OFFICE OF
INSPECTOR GENERAL
U.S. DEPARTMENT OF THE INTERIOR

NOV 15 2013

The Honorable Ron Wyden
Chairman, Committee on Energy and Natural Resources
United States Senate
Washington, D.C. 20510-6150

Dear Mr. Chairman:

This letter is in response to your letter dated October 23, 2013 regarding the Federal Coal Leasing Program. Our response to your questions is as follows:

In our response to question 1, at Bureau of Land Management's (BLM) request, we are not including BLM's pre-sale Fair Market Value (FMV) determinations (pre-sale FMV) and the difference between the pre-sale FMV and selling price for each listed lease sale on the chart. We also have not included the pre-sale FMV for the listed sales on the chart in our response to question 3. BLM, in consultation with the Department's Office of the Solicitor, has asked us to exclude this information to preserve the confidentiality of the pre-sale FMV. They have asserted that excluding this information will protect the Federal government and the American taxpayer's interest in receiving fair value for future federal coal leases. Specifically, they explained that disclosing the pre-sale FMV of a particular coal tract, even after it is leased, would allow bidders at future lease sales to "reverse engineer" the BLM's derivation of pre-sale FMV and adjust the bids to just slightly exceed the pre-sale FMV. Thus, the net effect of the release of the pre-sale FMV would very likely depress coal lease bids, resulting in less money to the U.S. Treasury and in contravention of the public and taxpayer interests.

If you feel that the FMV information is necessary for your activities, we ask that you seek this information from BLM directly. BLM explained to my General Counsel that they will work with your Committee to resolve any concerns.

1.) In its audit, the Office of Inspector General examined four individual coal lease sales that it estimated lost combined revenue of $2 million. However, the audit did not identify important information that is necessary to evaluate how and why BLM lost the revenue it did, if other leases experienced similar revenue shortfalls, and whether the BLM has taken appropriate steps to avoid such losses in the future.

   a) For each of the four sales, please identify the (i) coal tract that contributed to this loss in revenue; (ii) the selling price for the tract; (iii) the date of the sale; (iv) the size of the tract in tons and acres; (v) the State office in charge of the sale, and (vi) factors that led to accepting under-valued bids.
   Response: In our sample of 15 coal lease sales, BLM awarded 4 leases at a price below FMV, as shown in the following table.

Lease Number (Coal Tract)	Mine	BLM State Office	Date of Sale	Size of Tract		BLM FMV	Selling Price	Difference (Lost Revenue)
				Acres	Tons			
NMNM-78371	Salt River Project	New Mexico	07/31/91	3,082	19,600,000		$1,571,963	
NMNM-86717	Salt River Project	New Mexico	07/31/91	3,360	10,000,000		$799,680	
COC-068590	Colowyo Coal Co. LP	Colorado	05/30/07	1,407	92,000,000		$13,106,600	
COC-71429	Sage Creek Coal Co.	Colorado	08/22/12	400	3,240,000		$800,000	
Total								**$2,042,675**

b) In conducting these sales, the audit found that the State offices "did not comply with the [Mineral Leasing Act] because they accepted bids that were below the estimated [Fair Market Value]."

i. Which State offices did not comply with the Mineral Leasing Act?
Response: BLM's Colorado and New Mexico State Offices did not comply with the Mineral Leasing Act by accepting bids below the FMV.

ii. What section, or sections, of the Mineral Leasing Act did these State offices violate?
Response: The Mineral Leasing Act of 1920, as amended by the Federal Coal Leasing Amendments Act of 1976, § 2 (1) states that: "No bid shall be accepted which is less than the fair market value, as determined by the Secretary, of the coal subject to the lease."

iii. What actions have been taken to ensure that State offices will not engage in such violations in the future?
Response: BLM concurred with our report's recommendation that BLM should reject bids less than the established FMV, and appointed a high-level official responsible for implementing the recommendation. BLM stated that full implementation will be completed by May 31, 2014. In brief, BLM will issue supplemental guidance reiterating the lease sale requirements contained in its economic evaluation handbook. In addition, BLM will strengthen its Washington Office review of the State offices' FMV estimates, and will include a Washington Office minerals specialist in the post-sale panel for most lease sales.
To assess whether report recommendations are in fact implemented, we instituted a "verification review" process to check on the progress of the Department and bureaus. Accordingly, we will conduct a verification review after BLM has had sufficient time to complete the necessary corrective actions.

