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We have completed an audit of the Division of Minerals. This audit is part of the ongoing program of the Legislative Auditor as authorized by the Legislative Commission. The purpose of legislative audits is to improve state government by providing the Legislature, state officials, and Nevada citizens with independent and reliable information about the operations of state agencies, programs, activities, and functions. The results of our audit, including findings, conclusions, recommendations, and the Division's response, are presented in this report.

We wish to express our appreciation to the management and staff of the Division of Minerals for their assistance during the audit.

Respectfully presented,

A handwritten signature in black ink, appearing to read "Paul V. Townsend".

Paul V. Townsend, CPA
Legislative Auditor

March 28, 2006
Carson City, Nevada

STATE OF NEVADA
COMMISSION ON MINERAL RESOURCES
DIVISION OF MINERALS
AUDIT REPORT

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EXECUTIVE SUMMARY

COMMISSION ON MINERAL RESOURCES DIVISION OF MINERALS

Background

The Nevada Division of Minerals, a part of the Commission on Mineral Resources, is responsible for administering programs and activities to promote, advance, and protect mining and the development and production of petroleum and geothermal resources in Nevada. The Commission on Mineral Resources is responsible for advising the Governor and Legislature on mineral related issues. The Commission also adopts the regulations administered by the Division.

The Division focuses its efforts on three main areas: industry relations and public affairs; regulation of oil, gas, and geothermal drilling activities and well operations; and abandoned mine lands. The Division administers the following programs: Abandoned Mine Lands (AML), Reclamation Bond Pool, Education, Mining, and Oil, Gas, and Geothermal.

The Division's offices are located in Carson City and Las Vegas. As of June 30, 2005, the Division had nine full-time employees. In addition, six summer interns were assigned to the AML program. The Division is self-funded primarily from fees and grants and had expenditures totaling approximately \$1 million in fiscal year 2005.

Purpose

The purpose of this audit was to evaluate the Division of Minerals' financial and administrative practices, including whether transactions were carried out in accordance with applicable state laws, regulations, and policies. Our audit included a review of the Division's financial and administrative activities for the fiscal year ended June 30, 2005.

EXECUTIVE SUMMARY

COMMISSION ON MINERAL RESOURCES DIVISION OF MINERALS

Results in Brief

The Division of Minerals substantially complied with laws, regulations, and policies significant to its financial administration. However, we noted some weaknesses in the Division's oversight of wells and performance bonds and reporting performance indicators and accounts receivable. Specifically, the Division did not witness pressure tests of all geothermal wells, and performance bonds did not always meet the Division's requirements. In addition, performance indicators were not always accurate, supported by adequate documentation, or clearly defined. Finally, additional procedures will help ensure that all accounts receivable are properly recorded and reported.

Principal Findings

- Although required by regulations, the Division did not witness all tests of blowout prevention devices during the drilling of geothermal wells. Of the seven wells drilled in fiscal year 2005, the Division witnessed three and relied on engineering test reports for the remaining four. Regulations require all necessary precautions must be taken to keep wells under control and operating safely at all times. (page 8)
- Four of nine oil and gas well operators' bonds were less than the amount required. Each operator submitted a \$25,000 bond. However, the minimum bond required by the Division's regulations ranged from \$30,000 to \$50,000. Bonds help ensure that an oil or gas well is properly operated, repaired and plugged. (page 9)

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COMMISSION ON MINERAL RESOURCES DIVISION OF MINERALS

- The Division did not always terminate participation in the state's Reclamation Bond Pool as required. Participation must be terminated if an operator fails to pay their premium within 70 calendar days after the due date. However, two operators were allowed to participate even though they had not paid a premium within the 70-day limit. Timely premium payments help ensure the bond pool has sufficient funds to reclaim land disturbances if an operator fails to do so. (page 9)
- Our analysis of the Division's five performance indicators presented in the 2005-2007 Executive Budget, showed that one was reliable, one was unreliable, and three could not be verified because the underlying data was not readily available. In addition, the description of one indicator did not properly describe the reported information. Unreliable indicators can misrepresent the actual results of an agency's operational activities. (page 11)
- The Division's procedures should be revised to ensure all accounts receivable are properly recorded and reported. Specifically, procedures lacked clear direction on how to define, age, and report accounts receivable. As a result, not all bond pool premiums were billed timely. In addition, the Division's June 30, 2005, accounts receivable report submitted to the Office of the State Controller was understated. (page 12)

