Harold Rogers**
Chairman, House Committee on Appropriations
- **The Honorable Nita Lowey**
Ranking Member, House Committee on Appropriations
- **The Honorable Lamar Smith**
Chairman, House Committee on Science, Space and Technology
- **The Honorable Eddie Bernice Johnson**
Ranking Member, House Committee on Science, Space and Technology
- **The Honorable Howard P. McKeon**
Chairman, House Committee on Armed Services

- **The Honorable Adam Smith**
Ranking Member, House Committee on Armed Services
- **The Honorable Fred Upton**
Chairman, House Committee on Energy and Commerce
- **The Honorable Henry A. Waxman**
Ranking Member, House Committee on Energy and Commerce
- **The Honorable Rodney P. Frelinghuysen**
Chairman, Subcommittee on Energy and Water Development
House Committee on Appropriations
- **The Honorable Marcy Kaptur**
Ranking Member, Subcommittee on Energy and Water Development
House Committee on Appropriations

If you need additional information, please contact me or Mr. Brad Crowell, Acting Assistant Secretary, Office of Congressional and Intergovernmental Affairs, at (202) 586-5450.

Sincerely,

A handwritten signature in black ink, appearing to read 'Ernest J. Moniz', with a stylized, flowing script.

Ernest J. Moniz

Executive Summary

The Naval Petroleum Reserve No. 3 (NPR-3), created by Presidential order in 1915,¹ covers approximately 9,481 acres of land in Wyoming known as the Teapot Dome oilfield. The Naval Petroleum Reserves Production Act of 1976, Public Law 94-258 (April 5, 1976) directed the Naval Petroleum Reserves to be developed and produced at their maximum efficient rates for an initial six-year period beginning in April 1976, and authorized the President to extend production periods in increments of up to three years, provided that he first orders an investigation of the necessity for continued production; that he submits to the Congress, at least 180 days prior to the expiration of each production period, a copy of the report on the investigation along with a Presidential certification that authorization of continued production is in the national interest; and that neither house of Congress adopts a resolution, within 90 days of receiving the report and certification, disapproving further production.

Pursuant to the Production Act, President Reagan authorized continued production of NPR-3 on three occasions; President George H. W. Bush, once; President Clinton, three times; President George W. Bush, three times; and President Obama, once. The last of these, the *Authorization of Continued Production of the Naval Petroleum Reserves beyond April 5, 2012 (Authorization of Continued Production)*, was submitted to Congress in November 2011).²

NPR-3 is the only remaining Naval Petroleum Reserve administered by the Department of Energy (DOE). It consists of a small stripper well oilfield that currently produces about 200 barrels of crude oil per day. In Fiscal Year (FY) 2012, NPR-3 generated approximately \$4.8 million in revenues deposited into the U.S. Treasury, and the cost of production operations with overhead was \$3.3 million. Environmental restoration and remediation compliance costs were \$3.4 million during FY 2012. Under the current operating constraints, declining levels of production are projected to continue during the current authorization period and into the future. The most recent assessment of the proved reserves of NPR-3 are just over 400,000 barrels. Recapitalization of the productive capacity of NPR-3 has the potential to significantly increase the profitability of operations; however, it is most appropriate for the private sector to assume the risk of such an investment through lease or purchase of the property.

Co-located with NPR-3 is the Rocky Mountain Oilfield Testing Center (RMOTC). RMOTC was established in 1994 to utilize NPR-3's resources and facilities in order to assist the U.S. oil and gas industry, researchers, and academia in the field validation of new technologies through cost-shared arrangements. Recently, efforts have been made to make RMOTC a self-sustaining entity not dependent on appropriated funding. Beginning in FY 2011 cost-sharing was discontinued and all testing has been performed through 100 percent funds-in arrangements. While certain aspects of RMOTC may contribute to the marketability of the NPR-3 property as a whole, continued operation of

¹ Order of Withdrawal, issued by President Wilson on April 30, 1915 (reproduced in United States Geological Survey Bulletin 623, *Petroleum Withdrawals and Restorations Affecting the Public Domain* (GPO 1916), downloaded from <http://books.google.com>).

² See, 157 CONG. REC. S7699 (daily ed. November 17, 2011 (Statement of President Obama)).

RMOTC through 100 percent funds-in arrangements is unlikely to be in the best interest of a potential lessee or purchaser.

The President's FY 2012 Budget Request proposed the development of a plan for the disposition of NPR-3, and specified that the Department would analyze options and recommend a disposition path for NPR-3. The November 2011 report to Congress, *Authorization of Continued Production*, further specified that the disposition path should maximize the value obtained for NPR-3 by the U.S. Government, while minimizing the cost of environmental remediation.

