Summary of GAO Report on Federal Coal Leasing
Prepared for Sen. Edward J. Markey and Rep. Peter DeFazio

February 4, 2014

Background:

Roughly 450 million tons of coal are produced from federal lands each year, according to the Department of Energy. Following allegations of improprieties in coal lease sales held in the Powder River Basin (PRB) in Wyoming and Montana in 1982, then-Rep. Markey requested a Government Accountability Office (GAO) investigation into the lease sales. The GAO report issued in 1983 for Rep. Markey uncovered that the Reagan Administration's Interior Department had sold publicly owned coal in the PRB for roughly $100 million less than it was worth. As a result of that investigation, numerous changes were recommended to the way that Interior leases the federal coal that belongs to American taxpayers.

Because the federal coal leasing program had not been audited by the GAO since 1994, Sen. Markey requested a new GAO review when he was serving as Ranking Democratic Member of the House Natural Resources Committee to ensure that taxpayers in Massachusetts and across the country were not being short changed. The new Ranking Member of the House Natural Resources Committee, Rep. DeFazio, subsequently joined in this request.

The public GAO report being released today highlights a number of problems with the federal coal program, including many of the same issues that were identified following the 1982 PRB sales. As a result, we cannot be sure that taxpayers in Massachusetts and across the country are receiving a proper return on these public resources worth billions of dollars. A non-public version of the GAO report contains additional specificity that serves to further highlight these problems.

<u>Summary of the GAO's Major Findings regarding the Federal Coal Program:</u>

The public version of the GAO report found the following major problems with the federal coal program:

1. Competition for coal leases is still lacking.

Federal law (the Federal Coal Leasing Amendments Act of 1976) generally requires that all coal be offered competitively by the Interior Department (Interior), which conducts leasing through Bureau of Land Management (BLM) state offices. However, for the vast majority of federal coal tracts offered, the GAO found that there is no competition whatsoever.

- *The vast majority of coal leases receive a single bid*. GAO found that roughly 90 percent of the 107 leases it examined involved only a single coal company

> bidding. In 1983, GAO found "a similar lack of competition for federal coal leases" as exists today and concluded that coal leasing "was largely noncompetitive because lease tracts sold 'appear captive to adjacent mining operations."

However, despite this lack of coal industry competition, the GAO found that the federal government is accepting the overwhelming majority of initial coal company bids. The GAO found that when bids are rejected because they do not meet fair market value, companies <u>always</u> bid again at higher prices when the leases are reoffered.

- *The vast majority of those first bids are accepted by Interior*. The GAO found that 83 percent of federal coal tracts were leased the first time they were offered for sale.

The GAO found that for the 18 coal tracts where the initial coal company bid was rejected, companies always bid again and always did so at a higher level. The fact coal companies always bid again at higher levels when the government chooses to deviate from its typical practice of accepting the first bid from a single bidder, seems to suggest the possibility that the Interior Department is undervaluing federal coal resources or could be ensuring a better return for taxpayers.

2. Interior Lacks Rigor and Oversight in Determining the Fair Market Value of Federal Coal Leases.

Given the lack of market competition in coal leases, if the fair market value set by Interior is low, it can lead to significant losses for taxpayers. For instance, for every cent per ton that coal companies decrease their bids for the largest coal leases, it could mean the loss of nearly $7 million for the American people.

- *Interior is not always using multiple approaches to set the fair market value of coal*. BLM's guidance lays out two approaches to develop an estimate of fair market value – one using comparable coal lease sales and one using projected revenue from mining the coal over time. But BLM's guidance does not specify which approach must be used and the GAO found that not all states use both evaluations, as recommended by the appraisal organizations GAO interviewed. GAO concluded that BLM state offices that only use the comparable coal lease sales method "may not be fully considering current or new trends in coal markets when estimating fair market value."

- *Interior is using outdated information*. GAO found that Interior was using coal sales in setting its fair market value that were more than 5 years old. Further, when using these outdated sales numbers, some states did not even make adjustments to account for inflation.

- *Interior is not subjecting appraisals to independent review*. In reviewing the problems with the 1982 PRB coal lease sales, it was recommended that Interior obtain periodic independent reviews of coal activities. However, GAO found that Interior is not using an independent third party office within Interior to review these appraisals.

- *Appraisals are not receiving sufficient review*. The GAO found that BLM headquarters currently reviews only a tiny fraction of coal lease appraisal reports. GAO also found that the reports that underlie the fair market value were consistently not formally approved by the required number of officials and there was no mechanism in place to ensure this proper review occurred. As a result, GAO concluded that "appraisal reports may not be receiving the scrutiny they deserve." In fact, GAO found one state that did not prepare any justification for setting the fair market value at the lowest possible level allowed under the law.

3. Interior is not fully considering the potential of coal exports despite market changes.

U.S. coal exports have been increasing rapidly, primarily to Asia and Europe, where prices are generally higher. U.S. coal exports have more than tripled over the last decade to 12 percent of total U.S. production in 2012. Exports of steam coal – the primary type of coal mined on federal leases -- has also been increasing in recent years, more than doubling from 2010 to 2012 to 55.9 million tons.

- *BLM does not undertake sufficient consideration of exports.* BLM's guidance states that appraisal reports determining fair market value should consider specific markets for the coal being leases, including export potential. But the GAO found that some offices, such as Wyoming, typically contained only "generic boilerplate statements about the possibility of coal exports in the future and the uncertainty surrounding them." Further, many other states did not consider coal exports at all when valuing federal coal.

Because of the lack of competition for coal leases and the fact that they are issued for a 20-year term that can be further extended, not factoring exports to higher priced markets into the valuation of federal coal could mean that taxpayers are not getting a proper return on these valuable resources.

4. Interior is providing limited information to the public.

The GAO found that sufficient information is not being provided to the public, making it difficult to track federal coal leasing and leading to a lack of transparency.

- *BLM does not provide public versions of appraisal reports.* Although agency guidance states that a public version of the fair market value appraisal report that deletes all proprietary information should be made available, the GAO found that BLM has not been following this guidance.
- *There is inadequate information on agency websites.* The main BLM website does not include consolidated information on past or upcoming coal sales and the lack

> of this information is hampering the ability of the public to track federal coal leasing activity. Moreover, most state offices do not maintain information on past coal lease sales on their websites. This lack of information on Interior websites occurs despite OMB guidance directing federal agencies to use electronic media to make information more accessible to the public.

Conclusion

The public GAO report highlights similar problems with the federal coal leasing program as were identified following the 1982 PRB lease sales. The GAO reports identifies a lack of industry competition and problems with the way that Interior determines the value of public coal leases, meaning that the American people cannot be assured that they are getting a fair return on these tremendously valuable resources they own.

It is imperative that we ensure proper taxpayer protections are in place prior to moving forward with new coal leasing. As a result, Sen. Markey is transmitting a public letter to the Interior Department today calling on the Department to implement the reforms recommended by the GAO before conducting any future lease sales.