2) On page 7, the audit says "BLM should reflect the export potential in its [Fair Market Value] calculations to ensure the Government receives proper value for lease sales. … however, it appears that several State offices overlook the export potential, thus possibly undervaluing the public's coal."

i. Please list the states where Federal leases are located that have produced coal for export.
Response: Colorado, Montana, and Wyoming have recently produced Federal coal for export. Mining companies in other States may be exporting or making plans to export coal.

ii. Which State offices "overlook the export potential" of Federal coal leases?
Response: During our evaluation, we reviewed selected coal lease sale files from the following State offices: Colorado, Montana, New Mexico, Utah, and Wyoming. Based on our review, we determined that these State offices generally did not factor in export prices in the FMV determination. For some lease sales in these States, coal exports were briefly mentioned, but did not include an in-depth analysis. The Utah State Office, however, did a full analysis of the export potential in an appraisal for one coal lease sale in 2012, as described in item iii.

iii. Which State offices included an analysis of current coal export levels in pre-lease appraisals, Fair Market Value and other pre-lease documents?
Response: The BLM Utah State Office engaged a consultant to prepare the appraisal for a coal lease sale in 2012. The appraisal included an analysis of the export potential. Coal mined in Utah, however, has not been exported since 2003, and therefore, an analysis of current export levels was not relevant to the appraisal.

In the economic report component of an FMV appraisal, the BLM Wyoming State Office briefly mentioned current exports of Powder River Basin coal to Canada. However, the FMV determination did not contain an analysis of exports.

iv. Which State offices included an analysis of expected future coal exports in pre-lease appraisals, Fair Market Value and other pre-lease documents?
Response: The Utah State Office included an analysis of future coal exports in the appraisal report for a sale in 2012 and the results were reflected in the FMV determination.

v. What guidance has the Bureau of Land Management provided State offices in regards to evaluating coal exports?
Response: The BLM Washington Office generally is not involved in the preparation for a coal lease sale, as this is the responsibility of the applicable State office. As a result, State offices do not have strong guidance from the Washington Office regarding the analysis of coal export potential.

3.) In several instances, the audit discusses, but does not disclose, individual State BLM offices that have either run afoul of Departmental regulations, or have not followed guidance meant to ensure compliance with leasing procedures. It is important to know and understand additional information about these instances, especially given that the audit acknowledges the Bureau's headquarters staff "does not have direct lines of authority for the coal program," and "although the Washington Office manages the coal program, it does not directly control the program in many State and field offices that oversee coal leases."

a) On page 7, the audit says that there were "two recent sales in one State" in which "BLM developed its comparable sales analyses using a lower bid amount instead of the higher, actual sales price," for comparable sales. Please identify—
   i. the relevant coal tracts;
   ii. the selling price for the tracts;
   iii. the dates of the sale;
   iv. the size of the tracts in tons and acres;
   v. the State office in charge of the sales;
   vi. the prices for the lower bid and actual sales figure used in the comparable sales analyses; and

Lease Number (Coal Tract)	Mine Company	BLM State Office	Date of Sale	Size of Tract		BLM FMV	Selling Price
				Acres	Tons		
W. Antelope South WYW-177903	Antelope Coal, LLC	Wyoming	09/01/2011	1,909	721,150,000		$49,311,500
N. Porcupine WYW-173408	BTU Western Resources	Wyoming	06/28/2012	8,982	56,360,000		$793,270,311
Total							**$842,581,811**

   vii. the factors that led to the undervaluing.