Recommendations

This audit report contains six recommendations to improve the Division's oversight of wells and performance bonds and controls over performance indicators and accounts receivable. Specifically, the Division should witness geothermal well pressure tests as required, and ensure performance bonds meet minimum requirements and

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COMMISSION ON MINERAL RESOURCES DIVISION OF MINERALS

are terminated in accordance with regulations. In addition, the Division should implement controls to help ensure performance indicators are reliable and all accounts receivable are properly recorded and reported. (page 23)

Agency Response

The Agency, in its response to our report, accepted all six recommendations. (page 17)

Introduction

Background

The Nevada Division of Minerals, a part of the Commission on Mineral Resources, is responsible for administering programs and activities to promote, advance, and protect mining and the development and production of petroleum and geothermal resources in Nevada. The Commission on Mineral Resources is responsible for advising the Governor and Legislature on mineral related issues. The Governor appoints the seven members of the Commission to 4-year terms. The Commission also adopts the regulations administered by the Division.

The Division's mission is to conduct activities to further the responsible development and production of the State's mineral resources to benefit and promote the welfare of the people of Nevada. The Division focuses its efforts on three main areas: industry relations and public affairs; regulation of oil, gas, and geothermal drilling activities and well operations; and abandoned mine lands.

The Division of Minerals administers the following programs:

Abandoned Mine Lands (AML) Program – provides for public safety by identifying and ranking dangerous conditions at mines that are no longer operating, and by securing dangerous orphaned mine openings. The program also educates the public to recognize and avoid hazardous abandoned mines.

Bond Pool Program – provides reclamation bonds for those mining operators that cannot obtain a bond from commercial means. The participants in the pool pay a deposit and quarterly or annual premiums thereafter.

Education Program – promotes the minerals industry and the importance of mineral resources. The Division has developed educational materials for grade levels K-12; co-sponsors semiannual education workshops; and performs numerous classroom presentations.

Mining Program – compiles annual data on all active mines in Nevada and maintains the State's mine registry. Information concerning mining operations and production is made available to the public through a yearly publication.

Oil, Gas, and Geothermal Program – responsibilities include permitting, inspecting, and monitoring all oil, gas, and geothermal drilling activities on both public and private lands in Nevada. Staff also monitor the production of oil, gas, and geothermal resources to ensure proper management and conservation. Nevada is a member of the Interstate Oil and Gas Compact Commission.

The Division’s offices are located in Carson City and Las Vegas. As of June 30, 2005, the Division had nine full-time employees. In addition, six summer interns were assigned to the AML program. The Division is funded primarily from fees and grants and had expenditures totaling about \$1 million in fiscal year 2005. Exhibit 1 shows the Division’s and the Reclamation Bond Pool’s funding and expenditures for the fiscal year ended June 30, 2005.

Exhibit 1

**Funding and Expenditures
Fiscal Year 2005**

	Division of Minerals	Reclamation Bond Pool
<u>Funding</u>		
Beginning Cash	\$ 447,206	\$1,027,449
Fees	1,124,985	72,277
Grants	97,500	--
Deposits	--	499,680
Interest	14,817	26,884
Transfers	11,865	--
Total Funding	1,696,373	1,626,290
<u>Expenditures</u>		
Personnel	722,217	--
Operating	167,384	11,865
Abandoned Mine Support	125,131	--
Total Expenditures	1,014,732	11,865
Ending Cash	\$ 681,641	\$1,614,425

Source: State Accounting System.

The Division also holds performance bonds for oil, gas, and geothermal wells. These bonds can be CD’s, sureties, or cash deposits. As of June 30, 2005, cash deposits and accumulated interest from these bonds totaled \$338,409.

Scope and Objective

This audit is part of the ongoing program of the Legislative Auditor as authorized by the Legislative Commission, and was made pursuant to the provisions of NRS 218.737 to 218.893. The Legislative Auditor conducts audits as part of the Legislature's oversight responsibility for public programs. The purpose of legislative audits is to improve state government by providing the Legislature, state officials, and Nevada citizens with independent and reliable information about the operations of state agencies, programs, activities, and functions.

This audit included the financial and administrative activities of the Division of Minerals for the fiscal year ended June 30, 2005. The objective of our audit was to evaluate the Division's financial and administrative practices, including whether transactions were carried out in accordance with applicable state laws, regulations, and policies.