Accordingly, this NPR-3 Disposition Decision Analysis and Timeline summarizes two primary options for the disposition of NPR-3 (including RMOTC) and presents a recommended path forward. The legal authority for this recommended disposition path is Title XXXIV of the Strom Thurmond National Defense Authorization Act for Fiscal Year 1999, Pub. L. 105-261 (October 17, 1998) (NDAA 99).³ Additionally, DOE requested the General Services Administration (GSA) to conduct an analysis of each option consistent with the requirements of NDAA 99. GSA produced a report entitled "Review of Disposition Options Study Based on Highest and Best Use Analysis"⁴

DOE reviewed two primary options for the disposition of NPR-3:

- Transfer NPR-3 to the Department of the Interior (DOI) for leasing
DOE transfers all right, title, and interest in NPR-3 to DOI and DOI subsequently leases the property to oil and gas operators.
- Sell all right, title and interest in NPR-3 on the open market
DOE contracts with GSA or directly with a private firm, *i.e.*, an investment bank or oil and gas advisor, to sell all right, title, and interest in NPR-3 on the open market.

Maintaining DOE ownership and operation of the oilfield was not analyzed as an alternative to disposition. As determined in the November 2011 report to Congress, *Authorization of Continued Production*, this option is not in the national interest.

Based on GSA's analysis, DOE concluded that contracting with an investment banker or oil and gas advisor to sell the NPR-3 property under the NDAA 1999, is the preferred approach and is in the Government's best interest. Disposition of NPR-3 through an investment banker or oil and gas advisor with relevant experience can be accomplished expeditiously, is expected to provide a positive net present value (NPV), and will minimize risks associated with long term environmental liabilities.

Pending disposition of the property, DOE will continue its efforts to maximize proved reserves at NPR-3. With regard to continued production activities, cash flow projections made in the November 2011 report to Congress, *Authorization of Continued Production* (of NPR-3 for FY 2012 through FY 2015), indicate that profits from oil production under the then current operating conditions would average

³ Appears at 10 U.S.C. 7420 note.

⁴ See GSA Report entitled, *Review of Disposition Options Study Based on Highest and Best Use Analysis*, January 2013 located at http://www.rmotc.doe.gov/PDFs/RMOTC_Disposition_Analyses.pdf

\$145,000 per year, representing a five percent return on costs. The operating strategy through FY 2015 is designed to: a) generate revenues in excess of the costs of operation for deposit into the U.S. Treasury; b) maintain the value of the field pending disposition of the asset (as opposed to plugging wells and selling or transferring a non-producing oilfield) ; and c) defer and/or minimize costs incurred for environmental remediation.

Finally, in the FY 2012 Energy and Water Development Appropriations Bill, the Senate Committee report language requests the Department “provide a report on the Department’s obligations related to the reserves and a time-line for exiting from responsibility for the reserves.” This report contains the key milestones and the timeline for meeting these obligations in order to successfully and timely dispose of NPR-3. The obligations are divided into a three-phase NPR-3 Implementation Plan for selling NPR-3 with the goal of maximizing the value obtained for NPR-3 by the U.S. Government, and minimizing the cost of remediation to DOE. Over the course of the three phases, DOE will mitigate any adverse issues identified; complete the competitive sale of NPR-3; comply with relevant laws and regulations; and protect the safety and health of the NPR-3 staff, contractors, and visitors. DOE will close-out its activities in Casper, Wyoming by the end of calendar year 2015.



Naval Petroleum Reserve No. 3 Disposition Decision Analysis and Timeline Report to Congress

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I. Legislative Language

Two statutory enactments affecting the disposition of the U.S. Government's interest in Naval Petroleum Reserve No. 3 (NPR-3) appear as notes to 10 U.S.C. 7420: the National Defense Authorization Act for Fiscal Year 1996, Pub.L. 104-106 (Feb. 10, 1996) (NDAA 96), and the Strom Thurmond National Defense Authorization Act for Fiscal Year 1999, Pub.L. 105-261 (October 17, 1998) (NDAA 99).

National Defense Authorization Act for Fiscal Year 1996

Title XXXIV of the National Defense Authorization Act for Fiscal Year 1996 directed the Secretary of Energy, *inter alia*, to conduct a study of four options or combinations of options for maximizing the value of NPR-3:

- Retention and operation of the naval petroleum reserves.
- Transfer of all or a part of the reserve to the jurisdiction of another Federal agency for administration under 10 U.S.C. Chapter 641
- Transfer of all or a part of the reserve to the Department of Interior for leasing in accordance with the Mineral Leasing Act (30 U.S.C. 181, *et seq.*) and surface management in accordance with the Federal Land Policy and Management Act (43 U.S.C. 1701, *et seq.*).
- Sale of the interest of the United States in the naval petroleum reserves.

