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**Testimony of Professor Mark Squillace, University of Colorado Law School  
Subcommittee on Energy and Mineral Resources, House Natural Resources Committee  
Hearing on Oil and Gas Royalties on Public Lands, 116<sup>th</sup> Cong., 2<sup>nd</sup> Sess. 2020**

The Honorable Alan Lowenthal  
Chair, Subcommittee on Energy and Mineral Resources, House Natural Resources Committee  
1324 Longworth House Office Building  
Washington, D.C. 20515-6201

Dear Chairman Lowenthal:

Thank you for the opportunity to appear before the House Subcommittee on Energy and Mineral Resources to offer my views on the current oil and gas royalty policies on our public lands. I am the Raphael J. Moses Professor of Natural Resources Law at the University of Colorado Law School. I teach and work primarily in the fields of environmental, natural resources, and water law and I have written extensively on all of these subjects. My professional experience with public lands issues runs deep. As a law student at the University of Utah, I worked in the Utah State Office of the Bureau of Land Management (BLM) as a land law examiner – a position that allowed me to review all manner of public lands activities and gain first-hand knowledge about the operation of our public land laws. Following law school, and before entering law teaching, I was hired into the Solicitor's Honor's Program at the U.S. Department of the Interior where I gained significant additional experience on public lands and mineral law issues. I took a leave from teaching and returned to the Solicitor's Office in 2000 as a Special Assistant to the Solicitor where I worked on a wide range of special projects involving public lands. All of this experience both inside and outside of government has helped to inform my understanding of public lands management and the issues surrounding royalty payments for federal oil and gas leases.

My written testimony emphasizes five points. First, no policy involving oil and gas development, including federal policy on oil and gas royalties on public lands, should be made without considering its implications for climate change. Second, royalty relief is generally not appropriate for federal oil and gas leases because royalty rates have remained at the same 12.5% level for 100 years, a rate that is significantly out of step with market rates. Third, several western States are already suffering from the loss of revenue from fossil fuel production and this loss is exacerbated by the BLM's royalty relief policies. Fourth, royalty relief is only supposed to be granted under limited circumstances and the BLM has failed to produce a public record showing that these circumstances have been met in the myriad cases where relief has already been granted. Finally, the alleged need for royalty relief can be traced to the dramatic fall in oil and gas prices, but since royalties are based upon a percentage of the market value of the resource, royalty relief is built into the system and should not be further extended as is happening under the current Administration's royalty relief policies.

## 1. Royalty Relief Policies Exacerbate Climate Change

The summer of 2020 has borne witness to some of the worst climate-related disasters in our history. From the fires in California, Oregon, and throughout the west, to the hurricanes in the southeastern United States we see direct evidence of the external costs associated with the global development of fossil fuels. Beyond our borders, the climate crisis has triggered historic flooding in Bangladesh and “zombie” fires in the peat bogs of Siberia. We cannot turn off the spigot to federal oil and gas development overnight. For better or worse, our economy remains dependent on these resources for transportation and other needs in the short term. But we can and we must better manage the inevitable decline in the use of these fossil fuels and expedite a fair and equitable transition to cleaner energy. Subsidizing oil and gas development by offering producers royalty relief does the opposite. It incentivizes production at a time when we should be finding ways to ease companies out of the oil and gas business. We failed to responsibly manage the decline of the coal industry and the many bankruptcies in the coal industry that followed brought devastation to coal workers. Thousands of jobs were lost and companies have cynically used the bankruptcy process to renege on benefits that had been promised to their workers.

Like coal, oil and gas are not coming back. California has recently [announced](#) that all new vehicles in that State must be “zero emission” by 2035. Other states and countries will almost certainly follow suit. In addition, several of the largest oil companies, including BP and Shell, have recently announced plans to achieve [net zero carbon emissions by 2050](#). While they have a long way to go, they rightly see climate change as an existential threat and they are accordingly shifting away from oil and gas and toward cleaner fuels. All of this, of course, will cause demand for oil to plummet. We can ignore this reality as we did with the coal industry or we can plan for it now. Federal royalty policies are certainly not the most significant problem that we must confront in managing the decline of fossil fuels, including oil and gas. But the current royalty relief policy sends exactly the wrong signal about the direction of government policy on fossil fuels.

## 2. Federal Royalty Rates are Already Far Below Market Value

The Mineral Leasing Act of 1920 requires that oil and gas royalties be set at “*not less than 12.5%*” of the value of production. 30 U.S.C. § 223 (emphasis added). The rate has remained at this level for 100 years even as the market rates for oil and gas royalties have risen significantly. Thus, in a sense, the federal government’s failure to adjust royalty rates for federal onshore oil and gas lessees, as it is authorized to do under the law, already provides lessees with royalty relief.

