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# Royally Losing II: Below market royalty rates cost taxpayers billions of dollars in new revenue as oil and gas companies cash in on high prices



The federal government **lost up to \$13.1 billion in revenue from oil and gas drilling on federal lands from 2012 through 2021**, because it continues to apply a grossly outdated royalty rate set in 1920. Lost potential revenue **hit a record high of \$2.3 billion in 2021** as oil prices spiked. Bringing the onshore federal royalty into the modern era, in line with rates for state and offshore production, will stem the losses and generate billions of dollars more for federal and state coffers in the coming decades.

Federal lands throughout the Western United States contain vast deposits of valuable oil and gas resources. The U.S. government holds millions of acres of these lands in trust for the true landowners, federal taxpayers.

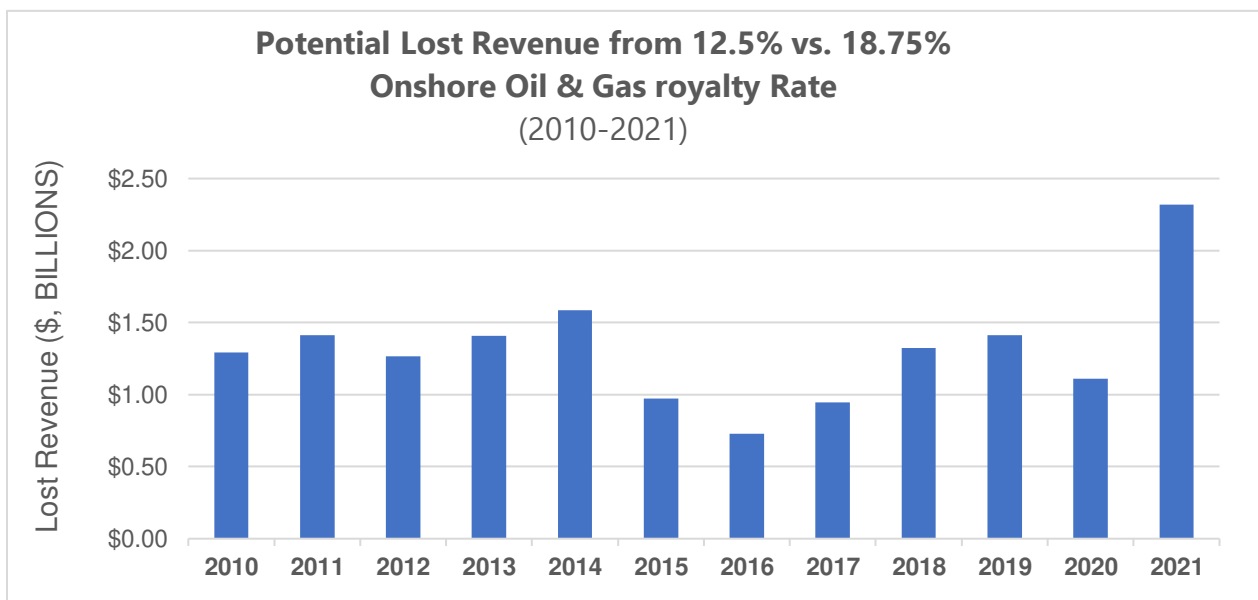
## The federal royalty rate - est. 1920

The Mineral Leasing Act of 1920 (MLA), 30 U.S.C. §181 et seq., established the process for leasing, managing, and developing publicly owned lands for oil and gas exploration and development. Since the 1970s, this process and much of the U.S. mineral estate has been administered by the Bureau of Land Management (BLM), an agency within the Department of the Interior (DOI). In exchange for the right to drill on federal lands, the BLM requires lessees to pay a bid at auction (not in all instances),<sup>1</sup> annual rent per acre of land leased, and a royalty on the value of extracted resources.

**More than 100 years ago**, the MLA established the royalty rate charged for the removal and sale of oil and gas from federal lands at no less than 12.5 percent of the resources' market value. That value fluctuates with the prices oil and gas producers can get for their products. The Secretary of the Interior has the authority to prescribe a higher royalty rate for oil and gas leases on federal lands.

