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UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548



RESOURCES AND ECONOMIC
DEVELOPMENT DIVISION

February 5, 1976

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The Honorable
The Secretary of the Interior 33

Dear Mr. Secretary:

During our review of the appropriateness of and compliance with acreage limitations on several minerals for the Chairperson of the Mines and Mining Subcommittee, House Committee on Interior and Insular Affairs, we noted a matter which we believe warrants your immediate attention.

The Bureau of Land Management did not apply the regulatory requirements calling for minimum royalty payments on potash and sodium leases based on minimum production. Instead, we found that minimum royalties were limited to rental rates, which were much less than royalties based on minimum production levels. The minimum royalty for another mineral (phosphate) included in our review was also based on the rental rate.

As you are aware, thousands of acres of land have been held under mineral leases for more than 10 years without development and thousands of additional acres are involved in pending leases which will be evaluated by the Bureau this year. Therefore, your prompt action could (1) help to encourage the development of the land leased, (2) add considerable income for the Federal Government, and (3) discourage the leasing of lands that would not be developed immediately.

STATUTORY AND REGULATORY PROVISIONS

The Mineral Lands Leasing Act (30 U.S.C. 212 and 283) concerning minimum royalties on phosphate and potash leases states:

"Leases shall be conditioned upon a minimum annual production or the payment of a minimum royalty in lieu thereof, except when production

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is interrupted by strikes, the elements, or casualties not attributable to the lessee."

The act does not have a similar provision for sodium leases. However, the mineral leasing regulations (43 CFR 3503.3-2 (b)(2)) for both sodium and potassium (potash) have the following provision:

"Leases will require the payment of a royalty on a minimum annual production beginning with the sixth full calendar lease year, unless operations are interrupted by strikes, the elements, or casualties not attributable to the lessee***."

The regulations (43 CFR 3503.3-2 (b)(3)) also provide that, for phosphate leases, the minimum royalty based on minimum production levels or payment of a minimum royalty, in lieu thereof, will begin with the fourth year from the date of the lease.

MINIMUM ROYALTY PROVISIONS NOT BASED
ON MINIMUM PRODUCTION LEVELS

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/ The Bureau of Land Management issues Federal mineral leases and the Geological Survey recommends lease terms and minimum royalties. The minimum royalty provision in the most recent potash and sodium leases was \$1 per acre and in the most recent phosphate leases was \$3.50 per acre. Bureau and Survey officials said that these provisions were not based on minimum production levels but on lease rental rates. The officials were unable to provide information on why the minimum royalty rates were based on rental rates instead of on minimum production levels. 215

The most recent potash and sodium leases contain an annual rental rate of \$1 per acre for the sixth and subsequent years, and the most recent phosphate leases contain an annual rental rate of \$3.50 per acre for the fourth and subsequent years. The act and regulations provide that any royalties due shall be reduced by the amount of rent paid. Therefore, the net effect of the Bureau's current practice on a nonproducing lease is that no royalties are paid.

Both agencies provided information which demonstrated large differences between minimum royalty rates based on minimum production levels and those based on rental rates.

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For example, the Survey estimated that the minimum annual production level of phosphate for a 133-acre lease in Utah should be about 10,000 tons. On the basis of this minimum production level, the Survey estimated that the lessee would have paid a minimum royalty of about \$23 per acre, whereas the lease actually required a rate of \$3.50 per acre.

The Government is incurring considerable losses of royalty revenue because many outstanding leases have minimum royalties based on rental rates. For example, 12 nonproducing lessees in Wyoming controlled 49,600 acres in 30 leases which were held 8 to 17 years. A Bureau official reported that all leases had a \$1 per acre minimum royalty rate. The Survey had no estimate of what the minimum royalty amount would have been had it been based on production.

Bureau officials told us that they will evaluate and consider applications for new leases and 20-year renewals involving several thousand acres this year. For example, in Utah and Idaho 67 lease applications are pending involving about 51,600 acres. Bureau offices in Utah and Idaho also have pending potash and phosphate prospecting permit applications exceeding 120,000 acres in each State. If valuable minerals are identified, preference right lease applications will follow. If the current minimum royalty provisions are established in the prospective leases based on rental rates, then considerable losses to the Federal Government will result.

We believe that the lessee should pay a minimum royalty based on a minimum production level beginning with the time periods specified in the regulations. Such minimum royalty provisions would tend to encourage development, discourage speculation, and provide a greater return to the Government. Therefore, we recommend that you require the Bureau of Land Management to include in all future phosphate, potash, and sodium leases a minimum royalty provision based on minimum production levels.

The Bureau agreed with our recommendation. We discussed the matter with Survey officials, but we were unable to obtain any specific comments as to whether they agreed or disagreed with our recommendation. An official in the Office of the Solicitor stated that the Bureau's practice

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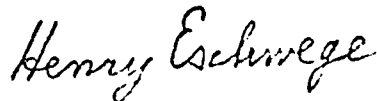
of charging a minimum royalty on potash, phosphate, and sodium leases based on the rental rate rather than minimum production levels had not been previously brought to their attention but added that they would now study the matter.

As you know, section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the House and Senate Committees on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Director, Office of Management and Budget; appropriate congressional committees; the Director, Bureau of Land Management; and the Director, Geological Survey.

We would like to be informed of any action taken on our recommendation. If you wish, we would be glad to discuss this report with you or your staff.

Sincerely yours,



Henry Eschwege
Director