

Report of the Commission

**Fiscal Accountability
of the
Nation's
Energy Resources**



David F. Linowes
Chairman

Michel T. Halbouty
Mary Gardiner Jones

Charles J. Mankin

Elmer B. Staats
Commissioners

January 1982

SUMMARY

Management of royalties for the Nation's energy resources has been a failure for more than 20 years. Because the Federal government has not adequately managed this multibillion dollar enterprise, the oil and gas industry is not paying all the royalties it rightly owes.

The government's royalty recordkeeping for Federal and Indian oil and gas leases is in disarray. For this reason, the exact amount of underpayment is unknown. The results of individual audits, which have often uncovered large underpayments, suggest that hundreds of millions of dollars due the U.S. Treasury, the States, and Indian tribes are going uncollected every year.

In addition, oil thefts are occurring on Federal and Indian leases. The extent of theft and the amount of royalty losses from theft are unknown, but it is well-documented that security at many Federal and Indian lease sites is lax and is an open invitation to theft.

The Nation can no longer afford mismanagement of royalties for its energy resources. The stakes are too high. With the rapid escalation of energy prices, oil and gas royalties have risen from less than \$500 million in 1971 to more than \$4 billion in 1981.

The government's royalty management system needs a thorough overhaul. This report of the Commission on Fiscal Accountability of the Nation's Energy Resources details 60 specific recommendations (listed in Chapter Nine of the report) for revising and rebuilding the system. Underlying these recommendations are some fundamental conclusions the Commission reached in the course of its intensive inquiry:

- ° The government's royalty management system must have qualified managers. The scientifically oriented Geological Survey, which now manages royalties, has never been able to supply the active, sophisticated management that is needed. It is largely for this reason that the Commission recommends removing the royalty management function from the Geological Survey. In a separate office with a clearly defined mission, royalty management could attract managers with the training and experience required.
- ° The Federal government should work more closely with States and Indian tribes. In fulfilling its royalty management responsibilities, it should cooperate much more than it has in the past with States and Indian tribes, sharing both information and specific tasks, such as auditing and site inspection.
- ° The Federal government should perform an oversight role. It must not waste its limited resources on tasks that are industry's responsibility. In managing royalty collection, it should not remain mired in bookkeeping details that rightly belong to the lessee. Instead, it should develop systematic, independent cross checks of royalties paid and reports submitted by companies, and it should impose meaningful penalties for false statements or gross errors. In helping to prevent theft, the government should not issue detailed; rigid regulations for security of lease sites. Rather, it should monitor the companies' performances in carrying out their own site security plans and should penalize violations.
- ° The oil and gas industry should carry out its obligation, as lessee, to pay royalties in full and on time. The industry, not the government, has primary responsibility for the detailed record-keeping needed to assure that all royalties are

paid. The industry also has the obligation to assure the security of lease sites. The industry, not the government, is best suited to develop effective site security plans, subject to the government's minimum standards.

If there is one concept that sums up the Commission's overall approach, it is accountability. Oil and gas companies must be held accountable for the obligations they undertake when they lease Federal and Indian lands for minerals production. The Federal government must be held accountable for fulfilling a public trust, that is, assuring that royalties for the Nation's energy resources are fully and fairly collected on behalf of the people of the United States.

The Federal government has not fulfilled this trust in the past 20 years. It is now taking steps to better its performance. Complex and demanding as the task may be, it is achievable if the internal controls, site security standards, and sanctions recommended here are made part of an improved royalty management system.