Section 3416 of NDAA 96 further directed the Secretary to retain an independent petroleum consultant to conduct a study of the above four options and provided that the study should examine the value to be derived by the United States from the transfer or sale of the reserves, including an assessment of the fair market value of the U.S. Government's interest. The assessment and estimate were to be made "in a manner consistent with customary property valuation practices in the oil and gas industry."⁵

The study required by NDAA 96 was completed in 1997.⁶ At the time that the study was completed, NPR-3 was producing about 1,100 barrels per day from 420 producing wells. The study recommended against divestment of NPR-3, and DOE accepted that recommendation. The recommendation was based on a conclusion that the costs of divestment would likely offset any revenues the United States would receive in a sale.⁷

The Strom Thurmond National Defense Authorization Act for Fiscal Year 1999

Title XXXIV of the Strom Thurmond National Defense Authorization Act for Fiscal Year 1999 authorized the disposition of NPR-3. Section 3404 of NDAA 99, *Disposal of Naval Petroleum Reserve Numbered 3*, further directed the Secretary to continue to administer NPR-3 "until such time as the Secretary makes

⁵ Section 3416(c).

⁶ See *Final Report: Study of Alternatives for Future Operations of the Naval Petroleum and Oil Shale Reserves (NPR3)*, by Gustavson Associates Geologists and Engineers, for the US Department of Energy, December 1996.

⁷ See, Statement of Patricia Fry Godley, Assistant Secretary for Fossil Energy, to the Subcommittee on Military Readiness, Committee on National Security, May 7, 1997, at http://fossil.energy.gov/news/testimony/1997/npr5_7.html

a determination to abandon oil and gas operations in Naval Petroleum Reserve Numbered 3 in accordance with commercial operating practices.” Additionally, section 3404(b) provided the following:

After oil and gas operations are abandoned in Naval Petroleum Reserve Numbered 3, the Secretary of Energy may dispose of the reserve as provided in this subsection. Subject to section 3406 [providing that any disposal of property at NPR-3 shall be subject to existing contracts or leases], the Secretary shall carry out any such disposal of the reserve by sale or lease or by transfer to another Federal agency. Any sale or lease shall provide for the disposal of all right, title, and interest of the United States in the property to be conveyed and shall be conducted in accordance with competitive procedures consistent with commercial practices, as established by the Secretary.

Section 3406(e) of NDAA 99 states that 10 U.S.C. 7431, requiring the Secretary of Energy to consult with Congress and obtain the President’s approval prior to contracting to “alienate from the United States the use, control, or possession of any part of the naval petroleum reserves,” would not apply to the disposal of property under NDAA 99.

II. Background

NPR-3, created by Presidential order in 1915,⁸ covers approximately 9,481 acres of land in Natrona County, Wyoming, known as the Teapot Dome oilfield. In the Naval Petroleum Reserves Production Act of 1976, Public Law 94-258 (April 5, 1976), Congress directed the Naval Petroleum Reserves to be developed and produced at their maximum efficient rates for an initial six-year period beginning in April 1976, and authorized the President to extend production in increments of up to three years, provided that he first orders an investigation of the necessity for continued production; that he submits to Congress, at least 180 days prior to the expiration of the current production period, a copy of the report on the investigation along with a Presidential certification that authorization of continued production is in the national interest; and that neither house of Congress adopts a resolution, within 90 days of receiving the report and certification, disapproving further production.

Subsequent to the enactment of Public Law 94-258, President Reagan authorized continued production of NPR-3 on three occasions; President George H. W. Bush, once; President Clinton, three times; President George W. Bush, three times; and President Obama, once. The last of these, the *Authorization of Continued Production of the Naval Petroleum Reserves beyond April 5, 2012* (*Authorization of Continued Production*), was submitted to Congress in November 2011.⁹

NPR-3 is the only remaining Naval Petroleum Reserve administered by the Department of Energy. It consists of a small stripper well oilfield that currently produces about 200 barrels of crude oil per day.

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⁹ See, 157 CONG. REC. S7699 (daily ed. November 17, 2011 (Statement of President Obama)).

The oilfield contains 680 wellbores completed in nine geologic formations. Under the current operating constraints, declining levels of production are projected to continue during the current authorization period and into the future. The most recent assessment of the proved reserves of NPR-3 are just over 400,000 barrels. Recapitalization of the productive capacity of NPR-3 has the potential to significantly increase the profitability of operations; however, it is most appropriate for the private sector to assume the risk of such an investment through lease or purchase of the property.