Response: The following table summarizes the details from the two coal sales. For both tracts, BLM largely based its FMV on an analysis of comparable sales in the region. In doing so, BLM identified various prior sales it considered to be similar (i.e. comparable) to the subject sales. BLM, however, decided that the lower sale prices should be considered in the comparable analysis, rationalizing that the higher prices did not represent actual market conditions. In our opinion, given that only one company historically bids on a lease sale, BLM's FMV represents the only form of competition for the bidder. Accordingly, rather than rationalizing a low price, BLM should more aggressively establish its FMV.

b. On page 10, the audit says that: "The process for accepting the winning bid at a lease sale is not consistent among BLM State offices," and that "at least three State offices . . . have allowed companies to provide information to justify their original bid."
   i. Which State offices engaged in these types of negotiations and information-sharing with companies, and over what period of time?
   Response: Staff from the BLM Colorado, New Mexico, and Utah State

Offices said they collected additional information from bidders after a lease sale was held to determine whether a lower bid should be accepted. This practice has been used for at least the past decade.

ii. The audit recommended that BLM negotiate with coal companies in the cases of failed first bids, suggesting it would be a more efficient and timely process than setting up a second lease sale. However, the audit notes that this type of negotiation process "would likely require legislative change to the MLA and revision of applicable regulations." Given this conclusion, are State offices operating in compliance with current statute and regulation when they allow companies to justify their original bids below FMV? How do the information exchanges between State offices and potential lessees differ from the recommended negotiations that the audit says would require legislative changes?
Response: Acceptance of a bid lower than the established FMV does not comply with the Mineral Leasing Act, as amended; and Title 43 Code of Federal Regulations, § 3422.3-2. Using direct negotiations with coal companies to establish the sales price would necessitate a change to the law and regulations.

Some BLM State and field offices have conferred with the mining company during the sale process to expedite the completion of a coal lease sale. These offices allowed companies to justify their initial failed bids to avoid the extra time and effort involved in holding a reoffer, which basically restarts the sale process. In our view, this is a form of negotiation currently prohibited by law and regulation.

iii. On page 10, please identify two states' offices that "normally reject a bid that does not meet or exceed the FMV."
Response: The BLM Montana and Wyoming State Offices normally rejected a bid that did not meet or exceed the FMV.

c. On page 11, the audit says that "some State offices do not adequately safeguard the [Fair Market Value] records" and reported that, despite strict data security standards, there was an "instance where one employee locked an appraisal in a standard file cabinet in a cubicle that other employees could access."

i. Please identify whether the lapses cited in the report pertained to pre-sale appraisals or post-sale appraisals, as outlined in BLM guidance.[1]
Response: The lapses included both pre-sale and post-sale appraisal records.

ii. Which State offices do not adequately safeguard Fair Market Value records?
Response: The BLM Colorado and Wyoming State Offices did not

[1] See sections IV and V of H-3070-1, Economic Evaluation of Coal Properties.

adequately safeguard FMV records.

iii. Please identify the State office (or offices) cited in the report where the appraisal data was locked in a standard filing cabinet that could be accessed by other employees.
Response: The appraisal file at the BLM Colorado State Office was kept unsecured in a vacant cubicle with open access to all other employees. Appraisal data at the Wyoming State Office was maintained in a current employee's cubicle with open access to all other employees. The records were locked in a standard filing cabinet, which we believe was insufficient security considering the value of the documents.

iv. Please identify the State office (or offices) cited in the report where an appraisal was stored on an unencrypted compact disk at an employee's home.
Response: We met with the employee at the Wyoming State office and were told that a disk was taken home with the employee for the purpose of safeguarding the information.

d. On page 11, the audit says that "at one State office, various personnel contribute to the specialized geologic engineering, and economic analyses that form the basis for the [Fair Market Value], but only one person computes the actual value."
  i. Please identify the State office where this one-person approach takes place.
  Response: BLM Wyoming State Office

  ii. Please provide an estimate of how many leases this "one person" practice has been used, and the total sales value of these leases.
  Response: From fiscal years 1991 through 2012, we estimate BLM used the "one employee" appraisal practice in 27 lease sales valued at $4.9 billion.

e. Mining companies and independent laboratories are allowed to determine the existence and extent of coal seams, and submit the information to the BLM before the bureau makes a tract available for lease. On page 12, the audit says "at least one State office" does not conduct field inspections of these exploration activities, which is required by BLM's Inspections and Enforcement handbook. Such due diligence is designed to ensure potential leases are not undervalued at the time of lease, and also to ensure royalty rate reductions are not improperly granted. Please identify the State offices that do not conduct such field inspections, and the time period in which such oversight has not taken place.
Response: Staff at the BLM Montana State Office said they do not inspect active exploration activities. This appears to be a long-standing practice at this Office.