Findings and Recommendations

The Division of Minerals substantially complied with laws, regulations, and policies significant to its financial administration. However, we noted some weaknesses in the Division's oversight of wells and performance bonds and reporting performance indicators and accounts receivable. Specifically, the Division did not witness pressure tests of all geothermal wells, and performance bonds did not always meet the Division's requirements. In addition, performance indicators were not always accurate, supported by adequate documentation, or clearly defined. Finally, additional procedures will help ensure that all accounts receivable are properly recorded and reported.

Oversight of Wells and Performance Bonds Needs Improvement

The Division's monitoring procedures did not ensure geothermal well pressure tests were conducted in accordance with regulations. Furthermore, the Division accepted certain performance bonds for amounts less than required. Finally, the Division did not always terminate participation in the state's Reclamation Bond Pool when operators failed to make timely premium payments. Pressure testing helps ensure wells are operated safely and bonds help ensure resources are available to plug wells and to fund mine reclamation projects.

Division Did Not Always Witness All Well Pressure Tests

Regulations require the Division to witness pressure tests of geothermal well safety equipment during the drilling process. However, the Division did not witness all tests conducted in fiscal year 2005. Of the seven wells tested, Division personnel observed three and relied on information submitted by the well operators to assess the safety of the remaining four.

NAC 534A.270 requires certain steps be taken to keep wells under control and operating safely at all times. This includes the installation of equipment during the drilling process for the prevention of a blowout. Furthermore, the equipment must be tested under pressure and the Division must witness the tests. According to Division personnel, it is not always feasible to witness these tests. Consequently, the Division

reviews the engineering test results submitted by well operators with established reliability. However, regulations do not address the review of engineering reports in lieu of witnessing the tests.

Certain Bonds Did Not Meet State Requirements

A well operator must submit a bond or place a deposit with the Division when obtaining a permit to drill a gas or oil well. The bond or deposit helps ensure the well is repaired in a manner which does not cause waste and is properly plugged if dry or abandoned. However, some bonds did not meet the minimum state bonding requirements. These bonds were for wells drilled on federal land.

NAC 522.230 requires an owner of a well to obtain a bond of not less than \$10,000 for each well, or in a sum of not less than \$50,000 covering all wells being drilled. An owner of a well drilled on federal land is not required to obtain a state bond if he has previously deposited a bond with the Federal Government. However, the bond must be in the same amount required by the Division.

Despite these requirements, four of nine well owners' federal bonds were less than the amount required. Although each bond was for \$25,000, the minimum amounts required by regulation ranged from \$30,000 to \$50,000. In total, the federal bonds were \$80,000 less than the minimum amount required. Since these bonds help ensure that oil or gas wells are properly repaired and plugged, it is important that they meet the minimum required amount.

Participation in Bond Pool Not Always Terminated as Required

The Division did not always terminate participation in the state's Reclamation Bond Pool as required. Regulations require the Division to terminate participation if an operator fails to pay their premium within 70 calendar days after the due date. However, two operators were allowed to participate in fiscal year 2005 even though they had not paid within the 70-day limit. One operator whose quarterly premium was \$538, had not paid a premium since April 2004. The second operator paid his \$2,624 quarterly premiums anywhere from 5 to 9 months after the due date. Timely premium payments help ensure the bond pool has sufficient funds to reclaim land disturbances if an operator fails to do so.

The bond pool program was established to allow small mining operations to comply with state and federal bonding and surety requirements. Each participant must pay an entry deposit and quarterly or annual premiums to participate in the bond pool. If a participant fails to pay a premium in the amount and by the time required, he must also pay a 5 percent penalty. However, if the premium and penalty are not paid within 30 calendar days after the premium due date, the participant is notified that his participation will be terminated if full payment is not received within 70 calendar days after the date the premium was due. If an operator's participation is terminated, the operator forfeits his deposit.

Division personnel stated one of the participants died but the bond was not terminated in case someone purchased the operation and assumed the bond. However, regulations do not authorize this practice. Staff also informed us the second participant had temporarily suspended operations but wanted to keep his bond active. As a result, he continues to make payments but they are not within 70 days after the due date. Although this approach may be reasonable, regulations do not provide this flexibility.

Recommendations

1. Witness geothermal well blowout prevention tests as required by regulation.
2. Ensure oil and gas bonds are sufficient to meet regulatory requirements.
3. Terminate mining operators' bonds in accordance with regulations.

Additional Controls Over Performance Indicators and Accounts Receivable Needed

The Division had not established written procedures to ensure performance indicators were reliable. As a result, performance indicators were not always accurate, supported by adequate documentation, or clearly defined. We also noted the Division's accounts receivable procedures were not complete. Additional controls will help ensure

that all accounts receivable are collected timely and the state's accounting records are reliable.