The President's FY 2012 Budget Request proposed the development of a plan for the disposition of NPR-3, and specified that the Department should analyze options and recommend a disposition path for NPR-3. The November 2011 *Authorization of Continued Production* report further specified that the disposition path should maximize the value obtained for NPR-3 by the U.S. Government, while minimizing the cost of environmental remediation to DOE.¹⁰

This report summarizes the due diligence and decision-making process that DOE used to evaluate and select a disposition path for NPR-3. At DOE's request, GSA developed a highest and best use analysis for the NPR-3 property, including an analysis of whether a sale of the U.S. Government's interest in NPR-3 or the transfer of NPR-3 to DOI for future leasing of the property would maximize the value obtained by the U.S. Government, and would minimize the cost of remediation to DOE.¹¹ In addition, qualitative data were gathered through structured interviews and meetings with a wide array of stakeholders and subject matter experts that included more than 50 sources:

- Federal government agencies with relevant expertise, including DOE's Office of Fossil Energy, DOE's Office of General Counsel, DOE's Casper Office, DOE's Office of Real Estate, DOE's Office of Historic Preservation, and GSA's Real Property Utilization and Disposal Division;
- State of Wyoming stakeholders and subject matter experts from the Wyoming Department of Environmental Quality, the Wyoming State Historic Preservation Office (SHPO), the Office of the Governor of Wyoming, the University of Wyoming School of Energy Resources, the DOI/Bureau of Land Management (BLM) Office of the State Director (Wyoming), the DOI/BLM Wyoming High Plains District Office, and the Natrona County (WY) Board of Commissioners;
- Oil and gas industry stakeholders from a spectrum of oil and gas companies;
- Investment bankers and oil and gas advisors experienced in selling oil and gas properties; and
- Federal and contractor employees who work at NPR-3.

¹⁰ The operating and disposal strategy of maximizing the value of NPR-3 while minimizing the cost of remediation to DOE was defined in the U.S. Department of Energy, *Authorization of Continued Production of the Naval Petroleum Reserves Beyond April 5, 2012: Report to Congress*, November, 2011, pp. ii and 2.

¹¹ See GSA Report entitled, *Review of Disposition Options Study Based on Highest and Best Use Analysis*, January 2013, located at http://www.rmotc.doe.gov/PDFs/RMOTC_Disposition_Analyses.pdf

III. Disposition Considerations and Alternatives

Disposal Utilizing the Federal Property and Administrative Services Act of 1949

DOE considered the applicability of the Federal Property and Administrative Services Act of 1949 (40 USC 101, *et seq.*) (Federal Property Act) as an alternative statutory basis for disposition. Under the Federal Property Act, DOE would be required to a) declare NPR-3 as excess, *i.e.*, no longer necessary to carrying out DOE's program responsibilities and b) utilize the General Services Administration (GSA) to dispose of the property using GSA established disposal procedures developed under the Act. This disposition process could lead to a wide variety of outcomes, including: a) sale to a for-profit corporation, b) sale to a non-profit corporation, c) transfer to DOI for lease, d) transfer to a U.S. Government agency other than DOI, and e) donation of NPR-3 to an educational institution. However, there would be no assurance under these scenarios that the U.S. Government would be able to maximize the value of the NPR-3 property or that the potential costs of environmental remediation would be minimized.

DOE determined that use of the Federal Property Act could lead to results that are inconsistent with the requirements of NDAA 99 which are specifically applicable to NPR-3. Furthermore, section 3403 (b) of the NDAA 99 provides the Secretary of Energy with specific authority to dispose of NPR-3; thereby, superseding the general asset disposal authority available under the Federal Property Act. Accordingly, DOE determined that utilization of the Federal Property Act procedures is not legally available.¹²

Special Transfer Authority

The Department considered disposition alternatives such as selling NPR-3 to a non-profit corporation for less than fair market value or donating NPR-3 to an educational institution. These alternatives were rejected by DOE because they are not authorized by section 3403 of the NDAA 99. Section 3403 (b) of NDAA 1999 provides mandatory requirements for the disposition of NPR-3 by limiting the disposition to sale or lease, in accordance with competitive practices, or by transfer to another Federal agency.

RMOTC as a Self-Sustaining User Facility

The House Committee in the FY 2012 Energy and Water Development Appropriations report language directs the Department "to develop a long-term management plan for the RMOTC that includes a transition to a self-sustaining facility." That concept has been analyzed and is described in this section.

RMOTC was established in 1994 as an internal NPR-3 project supported by joint grass roots efforts among DOE, industry, and academia. The purpose was to utilize NPR-3's resources and facilities to assist the U.S. oil and gas industry in the field validation of new technologies through cost-shared arrangements. From 1994 on, the production activities of NPR-3 and the R&D testing and demonstration activities at RMOTC took place side-by-side in an interdependent relationship.