f. On page 15, the audit found that out-of-date guidance contributes to inconsistent inspection and enforcement (I&E) program implementation by State offices. It also found that the BLM lacked enforcement tools, and rarely issued notices of noncompliance to mining companies.

i. Please identify the State offices that did not have sufficient documentation for I&E inspections.
Response: As stated in our report, BLM's handbook "H-3486-1-Inspection and Enforcement" is still in draft status. Accordingly, the policies and guidelines are not consistently followed by the inspection staff, and therefore, inspection and enforcement documentation was insufficient, particularly at the New Mexico State Office.

ii. Please provide information about the six instances of noncompliance that were reported between FY 2009 and FY 2011.
Response: The six instances of noncompliance were comprised of: Alabama, with one case in 2010; Kentucky, with two cases each in 2009 and 2011; and Oklahoma, with one case in 2011. BLM found that these leases did not produce commercial quantities of coal, did not pay advance royalty in lieu of continued operation, and were not officially suspended.

4.) On page 13, the audit found "that BLM may not be obtaining a fair return for lease modifications." Such tracts of coal are up to 960 acres, and are sold non-competitively to existing leaseholders, despite potentially holding tens of millions of tons of coal. Forty-five such tracts were sold since 2000, which were sold at an average 80 percent discount compared to regular leases, representing a potential loss of $60 million to the Federal Government, according to the audit. The audit went on to say that some State offices did not prepare full appraisals required by law; that more than half the modifications were appraised for the statutory minimum of $100 per acre, and that a sample of lease modifications showed inconsistent documentation, making it difficult to assess whether appraisals were properly justified.

a. Please provide the name, acreage, tonnage, sales price, date, lessee and any other pertinent information for each of the 45 lease modifications reviewed for this audit.
Response:

	Lessee	Mine	Lease Number	Date Modified	Acres Added	Price Per Acre	Size of Tract (Tons)	Sales Price
1	Mountain Coal	West Elk, CO	COC 001362	10/11/2001	160	$100.00	3,100,000	$16,000
2	Western Fuels	Deserado, CO	COC 00842401	01/05/2007	120	$100.00	1,150,000	$12,000
3	Western Fuels	Deserado, CO	COC 00842401	09/01/2007	840	$100.00	8,480,000	$84,000
4	Western Fuels	Deserado, CO	COC 00842501	02/01/2004	160	$100.00	1,600,000	$16,000
5	Western Fuels	Deserado, CO	COC 00842501	07/01/2009	400	$100.00	4,470,000	$40,000