Procedures Needed to Ensure Performance Indicators Are Reliable

The Division lacks written procedures that address how performance measures are computed and the retention of underlying data and supporting documentation. As a result, our analysis of the five performance indicators presented in the Governor's 2005-2007 Executive Budget, indicated that only one was reliable. Of the remaining four, one was unreliable and three could not be verified because the underlying data was not readily available. Exhibit 2 shows our analysis of each performance indicator.

Exhibit 2

**Analysis of Division of Mineral's Performance Indicators
Reported in the 2005-2007 Executive Budget**

Performance Indicator	Actual Reported FY 2004	Reliable	Unreliable	Could Not Determine Reliability⁽¹⁾
Percent of staff hours spent collecting, compiling, and publishing information on Nevada's mineral industry.	25%			X
Number of public awareness and education presentations given per FTE.	13			X
Percent of oil, gas, and geothermal drilling permits processed in three working days.	100%		X ⁽²⁾	
Percent of permitted oil, gas, and geothermal operations inspected.	100%			X
Percent of hazardous abandoned mine openings secured.	80%	X		

Source: Auditor review of Division records.

⁽¹⁾ Underlying data was not readily available.

⁽²⁾ Eight of the 13 permits we reviewed were processed within 4 to 38 working days after receipt.

In addition, the indicator regarding the percent of permitted operations inspected does not properly describe the reported information. This measure can be interpreted that the Division physically inspected all operations. However, the measure included oil and gas well inspections performed by a federal agency and desk reviews of geothermal well operators' reports.

The State Administrative Manual provides guidance to help ensure performance indicators are reliable. Agencies are required to develop written procedures on how the performance measures are computed. The procedures are to include formulas and

information on where the data is obtained and which reports are used. Further, staff is responsible for reviewing the procedures and ensuring they are followed. Also, the agency must retain the records used in computing the performance measures for three years.

Written procedures help ensure the process for collecting performance measurement data is reasonable and consistent over time. This, in turn, helps ensure that managers and oversight bodies receive reliable information that represents the actual results of an agency's operational activities when evaluating programs and making budget decisions.

Additional Procedures Will Ensure Accounts Receivable Are Properly Recorded and Reported

The Division billed over \$150,000 in fees and assessments for the fiscal year ended June 30, 2005. Generally, we found that the Division followed proper billing and collection practices. However, the Division's procedures should be revised to ensure all accounts receivable are properly recorded and reported. Specifically, procedures lacked clear direction on how to define, age, and report accounts receivable. As a result, bond pool premiums totaling about \$7,000 were not billed timely. In addition, the Division's June 30, 2005, accounts receivable report submitted to the Office of the State Controller indicated no receivables; however, we identified receivables totaling about \$19,000.

The Controller's *Accounting Policies and Procedures* recommend, at a minimum, that an agency maintain an accounts receivable subsidiary ledger that includes the beginning balance, current charges, payments, and outstanding balance for each customer. Implementing these elements will help ensure that the Division's accounts receivable are collected timely and the state's accounting records are reliable.

Recommendations

4. Develop written procedures to help ensure performance indicators are reliable and clearly stated.
5. Retain performance indicator data in accordance with the State Administrative Manual.

6. Revise procedures to ensure all accounts receivable are properly recorded and reported.

Appendices

Appendix A Audit Methodology

To gain an understanding of the Division of Minerals, we interviewed agency staff and reviewed state laws, regulations, policies, and procedures significant to the Division's operations. We also reviewed the agency's prior audit reports, financial reports, budgets, minutes of various legislative committees, and other information describing the activities of the Division. We documented and assessed the Division's internal controls over receivables, property and equipment, revenue, expenditures, personnel, performance bonds, and performance measures.

To accomplish our audit objective, we determined if the agency's accounts receivable were properly recorded and reported and that collection efforts were effective. We compiled the agency's receivables and reviewed 10 individual billings to verify that the Division followed proper billing practices. To verify that revenue was assessed, collected, and deposited in accordance with laws and regulations, we tested 33 receipts selected randomly and judgmentally. We also verified that the Division followed proper procedures for accepting grants and that all debit entries to revenue accounts were appropriate. Finally, we accounted for all cash receipt forms.