¹² See e-mail from Clarke Turner to Ed Myers, *RE: Legal Issues RE: NPR-3 Disposition*, February 10, 2012.

The FY 2010 President's Budget proposed that, "RMOTC will identify and analyze options for becoming a self-sustaining user facility." In response, DOE conducted an analysis¹³ of the options to meet this goal and discontinued cost-shared testing at the beginning of FY 2011.

The FY 2011 Congressional Budget called for RMOTC to become self-sustaining by supporting only 100 percent funds-in testing projects. In an effort to operate more like a user facility, RMOTC attempted to increase the amount of funds received from partners to cover operating costs previously funded by appropriations. In order to cover these overhead and indirect expenses (absent appropriated funding), the cost to project sponsors of individual projects increased, making testing cost-prohibitive for many sponsors. As a result, the number of projects has diminished, and the customer base has shifted to large companies capable of paying the higher rates.

As reported in the GSA highest and best use analysis¹⁴, the brief period of 100 percent funds-in operating data and a lack of comparable facilities provide insufficient data from which to determine the feasibility of a self-sustaining RMOTC with much confidence. However, RMOTC must be viewed in the context of the disposition of the full property. Qualitatively, the GSA report found that it would not likely be feasible to bring RMOTC to its full productive use given the co-location with NPR-3 under single ownership. In addition, RMOTC is unlikely to be the highest and best use of the overall property. Therefore, while certain aspects of RMOTC may add value to the overall property, it is unlikely a purchaser would utilize RMOTC assets other than in service of NPR-3 production operations.

IV. Analysis of Disposition Options

This section provides a description of the alternative disposition options that were evaluated by GSA; describes the key assumptions that served as the boundary conditions for meeting the criteria of maximizing the value obtained for NPR-3 by the U.S. Government while minimizing the cost of remediation to DOE;¹⁵ and provides the net present value (NPV) analysis for the options. This NPV analysis is not intended to represent an appraised value that the government would receive if NPR-3 was either sold or leased. Instead, this NPV analysis is intended to serve as a decision tool to investigate the comparative risk involved with either sale or lease to the U.S. Government under current laws and regulations.

Results of Highest and Best Use Evaluation

DOE commissioned GSA to perform a real estate "highest and best use" determination and a "sale versus lease" study. GSA concluded that there is no appreciable market value in RMOTC's testing

¹³ See Summary Paper by DOE FE-32 entitled, *Rocky Mountain Oilfield Testing Center (RMOTC) Alternative Funding Options Analysis*, September 30, 2010.

¹⁴ pp14-15 of GSA Report entitled, *Review of Disposition Options Study Based on Highest and Best Use Analysis*, January 2013, located at http://www.rmotc.doe.gov/PDFs/RMOTC_Disposition_Analyses.pdf

¹⁵ The operating and disposal strategy of maximizing the value of NPR-3, while minimizing the cost of remediation to DOE was defined in the U.S. Department of Energy, *Authorization of Continued Production of the Naval Petroleum Reserves Beyond April 5, 2012: Report to Congress*, November, 2011, pp. ii and 2.

facilities or other resources such as geothermal, wind and solar capabilities if such facilities or resources were separated and marketed independently. Both the surface infrastructure and subsurface geology support selling or leasing the entire property as a whole for oil and gas production purposes.¹⁶ Additionally, GSA found that, if NPR-3 were transferred to DOI for leasing, DOI would be required to offer it as four different lease offerings, not because of market or operational reasons related to the property, but because applicable regulations limit the size of an individual competitive lease.¹⁷ GSA concluded that it would be in the U.S. Government's best interest to sell the property as one parcel and not transfer the property to DOI for leasing.

The new owner will own both the surface and mineral rights and will be less encumbered by the issues that arise with split estate properties. Selling the property is a more practical alternative to the State of Wyoming and Natrona County. The Natrona County Commissioners (NCC) prefer that NPR-3 be sold to a private company, rather than transferred to DOI.¹⁸ Also, the Governor of the State of Wyoming has indicated that the State prefers that NPR-3 be sold to a private company, rather than transferred to DOI.¹⁹

Two Disposition Processes and Outcomes

After eliminating the alternative approaches described above as either impractical or not supported by the law, DOE identified two viable options for in-depth analysis. Each option is based on the legal authority in NDAA 1999.

- Transfer NPR-3 to the Department of the Interior (DOI) for leasing
DOE transfers all right, title, and interest in NPR-3 to DOI and DOI subsequently leases the property to oil and gas operators.
- Sell all right, title and interest in NPR-3 on the open market
DOE contracts with GSA or directly with a private firm, *i.e.*, an investment bank or oil and gas advisor, to sell all right, title, and interest in NPR-3 on the open market.

