Prepared Testimony of Ryan Alexander, president, Taxpayers for Common Sense

Legislative Hearing on Fossil Fuel Development: Protecting Taxpayers and Eliminating Industry Giveaways

Energy and Mineral Subcommittee
US House Natural Resources Committee

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Good afternoon Chairman Lowenthal, Ranking Member Gosar, and distinguished members of the subcommittee. My name is Ryan Alexander, and I am president of Taxpayers for Common Sense (TCS), a national, non-partisan budget watchdog organization.

Thank you for the opportunity to testify today on H.R. 4364, the Taxpayer Fairness for Resource Development Act; H.R. 4346 the Bonding Reform and Taxpayer Protection Act; the Coal Cleanup and Taxpayer Protection Act; and H.R. 2711, the Methane Waste Prevention Act. We have long supported reforming the Department of the Interior's (DOI's) fiscal management of our natural resources and are pleased to see bills that take important steps towards doing so.

The mission of Taxpayers for Common Sense is to achieve a government that spends taxpayer dollars responsibly and operates within its means. We have identified, highlighted, reformed and sometimes eliminated wasteful spending and tax breaks in agriculture programs, Pentagon spending, corporate welfare, and infrastructure – notably finding, naming and working for years to eliminate funding for the Bridge to Nowhere.

For nearly 25 years, TCS has worked actively to ensure that taxpayers receive a fair return on ALL resources extracted or developed on federal lands and waters. This includes oil, gas, coal, hardrock minerals, wind, solar and timber. Royalties and fees collected from resource development represent a significant source of income for the federal government and must be collected, managed and accounted for in a fair and accurate manner. As the rightful owners, taxpayers are entitled to fair market compensation for the resources extracted from our lands and waters, just like private landowners.

This morning, I will discuss the below-market rates and fees charged by the DOI for oil gas development and the Taxpayer Fairness and Resource Development Act; insufficient bonding protections, the well-documented problem of self-bonding for coal companies, and the Bonding Reform and Taxpayer Protection Act. Finally, I will address taxpayer losses from methane waste on federal lands and the Methane Waste Prevention Act.

Background

The Bureau of Land Management (BLM) is responsible for leasing federal land for oil and gas development throughout the federal onshore mineral estate. These leases may be issued on BLM-managed lands, but also U.S. Forest Service lands, other federally owned lands, and tens of millions of acres of private lands where the federal government holds the subsurface mineral rights. The Secretary of the Interior[1] and the Secretary of Agriculture[2] must prepare land use plans balancing multiple uses of federal lands.

[1] 43 U.S.C. 1712
[2] 16 U.S.C. 1604

At the end of fiscal year 2018, the BLM was managing more than 24 million acres leased for oil and gas development. The Secretary of the Interior is required to hold leases sales at least quarterly in every state where eligible unleased lands are available. The lease sale process begins with nominations from the public, usually industry, of available lands to be included in a sale. BLM then reviews these nominations which are shielded from the public and determines which lands to ultimately offer for lease. At competitive auction, leases are awarded to the highest bidder who offers at least a "national minimum acceptable bid" per acre. Leases issued by BLM have a "primary term" of 10 years and can be extended as long as it is producing oil and gas "in paying quantities." During the period of the lease, the lessee must pay either annual rent on the land, or royalties on oil and gas produced from the lease. Lessees must also post a bond or other financial assurance before drilling starts, to assure that the lease tract will be restored when operations cease.

Unfortunately, over the years taxpayers have lost billions of dollars to a broken oil and gas leasing system. Outdated laws and an inadequate and sometimes corrupt royalty collection system have cost us billions.

As oil and gas production on federal lands has significantly expanded over the last decade, numerous independent reviews have identified longstanding weaknesses in the existing management systems and practices in the DOI's oil and gas programs. These weaknesses make them increasingly susceptible to waste, fraud, and abuse.

Today's hearing to examine legislation regarding energy revenues for onshore oil and gas development, oil, gas, and coal bonding rates and lost methane gas is vitally important. A serious discussion on how to bring in more revenue to the federal Treasury and tackle deeply entrenched decades-old policies that favor oil and gas development over other uses for federal lands is long overdue. These reforms will not only provide financial benefits to the US Treasury and state coffers, they will also help ensure more oil and gas is brought to market.