In 2021, rising prices for natural gas and especially oil led the value of resources extracted from federal leases to surge. The amount of revenue taxpayers lost because producers paid royalties at just 12.5 percent of market value instead of the more common 18.75 percent also surged, up to \$2.3 billion (see graph).

The stagnant 12.5 percent royalty rate charged on federal lands stands in stark contrast to the increases states with significant oil and gas deposits have instituted for their royalty rates. Texas, Wyoming, New Mexico, Colorado, and Utah have increased their royalty rates for leases on state lands numerous times over the past few decades.



Congress considered increasing the minimum royalty rate during the last overhaul of the onshore oil and gas leasing system in 1987. At the time, DOI officials cited widespread use of the 12.5 percent rate on state and private lands as a reason for maintaining it for federal leases.<sup>ii</sup> The subsequent adoption of higher rates for leases on state lands in many states undermines that rationale for continuing the 12.5 percent rate today.

**The royalty rate has even changed for leases in federal waters.** Between 2006 and 2008, the Bush Administration increased the royalty rates for offshore drilling in federal waters to 18.75 percent. According to our analysis of DOI data, **if the onshore royalty rate had been set at 18.75 percent**, in parity with offshore oil and gas, **onshore production could have generated up to \$13.1 billion** in additional royalty revenue from 2012 to 2021.<sup>xix</sup>

A higher royalty rate would have also provided a boon to western states, as half of royalty revenues collected by the federal government are returned to the state where the development takes place. As the source of most onshore federal oil and gas production, Wyoming and New Mexico would stand to gain the most from a higher royalty rate (see table on next page).

<b>Federal Rate Lags State Rates</b>	
The federal royalty rate has not been updated since 1920 while state rates have risen several times	
<b>Leasing Jurisdiction</b>	<b>Oil &amp; Gas Royalty Rate</b>
<b>Texas</b>	<b>20 - 25 percent<sup>iii</sup></b>
<b>Pennsylvania</b>	<b>20 percent<sup>iv</sup></b>
<b>Alaska</b>	<b>12.5 or 16.67 percent typically<sup>v</sup></b>
<b>Oklahoma</b>	<b>18.75 percent<sup>vi</sup></b>
<b>North Dakota</b>	<b>16.67 or 18.75 percent<sup>vii</sup></b>
<b>New Mexico</b>	<b>18.75 - 20 percent<sup>viii</sup></b>
<b>Louisiana</b>	<b>20 - 25 percent<sup>ix</sup></b>
<b>Colorado</b>	<b>20 percent<sup>x</sup></b>
<b>West Virginia</b>	<b>20 percent<sup>xi</sup></b>
<b>Wyoming</b>	<b>16.67 percent<sup>xii</sup></b>
<b>California</b>	<b>Generally, 16.67 percent min.<sup>xiii</sup></b>
<b>Arkansas</b>	<b>up to 25 percent<sup>xiv</sup></b>
<b>Utah</b>	<b>16.67 or 18.75 percent<sup>xv</sup></b>
<b>Montana</b>	<b>16.67 percent<sup>xvi</sup></b>
<b>Mississippi</b>	<b>18.75 percent<sup>xvii</sup></b>
<b>Michigan</b>	<b>16.67 percent<sup>xviii</sup></b>
<b>Private Lands</b>	<b>Generally, 12.5 - 25 percent</b>
<b>Federal Lands</b>	<b>12.5 percent, sometimes less</b>
<i>Note:</i> States shown are top 20 states ranked by total production of oil and gas, 2018-2020. Ohio (9), Kansas (15), Alabama (17) and Virginia (20) are excluded due to either limited data or the lack of leasing on state lands.	



## The oil and gas industry is cashing in

While federal and state taxpayers miss out on increased revenues from higher oil prices, federal lessees and the industry in general is claiming that revenue in their books and funneling it to their shareholders. After the price of oil rose in the third and fourth quarters, the top 20 U.S. oil and gas drillers reported combined profits of \$73.6 billion in 2021, roughly three times what the same group reported in 2019. Exxon Mobil and Chevron led the pack with \$23 billion and \$15.6 billion in profits, respectively.