Key Considerations of the Alternatives Analysis

- Disposition is defined as transferring title of 100 percent of surface and mineral rights to an owner other than DOE. No processes or outcomes that involve DOE maintaining ownership of NPR-3 (in part or whole) were considered in the analysis of alternative options.

¹⁶ See p5 of GSA Report entitled, *Review of Disposition Options Study Based on Highest and Best Use Analysis*, January 2013, located at http://www.rmotc.doe.gov/PDFs/RMOTC_Disposition_Analyses.pdf

¹⁷ 43 C.F.R. 3120.2-3.

¹⁸ See Appendix for letter from the Chairman, Natrona County Board of Commissioners to the Director of NPR-3, Re: Disposal of Naval Petroleum Reserve Numbered 3, July 16, 2012.

¹⁹ See Appendix for email from Rob Hurless (Energy Strategy Advisor to Governor Matt Mead) to Clarke Turner (Director, RMOTC) on September 13, 2012, which states, "The Governor is aware that the Secretary of Energy is currently studying various options to dispose of the Naval Petroleum Reserve as authorized under the National Defense Authorization Act of 1999 (10 U.S.C. 7420). The Governor believes that the best option for disposition for the State of Wyoming is sale to a private entity."

- The net present value was the primary criterion used to evaluate the disposition options and identify a recommended disposition path to maximize the value obtained for NPR-3 by the U.S. Government, while minimizing the cost of remediation to DOE.²⁰
- Environmental remediation necessary to comply with regulatory requirements differs from site restoration associated with the plugging and abandonment (P&A) of wells and the removal of real property (e.g., buildings).
- Estimated site restoration costs associated with P&A of wells and well-sites vary greatly based on whether the NPR-3 property is sold or leased. A purchaser will likely factor the future cost of P&A into their evaluation of the property's value. DOE estimates the P&A costs of all existing open wells to be \$7.2 million.
- In accordance with section 106 of the National Historic Preservation Act, 16 U.S.C. 470f, and the regulations implementing that Act (NHPA), 36 CFR Part 800, sale of NPR-3 to private ownership outside a U.S. Government agency is viewed as an "adverse effect" and will require either a Memoranda of Agreement (MOA) with the State Historic Preservation Office (SHPO), or legally binding and enforceable language to be included in the deed of sale that protects the cultural resources on the NPR-3 site. This includes possible tribal interest associated with Native American petroglyphs and tepee rings on the South end of the NPR-3 field, which will be explored during the consultation process in FY 2013 and FY 2014 as part of the National Environmental Protection Act (NEPA) process through U.S. Government-to-U.S. Government discussions among DOE, the Bureau of Indian Affairs (BIA) within DOI, and the appropriate tribal authorities.

Analyses of Alternative Disposition Options

The economic analysis of the two alternative disposition options is detailed in the GSA report.²¹ A single most-likely NPV was not calculated for each option. Rather, a best case and worst case NPV was calculated for leasing vs. sale. In performing a lease vs. sale NPV analysis for NPR-3, it was assumed that all costs and revenues were the same until disposition in the beginning of FY 2015. For simplification, the analysis begins in FY 2015. In order to determine how sensitive the analysis was to the numerous assumed variables, a worst and best case NPV was developed for both sale and lease, and a sensitivity analysis was performed for various discount rates. The analysis did not include any value received for personal property (equipment and materials) as the government would sell all personal property if either leased or sold. This analysis is not intended to represent an appraised value that the government would receive if NPR-3 was either sold or leased. Instead, this analysis is intended to serve as a decision tool to investigate the comparative risk involved with either sale or lease to the U.S. Government under current laws and regulations.

²⁰ The operating and disposal strategy of maximizing the value of NPR-3, while minimizing the cost of remediation to DOE was defined in the U.S. Department of Energy, *Authorization of Continued Production of the Naval Petroleum Reserves Beyond April 5, 2012: Report to Congress*, November, 2011, pp. ii and 2.

²¹ See GSA Report entitled, *Review of Disposition Options Study Based on Highest and Best Use Analysis*, January 2013, located at http://www.rmotc.doe.gov/PDFs/RMOTC_Disposition_Analyses.pdf

The results of the NPV sensitivity profile are presented in Table 1 for the best and worst cases for the leasing and sale options.²²

Net Present Value Profile

Discount Rate	Sale Worst Case NPV, \$	Sale Best Case NPV, \$	Lease Worst Case NPV, \$	Lease Best Case NPV, \$
0%	808,999	10,744,095	(28,499,579)	187,146,383
3.5%	795,203	10,560,869	(21,795,869)	133,733,282
5%	789,502	10,485,163	(19,976,820)	116,810,106
10%	771,350	10,244,092	(16,261,078)	76,842,493
15%	754,395	10,018,920	(14,312,939)	52,671,027

Table 1: Net Present Value Sensitivity Profile for Sale vs. Lease of NPR-3

The 3.5% discount rate is used for the comparison of the options which represents the 20-year nominal interest rate on Treasury notes and bonds per OMB Circular A-94. All of the production, revenue, cost, and economic assumptions that were used in the NPV analysis are provided in the GSA report.