We randomly selected 20 expenditure transactions and tested each to determine if they were properly supported, correctly recorded and in compliance with applicable laws, regulations and policies. In addition, we verified that credit entries to expenditure accounts were appropriate. We also reviewed all credit card transactions for unusual charges. Finally, we verified that the agency's contracts were properly approved and payments were in accordance with terms of the agreements.

To verify that the Division complied with applicable personnel and payroll laws, regulations, and policies, we randomly selected two pay periods. We verified that all payroll transactions were processed correctly. We also verified that the Division developed work performance standards and that employees received performance

evaluations as required. Finally, we verified that changes in employment status and wage rates for employees were appropriate.

We also determined if the Division managed performance bonds in accordance with State laws and regulations by testing all additions and changes to Reclamation Bond Pool deposits and premiums for fiscal year 2005. In addition, we verified that the Division retained forfeited bond pool deposits as required. Finally, we verified that five well operators, selected at random, provided proper surety or deposits, and determined if certain other well operators met minimum bonding requirements.

We reviewed each of the five performance indicators, reported in the fiscal year 2005-2007 Executive Budget, to determine if they were reliable. We also determined if the Division witnessed certain well drilling tests required by regulation.

To determine if fixed assets were adequately safeguarded and accounted for, we verified that the Division had taken an annual fixed asset inventory and that the inventory list was accurate.

Our audit work was conducted from April through October 2005, in accordance with generally accepted government auditing standards.

In accordance with NRS 218.821, we furnished a copy of our preliminary report to the Administrator of the Division of Minerals. On March 15, 2006, we met with the Administrator to discuss the results of our audit and requested a written response to the preliminary report. That response is contained in Appendix C, which begins on page 17.

Contributors to this report include:

Gary J. Kulikowski, CPA
Deputy Legislative Auditor

Michael O. Spell, CPA
Audit Supervisor

Stephen M. Wood, CPA
Chief Deputy Legislative Auditor

Appendix B

Prior Audit Recommendations

Our 1997 audit of the Division of Minerals contained three recommendations related to the Abandoned Mine Lands program. The Division indicated that all three were fully implemented. The scope of our current audit did not include these prior recommendations. Therefore, we did not verify the Division's implementation of the prior audit recommendations.

Appendix C
Response From the Division of Minerals



KENNY C. GUINN
Governor

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ALAN R. COYNER
Administrator

March 27, 2006

Paul Townsend, Legislative Auditor
Legislative Counsel Bureau
401 S. Carson Street
Carson City, NV 89701-4212

Dear Mr. Townsend:

Pursuant to NRS 218.821, this letter shall serve as a written statement of explanation to the audit report on the Commission on Mineral Resources, Division of Minerals as presented to the Division on March 15, 2006. Also attached to this letter is the "Division of Minerals, Response to Audit Recommendations" page indicating the Division accepts the six audit recommendations.

The Division's written statement of explanation is as follows:

1) Witness geothermal well blowout prevention tests as required by regulation.

- 1) Seven geothermal wells were drilled during the audit period.
- 2) The Division asserts that three of the well tests were witnessed by the Division, two of the well tests may have been witnessed by the Division but supporting documentation was not available, and two of the well tests were witnessed by the BLM geothermal well inspector at the request of the Division.
- 3) The two well tests witnessed by the BLM geothermal well inspector were part of a four well series drilled by the same operator with the same drilling equipment. The well tests for the first and fourth wells of this series were witnessed by the Division.
- 4) The oil, gas and geothermal program manager is the only state employee responsible for geothermal production well inspection. The Division experienced a 3 ½ month vacancy in this position during the audit period. Since the previous occupant served 10 years in the position, transition issues did occur. The Division might have been able to produce evidence that the tests for the remaining two wells were witnessed had the log book and emails of the previous oil, gas, and geothermal program manager been available. The Division acknowledges evidence of such witness should have been noted in the well files.
- 5) The Division has had a cooperative program with the BLM since 1984 in the regulation of oil and gas drilling operations. This program streamlines permitting for industry, reduces duplication, and maximizes resource utilization between the two agencies. It is the most advanced program of its kind in the western states. During the audit period the existing Memorandum of Understanding (MOU) which guides this cooperative program was under revision to include geothermal activities. Based on this, the Division accepted the results of the BLM geothermal well inspector for two inspections.

