



United States
General Accounting Office
Washington, D.C. 20548

Resources, Community, and
Economic Development Division

B-262172

August 1, 1995

The Honorable John McCain
United States Senate

Dear Senator McCain:

You asked us to review draft legislation proposing the sale of Naval Petroleum Reserve Number 1 (NPR-1).¹ Specifically, you asked us to review the proposed method of sale to determine if it will provide an equal opportunity to all prospective purchasers and will yield the maximum proceeds to the federal government. In addition, you asked for any suggestions that we might have to improve this legislation to ensure that the government receives the best value for the reserve. As requested, we have also included a summary of earlier suggestions that we made to your office during the drafting of this legislation. (See enc. I.) Because the legislation we reviewed is in draft form and subject to change, our views are preliminary and could change on the basis of the language of the legislation in its final form.

In summary, the method of sale as proposed in the draft legislation, involving an invitation for bids, appears consistent with efforts to provide equal opportunity to all prospective purchasers. The proposed method of sale--by stipulating acceptance of the highest responsible offer that meets or exceeds the minimum acceptable price, which was determined as the net present value that the Department of the Treasury would receive from the reserve if the reserve were not sold--appears consistent with efforts to yield a fair market value to the government.

BACKGROUND

NPR-1, at Elk Hills, California, is one of the 10 largest domestic producing oil fields in the lower 48 states. It is also one of the nation's top producing gas fields. The U.S.

¹This proposal was to be incorporated in the Fiscal Year 1996 Defense Authorization Act.

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government owns about 78 percent of the reserve, while Chevron U.S.A. owns the remaining 22 percent. The reserve is managed by the Department of Energy (DOE) and operated under contract by Bechtel Petroleum Operations, Inc. Currently, both the administration and the Congress are proposing to sell the government's share of the reserve to the private sector.

THE PROPOSED METHOD OF SALE APPEARS
CONSISTENT WITH EFFORTS TO ENSURE EQUAL
OPPORTUNITY TO ALL POTENTIAL BUYERS

The method of sale contained in the draft legislation appears consistent with efforts to provide equal opportunity to all prospective purchasers. It includes an invitation for bids, will identify all equipment and facilities included in the sale, and provides for the acceptance of one or more contracts for the sale.² We did not identify any language in the draft legislation that excludes prospective buyers. While NPR-1 might prove unaffordable to a small prospective bidder, we did not identify any language in the draft legislation that precludes a group of prospective bidders from forming a consortium for the purpose of bidding on this property.

THE PROPOSED METHOD OF SALE APPEARS
CONSISTENT WITH EFFORTS TO YIELD A
FAIR MARKET VALUE TO THE GOVERNMENT

By stipulating acceptance of the highest responsible bid that meets or exceeds the minimum acceptable price set by the Secretary of Energy, the proposed method of sale appears consistent with efforts to yield a fair market value to the government. Establishing this minimum acceptable price for this reserve, which is defined as what the government could reasonably earn by continuing to own this reserve, makes receiving a fair market value more likely.³

The proposed method of sale also requires that equity or ownership shares in the reserve belonging to the government

²The draft legislation does not specify how the multiple-contract provision would work.

³See Naval Petroleum Reserves: Opportunities Exist to Enhance Its Value to the Taxpayer (GAO/T-RCED-95-136, Mar. 22, 1995) and Naval Petroleum Reserves (GAO/RCED-95-141R, Mar. 17, 1995). Fair market value is calculated by using private-sector rates of return.

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and Chevron be finalized before selling the reserve. Equity shares determine how each partner shares in the expenses and profits of the reserve and how much of the hydrocarbons (oil, gas, etc.) belongs to the government and to Chevron. Previously, we reported that if equity shares are not finalized and the government decides to sell its share of the reserve, the price it receives could be discounted to reflect uncertainty about the size of its shares.

Finally, we believe that the proposed method of sale provides the government with appropriate expertise to ensure a fair market value. The proposed method of sale authorizes the Secretary of Energy to employ independent experts to value the reserve and finalize equity shares and to use an investment banker to administer the sale.

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In reviewing the draft legislation, we compared its contents with findings from our previous reports dealing with ways to enhance the value of NPR-1. A listing of these reports is contained in enclosure II. We performed our review from June through July 1995.

We will send copies of this report to the Secretary of Energy and make copies available to others on request. If we can be of further assistance, please feel free to call me at (202) 512-3841.

Sincerely yours,



Victor S. Rezendes
Director, Energy and Science
Issues

Enclosures - 2

GAO'S SUGGESTIONS FOR DRAFT LEGISLATION ON THE SALE OF NPR-1

During the drafting of this legislation, we met with the office of Senator John McCain a number of times to discuss the results of our work on the Naval Petroleum Reserve No. 1 (NPR-1). On the basis of our work, we made a number of suggestions for inclusion in the proposed legislation to further enhance the opportunity to all potential buyers and fair market value to the government.

To help ensure that all potential buyers have an "even playing field," we suggested that the draft legislation require that the Secretary of Energy publish in the Federal Register a notice of intent to sell NPR-1. In addition, we suggested that the Department of Energy (DOE) make economic, technical, and geological data describing NPR-1 available to prospective buyers at the time of the announcement of intent to sell, rather than waiting until the announcement of the invitation for bids. These suggestions have been incorporated in the latest version of the proposed legislation.

We made other suggestions regarding the proposed method of sale that could increase the value that the government receives for the reserve. The draft legislation contained conflicting time requirements for DOE to make decisions during the sales process. For example, section (c)(4) of the draft legislation required the Secretary of Energy to publish an invitation for bids within 7 months, while section (c)(3) allowed the Secretary of the Treasury and Director, Office of Management and Budget (OMB), to have the draft contract before them for "approval" indefinitely. We suggested that Treasury and OMB be required to approve or disapprove the draft contract in time for the Secretary of Energy to meet the invitation-for-bid publication deadline. Additionally, we noted that the Secretary of Energy was directed in section (c)(5) to "accept" the highest responsible offer within 10 months but prohibited in section (j) from entering into a final contract until 31 days after notifying appropriate congressional committees. We suggested that the Secretary be required to instead "identify" the highest responsible offer within 10 months.

We also pointed out that the draft legislation did not require the Secretary to notify congressional oversight committees of potential obstacles to concluding the sale of NPR-1 within 1 year. We suggested that a provision be included to require the Secretary to notify the appropriate committees of any potential noncompliance with the statute's deadlines.

RELATED GAO PRODUCTS

Naval Petroleum Reserves: Opportunities Exist to Enhance Its Value to the Taxpayer (GAO/RCED-95-136, Mar. 22, 1995).

Naval Petroleum Reserves (GAO/RCED-95-141R, Mar. 17, 1995).

Naval Petroleum Reserve: Opportunities Exist to Enhance Its Profitability (GAO/RCED-95-65, Jan. 12, 1995).

Naval Petroleum Reserve: Limited Opportunities Exist to Increase Revenues From Oil Sales in California (GAO/RCED-94-126, May 24, 1994).

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