State royalty rates offer a useful comparison. Colorado, for example, imposes a 20% royalty for oil and gas production on state trust lands. On Texas state lands, the royalty rate is 25%. New Mexico and North Dakota both charge 18.75%, which is the same rate imposed on producers for federal offshore oil and gas leases.

The [Congressional Research Service](#) recently estimated that royalties from onshore oil and gas leases in FY2019 totaled \$2.931 billion, which represents nearly 73% of all revenue from federal onshore oil and gas leases. Since the host States receive 49% of these revenues, federal oil and gas royalties alone contributed \$1.46 billion to state coffers in FY2019. Imagine, however, if federal lessees were paying at North Dakota’s rates or at Texas’ rates. In that situation, States would have realized \$2.154 billion or \$2.91 billion respectively instead of the \$1.46 billion they actually received.

Rather than offering royalty relief, the Interior Department should be working aggressively to establish new, market-based royalty rates. Not only would this increase state and federal

revenues, it would also avoid the longstanding subsidies to the oil and gas industry that result from these below market rates, and it would help insure that marginal properties are not developed in the first place.

### 3. The Impact on Western States

The significant decline in the price of oil and gas was already going to cause a significant decline in State revenues from these resources. Production is down and fewer wells are being drilled. But the Administration's royalty relief policies are making a bad situation much worse for the host States by allowing companies to avoid paying a significant portion of the royalties they would otherwise owe. [Taxpayers for Common Sense](#) has identified 521 federal leases covering 346,496 acres of land that have received royalty relief. More recent data suggest that those figures have grown to 557 leases on 483,128.52 acres of land. For reasons that are not entirely clear, Wyoming lessees have received royalty relief on a disproportionate number of leases, accounting for 406 of the leases on 336,914.210 acres of land. And in every case thus far identified, the Wyoming BLM office has approved royalty rate reductions to 0.5%! This represents a 96% reduction from the standard 12.5% royalty. In other words, for every million dollars that Wyoming would have received under the standard royalty rate they can now expect to receive only \$40,000 from those leases that have obtained royalty relief.

In FY2019, the [Interior Department has reported](#) that the top five states in terms of mineral revenues from public lands were New Mexico at \$1.17 billion, Wyoming at \$641.11 million, Colorado at \$108.05 million, Louisiana at \$101.33 million, and North Dakota at \$93.65 million. Most of this came from oil and gas development. The numbers for FY2020 were already set to fall precipitously in light of COVID-19. For example, in July, 2020, the [Congressional Research Service described a report from Interior's Office of Natural Resource Revenues \(ONRR\)](#) that identified onshore oil and gas royalty collections of \$170 million for May 2020, a decline of 53% from May 2019. Much of this decline can be attributed to declines in production and the value of the resource. But as more leases receive royalty relief these declines are going to get worse. States like Wyoming are already struggling due to the dramatic decline in revenue that has resulted from the pandemic. They cannot afford federal policies like royalty relief that will almost certainly deepen their fiscal woes.

### 4. Interior Has Failed to Ensure that Royalty Reductions Meet Federal Standards

The Mineral Leasing Act provides in relevant part that:

The Secretary of the Interior, for the purpose of encouraging the greatest ultimate recovery of ... oil [and] gas ... and in the interest of conservation of natural resources, is authorized to waive, suspend, or reduce the rental, or minimum royalty, or reduce the royalty on an entire leasehold, or on any tract or portion thereof segregated for royalty purposes, *whenever in his judgment it is necessary to do so in order to promote development, or whenever in his judgment the leases cannot be successfully operated under the terms provided therein.*

30 U.S.C. § 209 (emphasis added). The Interior Board of Land Appeals has laid out the limited circumstances under which royalty relief under the Mineral Leasing Act may be granted:

On the basis of material that an appellant is required to submit in its application, *BLM must be able to find there is a reasonable probability [that] operations would cease or development, recovery, or conservation of the resource would be jeopardized before it*

*can even consider exercising its discretion to grant relief.* Otherwise, the Federal mineral owner has nothing to gain by reducing the royalty. [Peabody Coal Co.](#), 93 IBLA 317, 324, 327 (1986) (Emphasis added.). Unfortunately, the BLM has not been transparent about the adoption of its royalty rate policy, the applications for royalty relief that it has received, or the evidence upon which they made the case-specific findings required by the IBLA. So, the public cannot know the basis upon which the BLM made the judgment that a particular company faced a reasonable probability that operations on a particular lease would cease or development, recovery, or conservation of the resource would be jeopardized if royalty relief were not granted.

