The Congress declares that it is the policy of the United States that the United States receive ***fair market value*** *of the use of the public lands and their resources unless otherwise provided for by statute.*
43 U.S. Code § 1701

Time for Reform

The Secretary of the Interior has directed BLM to conduct a broad, programmatic review of the federal coal program to identify and evaluate potential reforms. These are some of the problems with the current system BLM needs to address:

How, When, and Where to Lease. BLM needs to examine how the leasing process should work, where to lease and where not to lease. Congress envisioned a competitive process for leasing federal coal; BLM needs to reform the current system to create competition. Other considerations like market conditions should affect the timing of lease sales.

Fair Return. Plenty of evidence suggests the current bonus bids, rents, and royalties received under the federal coal program are not securing a fair return to the American public. BLM must consider how these are calculated and how externalities should be included in the calculation.

Fair Market Value. Both the value of proposed tracts and the price assessed for purposes of royalty calculation on federal coal need to be updated and strengthened. BLM must consider potential exports of domestic coal and how it can evaluate export potential when determining values of federal coal.

TAXPAYERS FOR COMMONSENSE
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Federal Coal:
Getting a Fair Return for Taxpayers

May 2016

Coal is an important energy fuel in America. Over the last few years, an average of 41 percent of U.S. annual coal production came from federal lands. Yet, federal coal leasing has been the source of controversy for decades.

In 2013, both the Government Accountability Office (GAO) and the Interior Department's Office of Inspector General (OIG) issued reports expressing concerns about the federal coal program, particularly with respect to the leasing process and fair market value.

The Bureau of Land Management (BLM) administers 306 coal leases nationwide, covering 482,691 acres in 11 States, with an estimated 7.75 billion tons of recoverable federal coal.

The goal of BLM's review of the federal coal program—from the designation of lease tracts to the reclamation of abandoned mines—should be to create a program that strives for transparency and fulfills the fiduciary responsibility of the Department to manage these public resources on behalf of taxpayers.

"Since even a 1-cent-per-ton undervaluation in the fair market value calculation for a sale can result in millions of dollars in lost revenues, correcting the identified weaknesses could produce significant returns to the Government."

- DOI Inspector General

The BLM hopes to complete the Coal Programmatic EIS over roughly 3 years.

The last comprehensive review of the federal coal program was completed in January 1986.

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Need for Competition

According to GAO, of the 107 tracts leased between 1990-2012, about 90 percent involved a single bidder, which was generally the company that drew the tract. This lack of competition also applies to the coal producing regions in other states. BLM attempts to estimate the fair market value of federal coal have failed to replace competition as the best way to ensure a fair return.

Better Value for Coal

BLM provides information about 105 separate coal lease sales from 1991 to 2014. Combined, these sales account for 8.9 billion tons of minable federal coal. The successful bids for these leases, many of which were the only bids, averaged $0.38 per ton. By contrast, U.S. utilities reported buying coal to produce electricity at an average of more than $40 per ton from 2009-2013.

More Transparency

It is difficult to verify the adequacy of BLM's fair market value analyses because the data and methodology BLM uses are not publicly available. The Washington Office of BLM cannot provide statistics on the number of leases with reduced royalties, the rates involved, and the amounts of royalties foregone.

A Little History

After World War I, Congress enacted the Mineral Leasing Act of 1920 (MLA) directing the Secretary of the Interior to set up leasing systems for the development of federally owned deposits of war-related minerals such as oil, gas, coal, sulfur, and phosphate. The MLA requires the payment of rents, bonuses, and royalties to the government.

In the 1960s and 70s, in response to concerns about speculative leasing and failure to obtain fair value, Congress enacted the Federal Coal Leasing Amendments Act of 1976 (FCLAA), which amended the MLA to require competitive bids and to specify that no bid may be accepted that does not represent fair market value.

Despite Congressional direction, problems with BLM's management of the coal program continued, culminating in the alleged leaking of proprietary data to coal companies in 1982. Both the GAO and the Congressionally-appointed Linowes Commission made recommendations for reforms to the coal program. A few changes were made to the program in 1985, but there has been little meaningful oversight of the program since then.

Getting a Fair Market Value

Fair Market Value (FMV) is at the heart of the reforms enacted by Congress in 1976. However, there are fundamental weaknesses in the federal coal program, from beginning to end, that result in less than a fair return to taxpayers.

The predominant leasing process currently used by the BLM, known as Lease by Application, allows coal operators to "nominate" tracts , which if approved are put up for auction. Not surprisingly, 90 percent of lease sales receive bids from only one bidder, typically the operator of a mine adjacent to the new lease.

Because there is currently very little competition for federal coal leases, BLM's pre-sale estimates of coal value have become critical to the revenues realized by the government. But developing fair valuations for tracts can be both difficult and controversial. When value estimates are too low, it locks in a rolling system of continuing undervalued leases because final lease sale values are used for estimating values of new tracts.

Once the coal is out of the ground, the Office of Natural Resource Revenue (ONRR) estimates the sales value at the mouth of the mine for purposes of determining the royalties owed. Collecting a royalty on the price that coal is sold for at the mouth of the mine fails to capture the true value when that coal is sold at much higher prices on (often foreign) markets.

The royalty rates charged for federal coal are lower than other federal resources. Royalty rates for federal coal are 12.5 percent for surface mines and 8 percent for underground mines. By contrast, the federal government currently charges a royalty rate of 18.75 percent for offshore oil and gas production, and many states charge similar or higher rates for state-owned oil and gas.

Even the royalty rates that coal operators pay for the right to extract and sell taxpayer-owned resources from federal land are commonly reduced. Of the 80 federal leases nationwide reported with sales dates since 1990, 35 of them (44 percent) recorded a royalty rate reduction. All the federal leases in North Dakota sold between 1992 and 2013 received royalty rate reductions, with an average royalty rate of just 2.33 percent.

There are many steps in the process of leasing and selling federal coal, and the BLM has to update many of the policies that govern this process if it is going to fulfill its responsibility to ensure a fair value or fair return to taxpayers.

The federal coal program has been the source of controversy many times in the past for failing to ensure a fair return to taxpayers. It is appropriate for the Interior Department to step back and reevaluate the different steps of the process and to update policies that have not kept pace with today's energy markets.

- Ryan Alexander
President