Dennis Bryan; *Small-Scale Mining and Prospecting*
Richard DeLong; *Large-Scale Mining*
Patrick Fagan; *Geothermal Resources*

Commission on Mineral Resources

Fred D. Gibson, Jr., Chairman; General Public

Eugene Kozlowski; *Oil and Gas*
John Mudge; *Large-Scale Mining*
Ron Parratt, V. Chair.; *Exploration and Development*

- 6) The Division recognizes the provisions of NAC 534A.270 (3) "... These tests must be witnessed by the division" are absolute and offer no flexibility. Geothermal well drilling is a 24/7 activity. Due to the variable nature of onsite drilling conditions, the timing of scheduled blowout prevention tests can vary significantly. This can result in lengthy and unproductive trips to remote locations, and extremely expensive drilling rig standby time should the oil, gas, and geothermal program manager be unavoidably detained.
- 7) The sophisticated and modern drill rigs being used today have automatic systems that continuously record data, including such things as blowout prevention tests. Operators routinely submit these reports to the Division. These reports, along with verbal contact with the drill rig, allow for a certain level of monitoring and oversight of this activity.
- 8) NAC 534A.270 dates from 1985 and is in the process of being revised by the Commission on Mineral Resources. The Division has recommended to the Commission that this regulation be modified to eliminate the requirement for the Division to witness well blowout prevention tests.

2) Ensure oil and gas bonds are sufficient to meet regulatory requirements.

- 1) The Division has routinely recognized the bonds posted by industry with the BLM as required by NAC 522.230 (2). However, the Division failed to recognize the BLM minimum requirement is \$10,000 per lease or \$25,000 statewide, whereas the state requirement is \$10,000 per well or \$50,000 statewide.
- 2) The statewide "shortfall" in oil and gas bonding documented by the audit was \$80,000. All of the wells involved are on public land. Nevada had 99 producing oil wells in 2004. All of the oil wells on private property are properly bonded at the \$10,000/\$50,000 level.
- 3) Approximately 6 to 8 oil wells are drilled in Nevada each year and nearly all are drilled on public land managed by the federal government. The first line of responsibility for the plugging and abandonment of "orphan" wells is the federal government. There have been 953 oil and gas wells drilled in Nevada. Currently there are zero unplugged orphan oil wells in the state. The federal government has plugged two orphan wells in Nevada. The state has never had to plug an orphan oil well or incur any expense or liability related to the plugging of an orphan well.
- 4) The Commission has held two scoping sessions to consider revisions to NAC 522. The language to be submitted to the Legislative Counsel Bureau recommends a reduction in the bonding requirement for oil and gas drilling operations to \$10,000 per well or \$25,000 statewide, which would parallel the federal requirements, and result in no additional bonding requirements for wells on public land.
- 5) At this time all new operators are being required to meet the \$10,000 per well or \$50,000 statewide bonding requirements. Bonding for all existing operators is being held at current levels pending revisions to NAC 522.

3) Terminate mining operator's bonds in accordance with regulations.

- 1) The Division acknowledges that two participants were not terminated from the Reclamation Bond Pool as required.
- 2) The two bonds cited in the audit findings are for \$209,900 and \$43,041. The cash position (deposit plus premiums paid) for the two bonds is \$81,844 and \$11,845, respectively. The Bond Pool is only liable up to the amount of the bond and only liable for disturbances described in the bond document.

- 3) The current total amount of all bonds in the pool is \$2,265,263 and the total cash in the pool is \$1,959,106. The Bond Pool has sufficient resources to cover the forfeiture of the two bonds identified by the audit, if necessary, or to do the reclamation activities.
- 4) The Division has terminated the participant with the \$43,041 bond from the bond pool. The BLM is required to demand a replacement bond or the commencement of reclamation activities by the operator. This may take two or three years to occur. The Division is aware that the new owner of the operation bonded for \$43,041 has commenced reclamation activities and has applied to the BLM for a bond reduction to approximately \$8,000. This may significantly reduce the Bond Pool's exposure on this particular bond. The Division is in direct communication with the participant with the \$209,900 bond and is closely monitoring the situation. The participant has a large investment in the pool (\$81,844) and expects to be current by the end of March.

4) Develop written procedures to help ensure performance indicators are reliable and clearly stated.