The Department of Interior Must Provide Fair and Accurate Collection of Revenues for Extraction of Taxpayer-Owned Resources

Natural resources derived from federal lands and waters can and do provide great benefit to the entire nation. In addition to their end use and overall domestic economic benefit, their extraction provides valuable revenue to fund other priorities in the context of our nation's increasing annual deficits and exploding debt. But federal resources have the potential to provide much more.

Federally owned oil and gas resources have generated an average of $7 billion in revenue annually over the last five years.[3] But this amount falls dramatically short of what is rightfully owed to federal and state taxpayers. Federal lands and waters must be mined, drilled or otherwise developed in a manner that protects taxpayers' interests, first and foremost. It is the responsibility of DOI to represent the taxpayers' interests, not the industry's interests.

In March, the Government Accountability Office (GAO) placed the DOI oil and gas program on a list of federal programs and activities that have a high probability of waste, fraud, and abuse **- for the 8th year in a row**.[4] GAO questioned DOI's methods for accurately determining and collecting royalties from oil

[3] Office of Natural Resources Revenue, "Federal Revenue Data" – average revenue from federal oil and gas resources was $7.2 billion for FY2014-FY2018.
[4] GAO-19-157SP, "HIGH-RISK SERIES: Substantial Efforts Needed to Achieve Greater Progress on High-Risk Areas," March 6, 2019.

and gas production on federal lands. Further, the GAO reasserted its previous conclusion that DOI could better account for and manage methane emissions, resulting in higher capture rates and higher royalty revenues.

Instead of allowing the DOI oil and gas program to spend yet another year on the high-risk list, it should be reformed. This means collecting the appropriate fees, rents, and royalties for federal oil and gas development and ensuring long-term liabilities, such as clean-up or mitigation costs, are shouldered by the extractive industries and not the taxpayers.

Current Federal Royalty Revenue Falls Short

The Bureau of Land Management (BLM), the sub agency that oversees the application of onshore royalties, is failing as a responsible steward of federal lands. The most glaring example of this is its failure to raise royalty rates on oil and gas production from the minimum amount of 12.5 percent first set by Congress in 1920.[5] In the absence of agency action, it is imperative that legislation be enacted requiring the increase of royalties from 12.5 percent to 18.75 percent, as included in the Taxpayer Fairness and Resource Development Act.

The BLM's regulations for royalty rates collected from onshore oil and gas leases set a flat rate of 12.5 percent for competitive leases and non-competitive leases. The BLM is authorized to specify a higher royalty rate, but has not done so. The BLM's failure to raise onshore royalty rates, or to create an efficient process for rapidly increasing royalty rates in response to rising prices, represents a failure to ensure a fair return to taxpayers from oil and gas development on federal lands. This failure contradicts the agency's stated goal to "design an oil and gas fiscal system that both ensures that the United States' oil and gas resources are developed and managed in an environmentally-responsible way that meets our energy needs, while also ensuring that the American people receive a fair return on those resources."[6]

A fair return to taxpayers is a competitive rate of return – a royalty rate that is consistent with royalty rates charged on state and private lands. State and private lessors consistently charge royalty rates higher than 12.5 percent.[7] The BLM should increase the royalty rate to 18.75 percent for onshore oil and gas production, equal to the rate for federal offshore oil and gas production and that imposed by many state and private resource owners. The Congressional Budget Office (CBO) estimates increasing royalty rates to 18.75 percent for onshore parcels to match the rate for offshore parcels would generate $400 million in net federal and state income over the next 10 years.[8] And according to the GAO, raising the onshore royalty rate would have limited effects on industry interest in federal lands.[9] Our own analysis shows even greater potential revenues.

TCS recently completed in-depth analyses of the oil and gas leasing system on federal lands in Utah, Nevada, and New Mexico --all areas of significant leasing that illustrate various problems in the overarching system. In each case we found millions, sometimes billions, of dollars had been left on the table due to outdated leasing practices.

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[5] The Mineral Lands Leasing Act of February 25, 1920 (41 Stat. 437-451), Section 17
[6] 80 F.R. 22150.
[7] 80 F.R. 22151-22152.
[8] CBO, "Options for Increasing Federal Income From Crude Oil and Natural Gas on Federal Lands," April 2016. Online Version, p. 23.
[9] GAO-17-540, "OIL, GAS, AND COAL ROYALTIES: Raising Federal Rates Could Decrease Production on Federal Lands but Increase Federal Revenue," June 2017.