### Potential Lost Revenue from 12.5% vs. 18.75% Onshore Oil & Gas Royalty Rate by State (2012-2021)

(\$, millions)

State	Max Lost Revenue	State Share
Alaska	\$78	\$69 <sup>xx</sup>
California	\$505	\$247
Colorado	\$757	\$371
Montana	\$110	\$54
New Mexico	\$6,067	\$2,973
North Dakota	\$1,053	\$516
Utah	\$746	\$365
Wyoming	\$3,498	\$1,714

When reporting their results for Q3 and Q4 2021, many companies announced new programs to distribute their windfall revenue from high prices to their investors. Exxon Mobil and Chevron corporations announced their intent to spend up to \$10 billion each buying up their own common stock to boost its value to shareholders. Devon Energy, EOG Resources, and Pioneer Natural Resources announced they would distribute Q3 and Q4 earnings through special cash dividends worth up to \$4.2 billion combined. The boards of those three companies also authorized stock buyback programs worth \$10.6 billion.

Some of that windfall revenue could have been directed to taxpayers instead if the BLM had updated its terms for leasing federal lands years ago. If the BLM increases the federal onshore royalty rate now it would ensure taxpayers aren't left out of the next boom, while having negligible effect on overall production.

## Raising the federal royalty rate to meet the market

The available evidence suggests that increasing the federal onshore royalty rate would increase revenue without driving developers away, as industry representatives have claimed. Oil and gas production occurs where fossil fuel reserves are located—be that state, private, or federal land. When several states adopted higher royalty rates for their oil and gas leases, there was no noticeable drop in production on state lands.<sup>xxi</sup>



When studying an increase to the onshore royalty rate to 18.75 percent, the independent Congressional Budget Office found it would generate roughly \$400 million in the first decade while the effect on production of oil and gas on federal lands would be “negligible.” According to the CBO, oil and gas companies’ production decisions are primarily influenced by physical factors and market forces. The probability of finding oil or gas, the expected amount, the extraction costs, the current and expected future prices for oil and gas, and the firms’ costs of capital all have a large influence on a company’s decisions. Factors within a given leasing system, like the royalty rate, have a lesser impact.<sup>xxii</sup>

By continuing to retain the outdated royalty rate of 12.5 percent, the BLM has deprived federal and state taxpayers of tens of billions of dollars over the course of decades. Increasing the oil and gas royalty and reforming the royalty collection system is paramount if taxpayers are to receive a fair return for these valuable resources.

## **Time for Reform**

Low royalties on oil and natural gas produced on federal lands have deprived the federal treasury of billions of dollars. There are steps that both Congress and the Administration can take to reform oil and gas royalty collection policies. Congress can pass legislation to amend the Mineral Leasing Act of 1920 and update the royalty rate to 18.75 percent. The Administration can also increase the royalty rate for oil and gas produced on federal lands through rulemaking or on a lease sale-by-lease sale basis.

As oil prices surge and taxpayers lose considerably more potential revenue, it is it time to bring the federal oil and gas system into the modern era and ensure taxpayers receive a fair return for the use of their public lands by increasing the royalty rate from 12.5 to 18.75 percent, in line with the rate currently charged for offshore production.



## Endnotes

### PHOTO CREDITS

p. 1 – Drill Rig Mallik Test Site. Source: USGS.

p. 3 – CA Oil Pumps. © CGP Grey via Flickr.

p. 5 – Drilling. © Lostinfog via Flickr.

<sup>i</sup> The BLM allows oil and gas companies to avoid bidding for parcels of federal land at auction and acquire leases noncompetitively as soon as the day after a parcel is offered in a lease sale. The process is a relic of the leasing system in place prior to 1987. Roughly 1.8 million acres have been leased noncompetitively over the last decade.

<sup>ii</sup> J. Steven Griles – Assistant Secretary for Land and Minerals Management, U.S. DOI – in testimony before the House Committee on Interior and Insular Affairs, Subcommittee on Mining and Natural Resources. July 28, 1987.

<sup>iii</sup> H. Philip (Flip) Whitworth, “Leasing And Operating State-Owned Lands For Oil And Gas Development,” *Texas Tech Law Review*, Vol 16:672-724 (1985)

<sup>iv</sup> Pennsylvania Treasury transparency portal data; all leases executed since 2018 have had 20%.