- 1) The Division asserts the procedures for the five performance indicators were established, understood by the employees involved in the tabulation of the data to support the performance indicators, and the Division has substantially met the goals and objectives of the performance indicators.
- 2) The Division acknowledges the procedures for the five performance indicators were not in written form, therefore:
 - a. *Percent of staff hours spent collecting, compiling, and publishing information on Nevada's mineral industry* – The deputy administrator shall at the end of the fiscal year make an estimate of the percent of staff hours spent collecting, compiling, and publishing information on Nevada's mineral industry and forward a report to the administrator.
 - b. *Number of public awareness and education presentations given per FTE* – The administrative assistant shall at the end of the fiscal year review the weekly reports, determine the number of public awareness and education presentations given, divide by the number of FTE's in the Division, and forward a report to the administrator.
 - c. *Percent of oil, gas, and geothermal drilling permits processed in three working days* – The oil, gas, and geothermal program manager shall at the end of the fiscal year review the well file for the drilling permits issued during the fiscal year and determine for each permit the length in days between when the permit was fully complete and the approval date of the administrator, calculate the percentage that were processed in three working days or less, and forward a report to the administrator.
 - d. *Percent of permitted oil, gas, and geothermal operations inspected* - The oil, gas, and geothermal program manager shall at the end of the fiscal year review the well file for the drill holes spudded during the fiscal year, determine the number of drill holes that received a field inspection by either the Division or the BLM, calculate the percentage inspected, and forward a report to the administrator.
 - e. *Percent of hazardous abandoned mine openings secured* – The chief of the abandoned mine lands program shall at the end of the fiscal year query the AML database and determine the total number of hazardous abandoned mine openings

secured as a percentage of the total number of hazardous abandoned mine openings inventoried, and forward a report to the administrator.

- 3) The Division asserts that written procedures now exist for the five performance indicators.
- 4) The Division acknowledges the audit questioned the reliability of certain performance indicators reported in the 2005-2007 Executive Budget and responds as follows:
 - a. *Percent of staff hours spent collecting, compiling, and publishing information on Nevada's mineral industry* – The goal of this performance indicator is to ensure the Division does a specific amount of public outreach every fiscal year in order to increase the visibility of the Division and its mission. The audit questioned whether the deputy administrator could make a reliable estimate of percent of staff hours spent collecting, compiling, and publishing information on Nevada's mineral industry. During the course of the audit it was suggested the only reliable estimate would have to be based on employee time sheets with a "billable hours" type of breakdown. The Division has no intention of instituting such a system. The Division intends to drop or replace this performance indicator in the 2007 – 2009 Executive Budget.
 - b. *Number of public awareness and education presentations given per FTE* – The goal of this performance indicator is to bring every member of the Division staff in direct contact with the public, especially Nevada school children, and talk to them about abandoned mine safety and Nevada's rocks and minerals and their uses. The presentations are documented in the weekly reports provided by the Division to the Commission. The Division acknowledges more definitive notations of the presentations are needed since the audit documented more presentations than the Division reported in the 2005-2007 Executive Budget.
 - c. *Percent of oil, gas, and geothermal drilling permits processed in three working days* – The goal of this performance indicator is to have timely processing of oil, gas, and geothermal permits and to prevent administrative delay between when the permit is fully complete and approval by the administrator. The Division acknowledges a lack of good record keeping in the well file as to when the permit was fully complete. The Division asserts that better practice with regards to this record keeping is now being followed. Since the geothermal regulations require a permit must be issued within 30 days from when permit is fully complete, and the oil and gas statutes require a permit must be issued "promptly" from when the permit is fully complete, the Division intends to amend this performance indicator in the 2007 – 2009 Executive Budget from three days to thirty days.
 - d. *Percent of permitted oil, gas, and geothermal operations inspected* – The goal of this performance indicator is to ensure the Division and the BLM do not regulate the oil and gas, and geothermal industry from their offices, but actually meet and visit drilling operators on location. The BLM by necessity has to visit each oil and gas and geothermal well location on public land. The Division acknowledges that evidence of the BLM inspection activity was not well documented in the well files. The Division is not required by regulation to inspect or visit the oil and gas locations, but tries to visit as many as possible. Currently the Division is required to visit all geothermal operations by virtue of the requirement to witness the well blowout prevention tests. Due to manpower constraints and the difficulty of

depending on the BLM for supporting data, the Division intends to drop or replace this performance indicator in the 2007 – 2009 Executive Budget.

- e. *Percent of hazardous abandoned mine openings secured* – The goal of this performance indicator is for the Division to keep an adequate level of hazardous abandoned mine openings secured relative to the number of hazardous mine openings inventoried. The Division agrees with the audit finding that this performance indicator is reliable.

5) Retain performance indicator data in accordance with the State Administrative Manual.