In Utah, if BLM's onshore royalty rate had been 18.75 percent, state and federal taxpayers would have received at least $1.4 billion more in oil and gas revenues from 2008 to 2017. In New Mexico, numbers were even higher—with the state and federal taxpayers losing $5 billion in foregone revenue. TCS's three reports: *Giving it Away: How Utah Loses from Oil and Gas Development on Federal Lands*, *Gaming the System: How Federal Land Management in Nevada Fails Taxpayers*, and *New Mexico's Boom that Cost Billions: How Federal Oil and Gas Policies Fail Taxpayers* are enclosed for the record.

An 18.75 percent royalty rate is in line with the rates charged for federal offshore production, as well as rates charged by states and private landowners - almost across the board. In exchange for development rights on lands owned by US states and private landowners, producers regularly agree to royalty rates as high as 25 percent for oil and gas production. Three western states with significant oil and gas reserves – Utah, Wyoming, and New Mexico – do allow for leases with a 12.5 percent royalty rate, but only in special circumstances.[10] Such a low royalty rate can only be found regularly on federally owned lands.

Jurisdiction	Oil & Gas Royalty rate
California (State lands)	16.67 percent[11]
Colorado (State lands)	20 percent
Montana (State lands)	16.67 percent
New Mexico (State lands)	12.5 to 20 percent[12]
North Dakota (State lands)	16.67 to 18.75 percent[13]
Oklahoma (State lands)	18.75 percent
Texas (State lands)	20 to 25 percent[14]
Utah (State lands)	12.5 to 16.67 percent[15]
Wyoming (State lands)	12.5 or 16.67 percent[16]
Private Lands	Generally 12.5 percent to 25 percent
Federal Lands	Generally, 12.5 percent, sometimes less[17]

Rental Rates

Federal law requires private interests pay annual rent on each acre of federal land under lease. Whether or not this rent is enough to get a fair return on federal land for taxpayers depends entirely on the level and

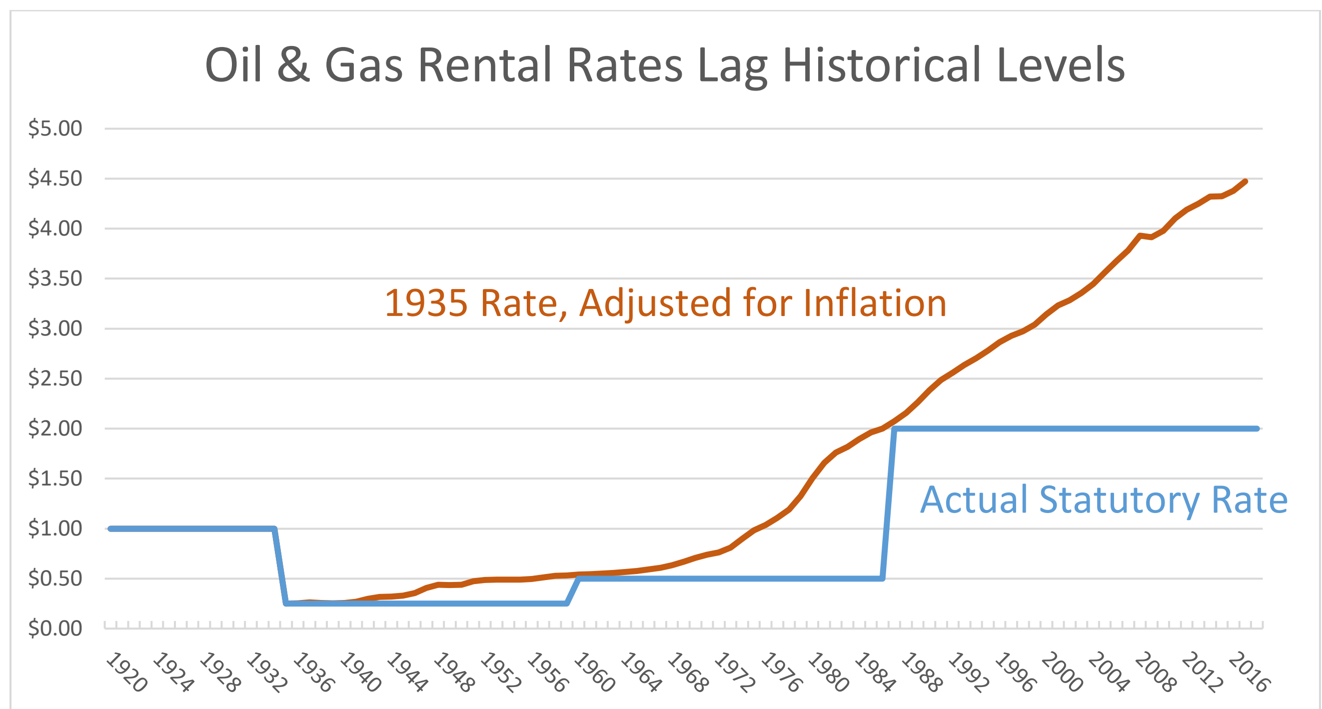
[10] For example, New Mexico offered leases with a 12.5% royalty rate in just five of the 60 lease sales held since September 2014.
[11] Negotiated on a lease-by-lease basis, but generally not less than
[12] The oil and gas royalty rates in New Mexico are based on the geographic location of the lease
[13] The oil and gas royalty rates in North Dakota are based on the geographic location of the lease
[14] The oil and gas royalty rates in Texas are based on the geographic location of the lease, with most categories subject to a 25 percent royalty rate
[15] The oil and gas royalty rates in Utah can change with the approval of the Director of the Utah Trust Lands Administration
[16] 12.5 percent if the parcel was offered in a previous lease sale but did not receive a bid
[17] Federal leases are sometimes granted royalty relief for various reasons as allowed by Department of the interior programs specific to production types