<https://patreasury.gov/transparency/e-library>

<sup>v</sup> Alaska Statutes § 38.05.180 sets the minimum royalty at 12.5 percent. But more recent leases have had 16.67%. On rare occasions royalty is charged on a sliding scale <https://www.dor.alaska.gov/Portals/5/Docs/Publications/acloserlook.pdf>

<sup>vi</sup> CBO, “Options for Increasing Federal Income From Crude Oil and Natural Gas on Federal Lands,” April 2018.

[https://www.cbo.gov/sites/default/files/114th-congress-2015-2016/reports/51421-oil\\_and\\_gas\\_options-OneCol-3.pdf](https://www.cbo.gov/sites/default/files/114th-congress-2015-2016/reports/51421-oil_and_gas_options-OneCol-3.pdf)

<sup>vii</sup> Government Accountability Office (GAO), “Raising Federal Rates Could Decrease Production on Federal Lands but Increase Federal Revenue,” June 2017. GAO-17-540. <https://www.gao.gov/assets/gao-17-540.pdf>

<sup>viii</sup> *Ibid.* The New Mexico State Land Office offered all parcels for lease with a 18.75 or 20% royalty rate in the last four years. In prior years, some parcels were leased with a 12.5-16.67% rate.

<sup>ix</sup> LSA- R. S. 30:127 sets the minimum rate at 12.5% but the state negotiates lease-specific rates. Recent lease sales have royalties ranging from 20 to 25 percent

<sup>x</sup> GAO-17-540. Some parcels not sold with the 20% rate are offered in subsequent sales with an 18.75% rate.

<sup>xi</sup> West Virginia Department of Commerce, Mineral Development - About the Process,

<https://wvmineraldevelopment.org/about-the-process>

<sup>xii</sup> GAO-17-540. For parcels offered but unsold in a previous sale, the rate is set at 12.5 percent.

<sup>xiii</sup> Ca. Pub. Res. Code § 6827

<sup>xiv</sup> According to Arkansas Oil and Gas Commission, Arkansas statute provided royalty is 12.5%. Lease sale data is unavailable, but royalties charged on state lands of up to 25% have been documented. <https://www.nwaonline.com/news/2010/jan/16/natural-areas-mineral-rights-leased-20100116/>

<sup>xv</sup> GAO-17-540. Starting in 2017, some leases offered with an 18.75% rate. The royalty is set at 12.5 percent on occasion if approved by the Director of the Utah Trust Lands Administration.

<sup>xvi</sup> GAO-17-540

<sup>xvii</sup> Mississippi Code § 29-7-3

<sup>xviii</sup> Michigan Department of Natural Resources, Oil and Gas Leasing Procedure.

<https://www2.dnr.state.mi.us/publications/pdfs/insidednr/publications/DNRPolProc/27.23.14.htm>

<sup>xix</sup> Estimate calculated from actual royalties collected from oil, gas, and natural gas liquids (NGL) production from federal, onshore leases reported by the Office of Natural Resources Revenue. Other commodities produced from BLM oil and gas leases like carbon dioxide and sulfur were omitted. The estimate captures additional potential royalty revenues had an 18.75% rate been in place for all BLM-managed leases using the sales value of resources net of transportation and processing deductions. The figure reflects a maximum, recognizing the potential for some, though likely minimal, deterred federal production under the alternative scenario of an 18.75% rate set decades ago. It also does not attempt to forecast increases in revenue from legislation setting an 18.75% rate prospectively.

<sup>xx</sup> Under current law, states other than Alaska receive 50% of all revenues collected from resource development in those states. Alaska receives 90%. Disbursements to states are subject to a 2% administration fee, which is deposited in the Treasury.

<sup>xxi</sup> In interviews conducted by the Government Accountability Office, officials from both Colorado and Texas stated raising their state royalty rates did not have a significant effect on production. (GAO-17-540)

<sup>xxii</sup> Congressional Budget Office, “Options for Increasing Federal Income From Crude Oil and Natural Gas on Federal Lands,” April 2018. [https://www.cbo.gov/sites/default/files/114th-congress-2015-2016/reports/51421-oil\\_and\\_gas\\_options-OneCol-3.pdf](https://www.cbo.gov/sites/default/files/114th-congress-2015-2016/reports/51421-oil_and_gas_options-OneCol-3.pdf)