- 1) The State Administrative Manual states, “Retain the records used in computing performance measures for three fiscal years.”
- 2) The Division asserts the records used in computing certain of the performance measures are being retained according to the State Administrative Manual, as follows:
 - a. *Percent of staff hours spent collecting, compiling, and publishing information on Nevada’s mineral industry* – All the reports of the deputy administrator which estimate the percent of staff hours spent collecting, compiling, and publishing information on Nevada’s mineral industry have been retained.
 - b. *Number of public awareness and education presentations given per FTE* – The records used to compute the number of public awareness and education presentations are noted in the weekly reports the Division provides to the Commission. The weekly reports are routinely retained in the Division’s files and form the basis for the monthly reports and quarterly reports (Administrator’s reports) published by the Division.
 - c. *Percent of oil, gas, and geothermal drilling permits processed in three working days* – The records used to compute this performance measure are found in the oil and gas well permit files and the geothermal well permit files which are permanent files retained by the Division.
 - d. *Percent of permitted oil, gas, and geothermal operations inspected* - The records used to compute this performance measure are found in the oil and gas well permit files and the geothermal well permit files which are permanent files retained by the Division.
 - e. *Percent of hazardous abandoned mine openings secured* – The records used to compute this performance measure are found in the AML database maintained by Division and backed up to the server daily. Additionally, the percentage is published annually in the Division’s Abandoned Mine Lands Annual Report.
- 3) The Division acknowledges that in most cases individuals were queried and verbal responses were used to obtain the numbers given for the performance measures in the 2005 – 2007 Executive Budget and written responses were not created or retained.

6) Revise procedures to ensure all accounts receivable are properly recorded and reported.

- 1) The Division notes with emphasis that the Division’s main accounting system maintained by the program officer had no findings or recommendations as a result of the audit.
- 2) The Division has three subsidiary account systems that generate accounts receivable:
 - a. *Surface disturbance fee associated with permitted disturbance by mining operations on public land* – This billing system is maintained by the field specialist as a spreadsheet and issued 21 bills totaling \$23,476 during the audit

period. This number of billings and billing total is average for this subsidiary account system. The Division notes that no financial errors in this system were documented by the audit. The Division acknowledges that the minor ledger changes recommended by the audit will improve the system, and the recommended changes have been implemented.

- b. *Annual geothermal well use fee* – This billing system is maintained by the administrative assistant as a spreadsheet and issued 14 bills totaling \$63,375 during the audit period. This number of billings and billing total is average for this subsidiary account system. The Division notes that no financial errors in this system were documented by the audit. The Division acknowledges that the minor ledger changes recommended by the audit will improve the system, and the recommended changes have been implemented.
- c. *Reclamation bond pool bond premiums* – This billing system is maintained by the Division under its responsibility to administer the State Reclamation Bond Pool. The finances of the State Reclamation Bond Pool are maintained as a separate budget account, totally independent from the Division's account. The billing system for the bond pool premiums is maintained by the deputy administrator as a spreadsheet and issued quarterly billings to 17 participants for 68 bills totaling \$129,133 during the audit period. The two billing errors totaling about \$7,000 detected by the audit were the result of the same unusual circumstance. The total bonded amounts for both of the bonds in question were increased during the same billing period. The additional premium needed to cover the increase in bond amount was detected at the next quarterly billing. The participants were contacted and additional payments were forwarded to the Division immediately. The Division acknowledges that the minor ledger changes recommended by the audit will improve the system, and the recommended changes have been implemented.

This completes the Division's written statement of explanation to the audit report.

Sincerely,



Alan R. Coyner, MBA, CPG#10520
Administrator

cc: Commission on Mineral Resources

**Division of Minerals
Response to Audit Recommendations**

<u>Recommendation Number</u>		<u>Accepted</u>	<u>Rejected</u>
1	Witness geothermal well blowout prevention tests as required by regulation.	<u> X </u>	<u> </u>
2	Ensure oil and gas bonds are sufficient to meet regulatory requirements	<u> X </u>	<u> </u>
3	Terminate mining operators' bonds in accordance with regulations.....	<u> X </u>	<u> </u>
4	Develop written procedures to help ensure performance indicators are reliable and clearly stated.....	<u> X </u>	<u> </u>
5	Retain performance indicator data in accordance with the State Administrative Manual	<u> X </u>	<u> </u>
6	Revise procedures to ensure all accounts receivable are properly recorded and reported.....	<u> X </u>	<u> </u>
	TOTALS	<u> 6 </u>	<u> 0 </u>