schedule of rental rates. Unfortunately for taxpayers, rental rates have not kept pace with inflation, losing tens of millions of dollars in revenue every year.

To ensure millions of dollars aren't left on the table every year, Congress needs to increase rental rates in statute and index them to inflation, as proposed in the Taxpayer Fairness Act. We support the bill's increase of rental rates from $1.50 per acre in the first five years to $3/acre and from $2/acre every year thereafter to $5/acre.

Congress first established a formal system for leasing federal land to develop oil, gas, coal and other resources through the Mineral Leasing Act (MLA) of 1920. For oil and gas leases attained by permit or through competitive bidding, the original MLA set the annual rental rate at, "not less than $1 per acre per annum."[18] In 1935, the rent due for oil and gas leases was reduced to $0.25 per acre.[19] In 1960, it was increased to $0.50 per acre.[20] Finally, in 1987, Congress set the current rates at, "*not less than* $1.50 per acre per year for the first five years of the lease and *not less than* $2 per acre per year for each year thereafter," (emphasis added).[21]

These rental rates, at $1.50/acre for the first five years and $2.00/acre thereafter, are fractions of the rates that have historically been set by Congress. That is, current rates lag the rental rates set in statute in 1920, 1935, 1960, and 1987, when adjusting for inflation. The rate increases in 1960 and 1987 approximately reflected the 1935 rate of $0.25/acre adjusted for inflation at the times, but now yield less than half the inflation-adjusted rate. (see chart below)



[18] Mineral Leasing Act of February 25, 1920, 41 Stat. 437-451, Sec. 17

[19] 49 Stat. 676 (Aug. 21, 1935)

[20] 74 Stat. 782 (Sept. 2, 1960); P.L. 86-705, §2

[21] Federal Onshore Oil And Gas Leasing Reform Act Of 1987 (Dec. 22, 1987), P.L. 100–203 §5101(c)

Rental receipts would be significantly greater had rental rates rose with inflation since the last statutory change in 1987. According to inflation measurements by the Bureau of Labor Statistics, $1.50 in 1987 is roughly equivalent to $3.25 in 2018 dollars, and $2.00 in 1987 is equal to $4.33 now.[22] The difference means taxpayers are getting as much as 50 percent less than they should from the use of federal land for oil and gas development. That amounts to a loss of roughly $30 million in just one year.

Despite the fact that increasing the rent per acre for federal oil and gas leases would improve overall returns to taxpayers, BLM has failed to take steps to increase the rate above the legal minimum year after year.