Table 1 indicates the NPV to the U.S. Government of the lease option could range from negative \$21.8 million to \$133.7 million. Key drivers of this wide range are the price of oil, the amount of oil produced via enhanced oil recovery, and the near-term costs to the Government. For example, a key assumption in this best-case scenario is that the U.S. government could participate in upside potential whereby future lessees might increase production through implementation of enhanced oil recovery (EOR) technologies and/or future oil prices could increase. Conversely, the NPV to the U.S. government could be a negative \$21.8 million under the worst lease case, assuming that DOI would not lease the property for several years while the existing infrastructure is remediated and that no upside reserves would be produced. DOI has stated that it will not assume the liability of the open wellbores and structures on the NPR-3 site and would likely want all the wells plugged and abandoned and the buildings removed to decrease their liability and increase the probability of being able to lease it under its typical approach.²³

By comparison, the NPV range for the sale option is significantly smaller, \$0.8 million to \$10.6 million, but more certain. As stated previously, neither NPV range is intended to represent an appraised value. Both the lease and sale options will proceed through a competitive process by which a fair market value of the lease or sale will be determined. Therefore, the NPV analysis is most useful as a decision tool for highlighting relative risks associated with each option.

²² See GSA Report entitled, *Review of Disposition Options Study Based on Highest and Best Use Analysis*, January 2013, located at http://www.rmotc.doe.gov/PDFs/RMOTC_Disposition_Analyses.pdf

²³ See Appendix for letter from the Wyoming State Director, United States Department of Interior, Bureau of Land Management to the Director of NPR-3, July 27, 2012.

V. Disposition Path Determination

Based on the NPV analysis of the best and worst cases of the lease and sale options, DOE concludes that sale of all right, title and interest in NPR-3 on the open market is most likely to maximize the value obtained for NPR-3 by the U.S. Government, while minimizing the cost of environmental remediation to DOE. To achieve this disposition path, DOE will retain a private firm with relevant experience to market and sell the NPR-3 property to a for-profit or non-profit corporation under NDAA 99 where both for-profit and non-profit corporations would pay fair-market value for the property. DOE will consult with GSA as appropriate. This can be accomplished expeditiously, is expected to provide a positive net present value, and minimizes risk associated with lease surface infrastructure liabilities and uncertainties as well as long term environmental liabilities.

VI. Operations Strategy Prior to Disposition

The overall operating strategy for the period prior to final disposition will be to direct all efforts to maximizing the value of the field for final disposition. Minimal maintenance efforts of production facilities at NPR-3 will allow oil to be produced profitably through the disposition of the field. It is forecast that NPR-3 will generate revenues that exceed the operational costs prior to final disposition.

As described in the November 2011 report to Congress *Authorization of Continued Production*, cash flow projections for continued operations of NPR-3 for FY 2012 through FY 2015 indicate that profits from oil production will average \$145,000 per year, which represents a five percent return on costs. Given the range of uncertainty in oil prices and revenue projections, production economics will be monitored monthly. Transfer of the field to new owners is expected to take place during FY 2015.

To achieve this positive cash flow operationally, NPR-3 has devised a strategy to rotate production among its nearly 550 wells available for production. Through FY 2014, NPR-3 will produce about 120 wells daily. There will be no capital investments made to existing wells. As the producing wells become “pumped off,” *i.e.*, there is no more oil in the wellbore, production activities will stop and a new group of wells will be produced. Since the primary mechanism for production is gravity drainage, the wells that are turned off will refill with oil to be produced at a later time. Wells will be rotated for production, thus reducing the overall decline rate of the field. Allowing the wells to sit idle for an extended period of time, *i.e.*, throughout the disposition process, is not a viable option as such action could result in damage to the pumping equipment and could result in non-compliance with Wyoming oil and gas regulations.

DOE has concluded that maintaining crude oil production in the field provides added value for disposition (vs. plugging and abandonment of the wells). Wells will not be shut-in or plugged and abandoned unless they fail the mechanical integrity test and are out of compliance with regulations. If it is determined that a well could be produced profitably by a private party, it will not be plugged. Infrastructure and wells that add no value to the field will be plugged and abandoned in accordance with state law. To minimize operating expenses, all maintenance will be curtailed except as required

for health, safety, and environmental protection. Typically, if a well stops producing because of mechanical problems, it will be plugged and abandoned since the cost of major repairs will not provide a timely payout. Repair of infrastructure will be limited to safety and health only.

