



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

# **CIVIL PENALTY SHARING PROVISIONS OF 30 U.S.C. § 1736 FOR FEDERAL OIL AND GAS**




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

**MAY 01 2012**

Memorandum

To: Rhea S. Suh  
Assistant Secretary, Policy, Management and Budget

From: Mary L. Kendall   
Acting Inspector General

Subject: Management Advisory – Civil Penalty Sharing Provisions of 30 U.S.C. § 1736  
for Federal Oil and Gas Leases  
Report No.: CR-MA-ONRR-0003-2012

In November 2011, the Office of Natural Resources Revenue (ONRR) requested a meeting with the Office of Inspector General to discuss how to comply with the civil penalty sharing provision of 30 U.S.C. § 1736. This provision applies to ONRR's agreements to have States and Tribes conduct royalty audits of Federal and Indian oil and gas lessees<sup>1</sup> within their jurisdictions. It calls for ONRR to provide States and Tribes 50 percent of any civil penalties that result from this audit work and to reduce by a corresponding amount the funding that ONRR gives the States or Tribes to conduct the royalty audits.

Despite this requirement, State and Tribal audit organizations have asked ONRR not to share the penalty money with their respective State or Tribe because of their concerns that doing so would result in the elimination of the funding for their audit work. ONRR now owes State and Tribal governments a total of \$441,000 in penalties (dating back to May 2006).

ONRR is taking steps to implement §1736, but, like the State and Tribal audit organizations, it is concerned that the penalty sharing requirement could lead to a loss of funding for those audit programs—a problematic outcome, since these royalty audits play a key role in identifying the violations that result in civil penalties.

We support ONRR's efforts to comply with §1736 and understand its concerns about the impact a reduction in obligated funds could have on State and Tribal audit programs. We make several recommendations to the Department to help ONRR address these concerns while correctly and effectively implementing the penalty sharing requirement of §1736.

## Background

The Federal Oil and Gas Royalty Management Act of 1982, for Federal and Indian oil and gas leases, and 30 U.S.C. § 196 authorize the Department to allow States and Tribes to carry out various types of regulatory activities, including audits, inspections, and investigations, within

<sup>1</sup> In 1991, Congress also authorized the Secretary to delegate audit, investigation, and inspection authority to States for solid mineral, geothermal, and Section 8(g) leases. Pub. L. 102-154, 105 Stat. 1001 (1991) (codified at 30 U.S.C. § 196).

their jurisdictions. The Department authorizes and fully funds this audit work by entering into cooperative agreements with Tribes or by delegating audit authority to States.

Under §1736, the Department must pay the States or Tribes 50 percent of any civil penalties collected as a result of their audit work under cooperative or delegation agreements. The statute also states that the Department must subtract the penalty money it owes a State or Tribe from the amount it has obligated to fund this audit work. For example, if a State has an agreement with ONRR that calls for ONRR to pay the State \$1 million for the State's work auditing Federal lessees, and the resulting work by the State causes ONRR to pay it \$500,000 in civil penalties under §1736, then ONRR would also subtract \$500,000 from the \$1 million agreement. This would result in the State receiving only half of the direct funding originally agreed to. Civil penalty sharing could conceivably result in an audit agreement's direct funding being reduced to zero as penalties are shared with the State or Tribe.

Although ONRR understands that it must begin to comply with §1736, ONRR and the affected State and Tribal audit agencies are concerned that the requirement to reduce funding will mean the audit work ONRR contracts for will not be fully funded. Specifically, their concern is that State and Tribal governments may divert the civil penalty money they collect through this provision to meet other needs rather than use the money to fund the ONRR-delegated audit programs. ONRR is currently considering how best to implement §1736.

### **ONRR's Current Actions and Remaining Issues**

ONRR told us it agrees that §1736 requires civil penalty sharing and that the audits conducted by States and Tribes under agreements and delegations qualify them to share any resulting civil penalties. ONRR has also taken the following actions to begin to address penalty sharing and its potential impacts:

- ONRR has researched civil penalty actions resulting from State and Tribal audits dating back to fiscal year 2000 and identified 21 cases with total civil penalties of \$1.354 million, of which the potential sharing liability would be \$677,000.
- ONRR believes there is a 6-year statute of limitations related to §1736, and has applied this limitation back to 2006 and concluded the potential sharing liability to be \$441,000.
- ONRR has identified six ongoing civil penalty cases that would require payment to be made to the respective State or Tribal government. These cases have potential civil penalties totaling \$6.84 million; resulting in a potential sharing liability of \$3.42 million.

As we have noted, civil penalty sharing may result in an audit agreement's direct funding being reduced substantially as ONRR shares penalties with a State or Tribe. In its fiscal year 2013 budget justification, the Department proposes language that would eliminate this requirement. The proposal would instead reduce the civil penalties that ONRR must share by the amount of the applicable cooperative agreement. The proposed language reads in full:

SEC. 119. Section 206 of the Federal Oil and Gas Royalty Management Act of 1982, Public Law 97-451 (30 U.S.C. 1736), as amended, is hereby amended by striking the second sentence and inserting in lieu thereof: “Any payments under this section shall be reduced by an amount equal to any payments provided or due to such State or Indian Tribe under the cooperative agreement or delegation, as applicable, during the fiscal year in which the State or Tribe receives the civil penalty, up to the total amount provided or due for that fiscal year.”

ONRR is also consulting with States and Tribes on this matter; however, ONRR officials informed us that the matter has become more urgent as a result of ONRR’s increased emphasis on royalty enforcement activities and pending large civil penalty actions. They also told us that concern over this issue has had a chilling effect on the collaborative working relationships between the States’ and Tribes’ audit teams and ONRR’s Office of Enforcement, leading to a noticeable decrease in enforcement referrals.

## **Recommendations**

We recommend the Department—

1. Support ONRR and work with Congress to address the concerns ONRR has over the impact of §1736 in order to find a permanent solution to this issue through legislative amendment.
2. Work with States, Tribes, and the Office of the Solicitor to comply with the civil penalty sharing requirements of §1736 without jeopardizing audit agreements.
3. Request a Solicitor’s opinion on legal issues related to the application of statutes of limitations related to civil penalty sharing requirements and any other legal issues that arise regarding the sharing of penalties with the States and Tribes.

## **Conclusion**

ONRR has avoided implementation of the civil penalty sharing requirements of §1736 because of the negative impact it could have on State and Tribal audit agreements. This issue has, however, gained in significance and potential monetary impact with the increased emphasis on ONRR’s royalty enforcement activities and pending large civil penalty actions. Therefore, the Department must act promptly to find a permanent solution to this problem.

Please provide a written response to this management advisory within 30 days of receipt. The response should detail the Department’s action plan for implementing our recommendations, as well as targeted completion dates and title(s) of officials responsible for implementation. We will include information contained in this management advisory in our Semiannual Report to Congress. If you have any questions, please contact me at 202-208-5745.

cc: Chief of Staff, U.S. Department of the Interior  
Deputy Secretary, U.S. Department of the Interior  
Acting Deputy Assistant Secretary, Natural Resources Revenue  
Deputy Assistant Secretary for Budget, Finance, Performance, and Acquisitions  
Director, Office of Natural Resources Revenue

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