Minimum Bids

The Mineral Leasing Act sets the minimum bid for a federal oil and gas lease at $2 per acre for a period of two years beginning in December 1987. Under the MLA the Secretary may, at the conclusion of the two-year period, "establish by regulation a higher national minimum acceptable bid for all leases based upon a finding that such action is necessary: (i) To enhance financial returns to the United States; and (ii) to promote more efficient management of oil and gas resources on Federal lands."[23] The Secretary (through the BLM) has not exercised this authority. The BLM's experience indicates most parcels sell for well in excess of the current minimum acceptable bid, which indicates the current minimum acceptable bid should be higher. Like rental rates, the minimum bid should at least be pegged to inflation, which would equal $4.33 per acre today. Ideally, the BLM should study what level of minimum bid will lead to decreased bidding and adopt a minimum bid that ensures competitive leasing but also ensures the recovery of full value for taxpayers.

According to the CBO, increasing the minimum bid to $10 per acre for competitive and noncompetitive leases would boost net federal and state income by an estimated $100 million over 10 years.[24] This accounts for decreases in rental and royalty income for parcels that attract no bids, which would be minimal because such parcels have historically generated relatively little production and royalty income. The CBO also found that parcels that go unleased as a result of the higher minimum bid would have had relatively little exploration and would have a negligible effect on realization of new information about the locations of oil and gas resources. Parcels that attract no bids would then be available for other uses, including geothermal, wind, and solar development and recreation use.

TCS supports the increase of minimum bid prices in H.R. 4364 Taxpayer Fairness for Resource Development Act from its current level of $2 /acre to $5/acre.

Non-producing leases and speculation

The failure to update minimum bid and rental rates has allowed oil and gas companies to lease vast amounts of federal lands at little cost. At the end of fiscal year 2016, more than half of all federal acreage set aside for oil and gas leasing was tied up in non-producing leases, locking out other potential uses. A significant portion of these leases have characteristics that suggest they represent unreasonable speculative activity. The BLM leasing rules need to better reflect the value of holding federal land and minimize how much is idly held, especially with speculative intent.

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[22] CPI averages for fiscal years 1988-2018 were calculated using Bureau of Labor Statistics, Consumer Price Index Detailed Report – Table 24: Historical Consumer Price Index for All Urban Consumers (CPI-U)

[23] Mineral Leasing Act of 1920 (as amended) §17(b)(1)(B) - 30 U.S.C. 226

[24] CBO (2016). Page 22

Allowing millions of acres of federal lands to be locked up in leases with minimal chance of producing oil or gas contradicts the multiple-use mandate that guides the BLM's management of federal lands under federal law.

Oil and Gas Bonding

On top of these outright giveaways, taxpayers are subsidizing the oil and gas industry by assuming much of the financial responsibility of cleaning up their operations on federal lands. Oil and gas companies benefit generously from embedded subsidies throughout the leasing process and, too often, we are left with the tab to clean-up their mess. H.R. 4346, The Bonding Reform and Taxpayer Protection Act of 2019, takes important steps to remedy this situation.

Drilling on public lands generates significant wastes that can contaminate ground water, public lands, vegetation and wildlife. In order to protect taxpayers, bonding rates were established to guarantee oil and gas companies would reclaim their abandoned wells. However, today's extremely low bonding rates offer little incentive to ensure proper clean-up. Inadequate bonding enables oil and gas companies to incur little financial risk, hence avoiding the full costs and risks of doing business, leaving taxpayers to pick up the tab.

Minimum bond prices for individual leases were determined by law in 1960 and state and nationwide minimum prices were determined by law in 1951. They have remained static since then. To cover a bond for an individual lease, oil and gas companies must pay a minimum bond of $10,000. Alternatively, a single oil and gas operator can cover all of their leases in a single state for $25,000. Or, even still, a single operator can cover all their bonds nationwide for $150,000.

A [2019 report] by the GAO details the steps the DOI should take to better manage potential oil and gas well liability. The report found that reclamation costs for wells orphaned from 2017-2019 would cost $46 million.[25] The report encourages the BLM to "increase bonds as necessary to ensure they reflect risks posed by the operator." The report finds: "In 2008, BLM held bonds worth an average of $2,207 per well in 2018 dollars. BLM held bonds worth an average of $2,122 per well in 2018, a decrease of 3.9 percent as compared to 2008."[26] Despite significant risks to taxpayers and the environment, BLM has increased potential costs to taxpayers from future liabilities by decreasing bond amounts per well.