The cost-shared portion of the RMOTC testing program was discontinued as of October 1, 2010. However, testing of 100 percent funds-in projects will continue on a limited basis, provided that the testing does not conflict with the disposition strategy.

VII. Timeline for Disposition of NPR-3

In the FY 2012 Energy and Water Development Appropriations Bill, the Senate Committee report language requests the Department “provide a report on the Department’s obligations related to the reserves and a time-line for exiting from responsibility for the reserves.” The following are the key milestones and the timeline for meeting these obligations in order to successfully and efficiently dispose of NPR-3. The obligations are divided into a three-phase NPR-3 Implementation Plan for selling NPR-3 with the goal of maximizing the value obtained for NPR-3 by the U.S. Government, and minimizing the cost of remediation to DOE. Over the course of the three phases, DOE will mitigate any adverse issues identified; comply with relevant laws and regulations; and protect the safety and health of the NPR-3 staff, contractors, and visitors. The three phases are:

- Phase I: Continue to Prepare NPR-3 for Sale
- Phase II: Sale of NPR-3
- Phase III: Closeout the DOE Casper Office

Phase I: Continue to Prepare NPR-3 for Sale (FY 2013 – mid-FY 2014)

Milestone	Timeline
Reorganize the Service Support Contractor (SSC) staff to support disposition activities	July 31, 2012
Develop an Employee Transition Plan for managing the Federal staff	October 26, 2012
Reorganize the Federal staff to support disposition activities	January 31, 2013
Disposition Decision: Sell vs. Lease	July 1, 2013
Initiate the regulatory consultation processes required by the NHPA.	July 2, 2013
Complete the regulatory consultation process required by the NEPA .	September 30, 2013
Issue IFB for an independent firm to conduct rigorous Oil and Gas Reserves Evaluation including preparing a reserves upside report.	September 30, 2013
Obtain regulatory closure permits on all facilities that require regulatory oversight from the State of Wyoming, including closeout permits as needed.	September 30, 2013

Contract with an independent firm to conduct a rigorous Oil and Gas Reserves Evaluation	November 30, 2013
Complete mechanical integrity tests of all idle wells	December 31, 2013
Issue IFB for investment banker or oil and gas advisor services to sell the NPR-3 property	January 31, 2014
Complete regulatory consultation processes required by the NHPA by signing an MOA with WYSHPO and ACHP.	March 31, 2014
Independent firm completes Oil and Gas Reserves Evaluation and Upside Report	April 30, 2014
Award contract with an investment banker or oil and gas advisor experienced in the marketing and sales of oil and gas producing properties to sell the NPR-3 property	May 31, 2014
Complete all production enhancement (well workovers and facility repair and rehabilitation) projects within available budgetary resources	May 31, 2014
Complete plugging and abandonment of wells that pose a risk to the environment and/or have no potential value to a new owner	May 31, 2014

Phase II: Sale of NPR-3 (mid FY 2014 – early FY 2015)

Milestone	Timeline
Investment banker begins marketing NPR-3	June 30, 2014
Investment banker completes competitive sale	September 30, 2014
Complete phased disposition of majority of NPR-3 field personal property	September 30, 2014
DOE evaluates and accepts winning bid	October 31, 2014
Sales contract awarded	November 30, 2014
Right, title, and interest of NPR-3 transferred to new owner	December 31, 2014

Phase III: Closeout the DOE Casper Office (early FY 2015 – early FY 2016)

Milestone	Timeline
Close out operational contracts and agreements	November 30, 2015
Complete remaining mitigation activities resulting from regulatory consultation processes	November 30, 2015
Complete phased shut down of Casper main office IT and communication systems	December 31, 2015

Casper office lease expires	December 31, 2015
Forward remaining contracts required for office closing activities to Headquarters Procurement Operations for close out	December 31, 2015
Complete records disposition activities	December 31, 2015
Dispose of Casper office personal property	December 31, 2015

VIII. Conclusion

Based on the NPV analysis of the best and worst cases of the lease and sale options, DOE concludes that sale of all right, title and interest in NPR-3 on the open market is most likely to maximize the value obtained for NPR-3 by the U.S. Government, while minimizing the cost of environmental remediation to DOE. To achieve this disposition path, DOE will retain a private firm with relevant experience to market and sell the NPR-3 property to a for-profit or non-profit corporation under NDAA 99 where both for-profit and non-profit corporations would pay fair-market value for the property. DOE will consult with GSA as appropriate. This can be accomplished expeditiously, is expected to provide a positive net present value, and minimizes risk associated with lease surface infrastructure liabilities and uncertainties as well as long term environmental liabilities