Under section 102(2)(E) of the National Environmental Policy Act, 42 U.S.C. § 4332(2)(E), federal agencies are required to “*study, develop, and describe appropriate alternatives to recommended courses of action in any proposal which involves unresolved conflicts concerning alternative uses of available resources.*” The royalty relief policy and the individual applications for royalty relief all involve unresolved conflicts over alternative uses of available resources. Regarding the royalty relief policy, for example, the BLM might have considered alternatives that would have limited royalty relief to no less than 8%, 6%, or 4% of the value of the resources. Regarding individual applications, the BLM would, at a minimum, have been required to “study, develop, and describe” the consequences of granting royalty relief, and the alternative of allowing a well to shut down if that was the potential consequence of denying royalty relief.

Moreover, the alternative analysis required by NEPA would have offered a vehicle for providing transparency and engaging the public on these important questions. Yet it does not appear that the BLM has complied with NEPA with respect to either its royalty relief policy or the individual royalty relief applications. Indeed, the mere fact that the BLM has apparently provided royalty relief on at least 557 leases covering 483,128.52 acres of public land over the course of the past several months strongly suggests that they have not engaged in the type of analysis required by NEPA. And they appear to have made no effort to involve the public or even the affected States in these decisions. Preliminary results from the GAO study of this matter seem to confirm the haphazard way in which the BLM has handled these applications.

Given the lack of transparency it is difficult to know whether any or all of the BLM’s decisions on royalty relief applications have been arbitrary and capricious, but they certainly have not followed all of the strictures of NEPA and thus are vulnerable to a claim of having made decisions that are not in accordance with the law. See 5 U.S.C. § 706(2)(A). Indeed, it is not at all clear that the BLM could produce an administrative record for any of these cases that would be sufficient to justify its decisions and satisfy its obligations under the Administrative Procedure Act (APA). Gaining documentation of the applications and the decisions on those applications is a critical first step that will be needed to evaluate the Department’s actions and their compliance with the NEPA, the APA, and the Mineral Leasing Act.

If royalty relief is ever warranted for federal oil and gas leases it should be extremely rare. As the IBLA has found it should only be granted where “there is a reasonable probability [that] operations would cease or development, recovery, or conservation of the resource would be jeopardized....” Yet some BLM offices appear to be handing out royalty relief like it is candy. In one way or another we all end up paying for this short-sighted policy.

## 5. Lessees are Already Receiving Royalty Relief Due to Low Commodity Prices

As previously noted, the economic downturn caused by COVID-19 pandemic caused the price of West Texas Intermediate (WTI) oil to drop dramatically in March and into April and May, at one point leveling out at less than \$17/barrel. The price has recovered somewhat over the last several months, hovering around \$40/barrel. Nonetheless, this is down substantially from the pre-pandemic price, which over the past three years has [ranged from roughly \\$50 to \\$65/barrel](#). While oil prices have long been volatile and difficult to predict, the decline in global demand is real and oil prices seem unlikely to recover in any substantial way going forward as the demand for these resources continues to shrink. From the perspective of a producer, one salutary consequence of this price decline is that the royalties paid by lessees, which are set as a percentage of the value of the resources, drop at the same rate as the price of oil and gas.

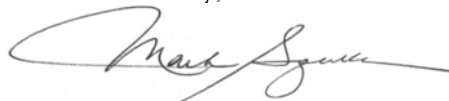
Of course, the drop in the price of these commodities poses a major risk for oil and gas producers, but they know as well as anyone that their business model is defined by risk. Since the costs of production at any individual well are largely static, when they choose to drill a well they are betting that the price that they receive for the oil and gas resource will allow them to earn a reasonable profit. Historically, oil and gas producers have profited handsomely from this bet. Going forward, however, if the price remains low, the profits will not be sufficient to induce operators to produce more oil and gas. As argued in the discussion above about the climate impacts from oil and gas development, this may be a very good thing. As producers gradually leave the industry they will open more opportunities for cleaner fuels. But whatever the impact of lower oil and gas prices, the BLM ought not subsidize producers in a manner that denies the state and federal governments a fair return on whatever oil and gas resources are produced.

Moreover, even assuming that some wells might have to shut down if they are denied royalty relief, the Mineral Leasing Act affords Interior broad discretion to deny such relief and that denial may be entirely appropriate in light of other public interest factors that the agency must take into account. This seems especially true where, as here, the agency has failed to provide the public with compelling, case-specific evidence that supports granting the royalty relief requests.

Regardless of the BLM's royalty relief policies, the economic realities of the oil and gas industry will likely force some public land oil and gas wells to shut down. Rather than viewing this as a problem, Interior should view it as opportunity to jump start plans to ratchet down oil and gas development on public lands. A substantial decline in federal oil and gas development over the next two decades is inevitable. Responsible planning for that decline is long overdue. A good place to start is by abandoning a royalty relief policy that exacerbates climate change and deprives the States of critical revenues, even as it does little to help the industry.

Thank you again for the opportunity to appear before the Committee today. I wish the Committee well as it seeks to address the important issues that surround royalty rates for oil and gas development on our nation's public lands.

Sincerely,



Mark Squillace