TCS supports H.R. 4346, which would increase minimum BLM oil and gas bond amounts to $50,000 for all operator's wells on an individual lease, $250,000 for all wells held at the state level, and $1,000,000 for all wells held nationwide, and – importantly – requires the amounts adjust regularly for inflation.

Self-Bonding for Coal

In addition to standard reclamation bonds, the practice of self-bonding is of particular concern for TCS. In certain circumstances, rather than requiring a reclamation bond, producers are allowed to provide financial statements to show they possess a level of assets at the time of permitting which would enable them to cover all reclamation costs.[27] But self-bonding provides no guarantees and amounts to little more than an IOU if a company were to become insolvent.

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[25] Government Accountability Office (GAO), Bureau of Land Management Should Address Risks from Insufficient Bonds to Reclaim Wells, GAO-19-615: Published: Sep 18, 2019

[26] Government Accountability Office (GAO), Bureau of Land Management Should Address Risks from Insufficient Bonds to Reclaim Wells, GAO-19-615: Published: Sep 18, 2019. Page 3, 11.

[27] Office of Surface Mining and Reclamation and Enforcement. https://www.osmre.gov/resources/bonds.shtm

If a self-bonded coal company is unable to cover the cost of reclamation, such as in the cases of substantial debt or bankruptcy, the federal government will be left with the cost of cleaning up their mess. The practice of self-bonding has become especially distressing in recent years given the instability of the coal industry. In late 2015 and 2016 three of the top four U.S. coal producers filed for bankruptcy: Peabody Coal, Arch Coal, and Alpha Natural Resources. Just these three companies carried a combined $2.5 billion in self-bonds for reclamation liabilities.

TCS supports the Coal Cleanup Taxpayer Protection Act which would prevent the Office of Surface Mining and Reclamation Enforcement and state regulatory authorities from accepting new self-bonds for coal reclamation.

Methane Waste

For years, TCS has closely tracked royalty payments on natural gas that is lost during the production of oil and gas on public lands. The primary component of the natural gas released during the drilling operations is methane, which is a highly potent greenhouse gas as well as a marketable fuel.

Our own analyses since 2014 shows existing oil and gas management practices have led to the dramatic under-collection of royalties owed to federal taxpayers on this lost gas. Among the problems we identified were the inability to accurately track natural gas that is leaked, vented, or flared during production on federal lands, and the lack of clarity on when to appropriately charge royalties on that lost gas.

TCS supported the 2016 BLM methane rule because it would have led to the capture of more leaked, vented, or flared royalty-free natural gas, bringing more of this gas to market, and collecting millions of dollars more for federal taxpayers each year. TCS supports the reinstatement of the 2016 rule until new methane regulations are implemented that require increased capture, prohibit venting in most cases, require leak detection and repair, among other things, as required by the *Methane Waste and Prevention Act*.

TCS agrees that gas consumed within the area of the lease tract for the purposes of drilling operations, so called "beneficial use" gas, should also be assessed a royalty. Under current rules, operators consume billions of dollars' worth of natural gas for free. From fiscal year 2009 to 2018, operators reported using 1.75 trillion cubic feet of natural gas on federal leases, royalty free.[28] Not only is this another subsidy embedded in the leasing process, but it serves as a disincentive to invest in more efficient, less wasteful pneumatic equipment. Outdated, leaky drilling equipment is a significant source of lost natural gas.

TCS also fully supports provisions which require measurement of disposition of all gas volumes (rather than estimation); require installation of metering devices and the application of civil penalties and other enforcement mechanisms when flaring takes place.

Finally, after years of digging piecemeal through DOI's various datasets, TCS would certainly welcome free, downloadable, searchable, sortable methane data, as required in H.R. 2711.

[28] Data from Oil and Gas Operations Reports (OGOR-B) submitted to ONRR and attained by TCS through FOIA request

Conclusion

The country is now facing a $22 trillion debt. Many things need to be done to resolve the nation's fiscal woes, not the least of which is ensuring federal taxpayers get the revenue they deserve for the resources they own. Federal lands and waters must be used responsibly, and taxpayers must receive appropriate payment and financial assurances from those companies benefiting from resource extraction.

It's never a good idea to leave money on the table. These problems must be resolved as we move forward with additional energy production on federal lands and waters.