6	Cyprus	Foidel Creek, CO	COC 020900	07/27/2007	221.86	$5,746.87	5,100,000	$1,275,000
7	N/A	NA	COC 056447	10/11/2001	149.48	$100.00	N/A	$15,000
8	Cyprus	Bowie No. 2, CO	COC 061209	01/01/2004	50	$100.00	152,000	$5,000
9	Cyprus	Bowie No. 2, CO	COC 061209	09/07/2005	83.13	$100.00	68,000	$8,400
10	Cyprus	Bowie No. 2, CO	COC 061209	10/01/2008	560	$402.11	2,780,000	$225,180
11	Oxbow Mining	Elk Creek, CO	COC 061357	02/13/2003	159.99	$100.00	766,000	$16,000
12	Oxbow Mining	Elk Creek, CO	COC 061357	05/01/2007	190.67	$860.68	2,026,000	$164,106
13	Oxbow Mining	Elk Creek, CO	COC 061357	01/01/2009	148	$317.98	581,000	$47,061
14	Oxbow Mining	Elk Creek, CO	COC 061357	05/01/2012	158.79	$100.00	235,000	$15,900
15	Colowyo Coal	Colowyo, CO	COD 0034365	09/28/2005	60	$100.00	472,000	$6,000
16	Cyprus	Bowie No. 2, CO	COD 0036955	01/28/2011	160	$250.00	400,000	$40,000
17	Mountain Coal	West Elk, CO	COD 0044569	05/18/2006	40	$356.96	171,000	$14,278
18	Cloud Peak	Decker, MT	MTM 037604	06/19/2006	49.6	$4,600.00	2,480,000	$228,160
19	Westmoreland	Rosebud, MT	MTM 080697	03/02/2004	30	$375.00	250,000	$11,250
20	Spring Creek	Spring Creek, MT	MTM 0069782	06/16/2010	498.11	$7,809.52	38,900,000	$3,890,000
21	Cloud Peak	Decker, MT	MTM 057934	06/19/2006	50.8	$4,491.34	2,480,000	$228,160
22	Westmoreland	Beulah, MT	NDM 0041765	12/02/2009	240	$100.00	N/A	$24,000
23	San Juan	San Juan UG, NM	NMNM 028093	05/12/2006	160.6	$100.00	1,250,000	$16,060
24	P&K Co.	Pollyanna #8, OK	OKNM 091190	09/27/2007	170	$100.00	600,000	$17,000
25	Hudson -Blake	Shady Point / Cavanal, OK	OKNM 091590	02/12/2008	20	$100.00	10,000	$2,000
26	Canyon Fuel	Sufco, UT	UTSL 0062583	11/23/2009	880	$4,371.97	9,600,000	$3,847,333
27	UtahAmerican Energy	Lila Canyon, UT	UTSL 0066490	06/10/2011	5	$3,700.00	50,000	$18,500
28	COP Coal Devel. Co	COP - Bear Canyon, UT	UTU 038727	06/19/2002	40	$3,125.00	500,000	$125,000
29	Canyon Fuel	Sufco, UT	UTU 047080	11/23/2009	795.68	$4,703.31	9,300,000	$3,742,333
30	COP Coal Devel. Co.	COP – Bear Canyon, UT	UTU 061049	06/19/2002	160	$6,250.00	4,000,000	$1,000,000
31	Canyon Fuel	Sufco, UT	UTU 063214	11/23/2009	640	$3,003.65	4,100,000	$1,922,333
32	Arch	Skyline, UT	UTU	04/02/2012	770	$7,168.83	13,800,000	$5,520,000

			067939					
33	Andalex Resources	Crandall, UT	UTU 068082	02/28/2005	120	N/A	900,000	N/A
34	White Oak Horizon	Horizon, UT	UTU 074804	03/10/2009	936	$1,073.08	10,800,000	$1,004,400
35	UtahAmerican Energy	West Ridge, UT	UTU 078562	04/06/2009	602	$1,627.91	2,800,000	$980,000
36	UtahAmerican Energy	West Ridge, UT	UTU 078562	06/09/2011	351	$5,270.66	5,000,000	$1,850,000
37	PacifiCorp	Deer Creek, UT	UTU 0006039	12/14/2001	65.7	$327.25	800,226	$21,500
38	Arch	Dugout, UT	UTU 0007064	03/12/2007	487.57	$943.45	2,300,000	$460,000
39	Arch	Dugout, UT	UTU 0007064	0/25/2009	367.44	$4,517.74	8,300,000	$1,660,000
40	Arch	Dugout, UT	UTU 0007064	07/21/2010	50	$490.00	70,000	$24,500
41	Bridger Coal	Bridger, WY	WYW 002727	10/05/2010	560	$682.14	5,900,000	$382,000
42	Black Butte	Black Butte, WY	WYW 006266	04/26/2002	80	$1,056.25	1,740,000	$84,500
43	Peabody	N. Rochelle, WY	WYW 071692	01/10/2003	10.19	$490.68	65,000	$5,000
44	Peabody	Rawhide, WY	WYW 083395	04/23/2008	315.18	$6,107.62	34,600,000	$1,925,000
45	Arch	Black Thunder, WY	WYW 146744	06/19/2006	40.36	$12.39	8,000	$500
Total					**12,157**		**192,154,226**	**$30,989,454**

b. How many of the 45 lease modifications reviewed by OIG sold for the minimum price of $100 per acre?
Response: BLM approved 16 lease modifications at the regulatory minimum price of $100 per acre or less.

