

# Correction & Clarification

Article:

**Royalties Not in line with profits**

Reporter:

**Edmund L. Andrews**

Paper:

**New York Times via The Denver Post**

Publication Date:

**January 23, 2006**

Issued by:

The Independent Petroleum Association of Mountain  
States

410 17<sup>th</sup> Street, Suite 1920

Denver, CO 80202

(303)623-0987

[www.ipams.org](http://www.ipams.org)

**January 27, 2006**

Contact: Andrew Bremner

# Royalties not in line with profits

*Low natural-gas payments to the government appear parallel to oil scandals of the past, a report finds.*

By Edmund L. Andrews  
*The New York Times*

**Washington** — At a time when energy prices and industry profits are soaring, the federal government collected little more money last year than it did five years ago from the companies that extract more than \$60 billion in oil and gas from publicly owned lands and coastal waters.

If royalty payments in fiscal 2005 for natural gas had risen in step with market prices, the government would have received about \$700 million more than it actually did, a three-month investigation by *The New York Times* has found.

But a complicated set of federal regulations, largely shaped and fiercely defended by the energy industry, allowed companies producing natural gas to provide the Interior Department with much lower sales prices — the crucial determinant for calculating government royalties — than they reported to shareholders.

As a result, the nation's taxpayers — collectively, the biggest

Because there was less production than in 2001.

What's the methodology? It's never disclosed in the article.

Most federal regulations are complicated. Federal Regulations are promulgated through publication in the Federal Register and the public is given the opportunity to make comments. You provide no basis for industry "fiercely" defending the regulations.

Figures are Not Comparable. It will always be lower because of the different reporting requirements for royalties and the SEC. The value received for natural gas is disclosed to MMS as well as any deductions.

# DRILL: Royalties for natural gas questioned

< CONTINUED FROM 1A

owner of U.S. oil and gas reserves — have missed much of the recent energy bonanza.

The new disparities in natural gas parallel those uncovered five years ago in a wave of scandals involving royalty payments for oil. Between 1998 and 2001, a dozen major companies, while admitting no wrongdoing, paid a total of \$438 million to settle charges that they had fraudulently understated their sales prices for oil.

Since then, the federal government has tightened its rules for oil payments. But with natural gas, the Bush administration recently loosened the rules and eased audits intended to uncover cheating.

Administration officials say they have found no evidence of wrongdoing.

Industry executives say the disparities stem primarily from different rules for calculating the sales prices for paying royalties and the sales prices for informing shareholders.

"The price of gas downstream is always going to be higher because you have costs that have to be recouped for getting it to the customer," said Robert Davis, a spokesman for Exxon Mobil. "You have to process the gas. You have to transport it, and you have to sell it. There will always be a discrepancy there."

Companies that pump oil and gas on federal property are required to pay the government royalties, usually 12 percent to 16 percent of the value of what they sell.

Gas is often sold through longer-term contracts, but royalties should track relatively closely with market prices. Indeed, payments to the government have climbed significantly in the past three years, after plunging in 2002 in tandem with the market.

The rise, however, has lagged behind the resurgence in prices.

Because much of the information about specific transactions is secret, it remains unclear to what extent, if at all, the weakness in royalty payments stems from deliberate cheating or from problems with the rules themselves.

But one major producer, Burlington Resources, acknowledged to shareholders last year that it might have underpaid about \$76 million in gas royalties during the 1990s. And in Alabama, a jury ruled in 2003 that Exxon had cheated on \$63.6 million in royalties from wells in state-owned waters. The jury awarded \$11.9 billion in punitive damages, which a judge later reduced to \$3.5 billion. Exxon disputes the charges and is appealing the verdict.

The possible losses to taxpayers in gas could be even higher than the losses tied to the earlier scandals over oil royalties.

For one thing, natural gas production on federal land is worth twice as much as oil production.

Moreover, the Interior Department has scaled back on full audits, pushed out a couple of its more aggressive auditors and received scathing criticism from its inspector general for the audits that it did pursue.

"We are talking about the same issues and in many cases the same players as before," said Danielle Brian, executive director of the Project on Government Oversight, a nonprofit watchdog group that exposed many of the scandals over oil royalties.

"It was definitively proven that these very companies had knowingly been cheating on oil for years, if not decades," Brian said. "To ignore the likelihood that the same thing is happening on the gas side is absurd."

Not True. The rise and fall of royalty revenues do not necessarily track "in tandem" with the changes in EIA's wellhead and MMS's unit price received. Some years' revenues exceeded the change in price — does that mean companies overpaid?

Or neither. Further, the government has always had stringent reporting requirements and keeps the records of sales and deductions.

This matter has been in dispute for years. The statement was to justify a set aside of funds in case the matter settled.

MMS Reports 505 audits for FY 2005 and 123 for FY 1998.

The agency responsible for ensuring proper payment has found no evidence of wrongdoing.

If any.

Two different sets of rules. One requires gross figures and the other requires a net figures for each lease. Regardless, sales price and any deductions must be reported to MMS.

"Scathing criticism" was based upon audits mainly performed during the last administration.

## Fiscal Year 2005

\$60 Billion Generated, \$8.2 Billion Royalty Revenues, 13.66% in royalties.

POGO, a group found to have paid two government officials \$383,000. See Thompson Report, July 2000, S. Prt 106-55.

Perhaps the long-term contracts contain part of the answer.