c. In terms of acreage and tonnage, how many leases by application sold by BLM after 2005 were of lesser size than the statutory maximum allowed for lease modifications?
Response: From January 2006 through June 2012, BLM held 9 lease by application sales in which the size was less than the statutory maximum for lease modifications (960 acres). The 9 sales totaled 3,000 acres and 75 million tons of coal.

d. How many tons and acres were sold through lease modifications?
Response: BLM sold 12,157 acres and 192,154,226 tons of coal through lease modifications from 2001 through 2012.

e. Please identify the States that did not prepare FMV appraisals for modifications.
Response: The BLM Colorado, Utah, and Wyoming State Offices did not prepare full FMV appraisals as required by 43 CFR §3432. Specifically, BLM used the

regulatory minimum bonus bid of $100 for 16 modifications since 2000. We reviewed six of these modifications and concluded that BLM's appraisal was inadequate to justify the minimum price.

f. Please identify the 11 modifications and 4 states that were sampled.
Response:

	Mine	Lease Number	Date Modified	Lease Mod. Acres Added	Price per Acre	Size of Mod. (Tons)	Total Bonus
1	Deserado, CO	COC 00842401	01/05/2007	120	$100.00	1,150,000	$12,000
2	Deserado, CO	COC 00842401	09/01/2007	840	$100.00	8,480,000	$84,000
3	Deserado, CO	COC 00842501	02/01/2004	160	$100.00	1,600,000	$16,000
4	Deserado, CO	COC 00842501	07/01/2009	400	$100.00	4,470,000	$40,000
5	Bowie No. 2, CO	COC 061209	01/01/2004	50	$100.00	152,000	$5,000
6	Bowie No. 2, CO	COC 061209	09/07/2005	83	$100.00	68,000	$8,400
7	Bowie No. 2, CO	COC 061209	10/01/2008	560	$402.11	2,780,000	$225,180
8	Spring Creek, MT	MTM 0069782	06/16/2010	498	$7,809.52	38,900,000	$3,890,000
9	Dugout, UT	UTU 0007064	03/12/2007	488	$943.45	2,300,000	$460,000
10	Bridger, WY	WYW 002727	10/05/2010	560	$682.14	5,900,000	$382,000
11	Rawhide, WY	WYW 083395	04/23/2008	315	$6,107.62	34,600,000	$1,925,000
Total				**4,074**		**100,400,000**	**$7,047,580**

g. Which of the modifications identified in 4(f) were adjacent to operating mines?
Response: All modifications were adjacent to operating mines.

5.) On page 12, the audit discusses the Utah State Office's use of external consultants in instances where there are insufficient employees to process leases. The audit recognizes that such arrangements may "prove useful." It also raises concerns about conflicts of interest and the need for safeguarding confidential information.

a. Please identify external consultants that the Utah State Office, or other BLM State offices, have used to process coal lease sales, and the functions they performed.
Response: We found that BLM used the services of an external consultant in one coal lease sale. Specifically, the BLM Utah State Office contracted with NorWest

Corporation to help determine the FMV for a lease sale held in 2012.

b. Please provide the estimated cost of hiring the identified consultants.
Response: The contract with NorWest Corporation was for $63,200.

c. Have these external consultants provided consulting or other services to individuals or companies who bid on coal leases sold by the Department of Interior?
Response: We are not aware if the consultant has performed work for companies who bid on coal leases on Department of the Interior lands.

d. What safeguards are currently in place to ensure that external consultants do not use information gathered about coal leases to benefit themselves or (current, previous, and future) clients who could potentially bid on leases?
Response: BLM concurred with our recommendation to strengthen its internal controls over the FMV records, which would include the use of external consultants. In the case of the external consultant recently hired by the BLM Utah State Office, the consultant did not sign a nondisclosure agreement. The contract between BLM and the consultant, however, required the consultant to keep confidential all assessments, findings, conclusions, and recommendations.

At an appropriate future date, OIG will conduct a verification review to assess whether BLM improved its internal controls.

If you have any further questions, please do not hesitate to contact me at 202-208-5745, or your staff may call Kris Kolesnik, Associate Inspector General for External Affairs at 202-513-0326.

Sincerely,

Mary L. Kendall
Deputy Inspector General