



DOI's Repeal of Obama Administration Valuation Reforms May Signal More Change for Coal, Oil & Gas Industries

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On August 4, 2017, the Department of the Interior ("DOI") announced that it was repealing a 2016 final rule ("2017 Valuation Rule") that sought to reform the Federal government's approach to oil, gas, and coal royalty valuation and reporting and that had gone into effect on January 1, 2017. The 2017 Valuation Rule sought to close what some considered a loophole that allowed coal companies to sell coal at artificially low prices to affiliated entities (with reduced royalty payments to the federal government), by instead requiring coal and gas to be valued based on the first arm's-length disposition. To justify the repeal, DOI stated that after the 2017 Valuation Rule had been published, the Office of Natural Resources Revenue ("ONRR") "discovered several significant defects in the rule that would have undermined its purpose and intent" and received "numerous comments" that were highly critical of parts of the rule. The repeal reinstates the regulations that had been in effect prior to the effective date of the 2017 Valuation Rule.

This Alert summarizes the Trump Administration's justifications for its Repeal of Consolidated Federal Oil & Gas Federal & Indian Coal Valuation Reform ("Repeal"), analyzes the status of pending litigation challenging the 2017 Valuation Rule, and explores potential future reforms on oil, gas, and coal valuation and reporting.

The Administration's Stated Reasons for the Repeal

In the Preamble to the Repeal, ONRR states that there are three reasons why it is repealing the 2016 Rule in its entirety. First, according to ONRR, the 2017 Valuation Rule had "a number of defects that make certain provisions challenging to comply with, implement, or enforce." These defects, according to ONRR, would, among other things, "compromise ONRR's mission to collect and account for" royalty revenues and "impose a costly and unnecessary burden on Federal and Indian lessees."

Second, ONRR concluded that certain provisions in the 2017 Valuation Rule would "unnecessarily burden the development of Federal oil and gas and Federal and Indian coal beyond the degree necessary to project the public interest or otherwise comply with the law," and therefore were inconsistent with Executive Order 13783 – Promoting Energy Industry and Growth, issued by the President in March 2017.

Third, ONRR stated that on March 29, 2017, Secretary Zinke announced that he was reestablishing the Royalty Policy Committee ("RPC") under the Federal Advisory Committee Act. The RPC will advise ONRR on issues related to fair market value and collections of royalties from energy and natural resources on Federal and Indian lands. ONRR expects that further internal assessment and analysis, with input from the RPC, will lead to the development and issuance of a new, revised valuation rule.

Impact on Royalties

In the Preamble, ONRR estimates that the repeal will result in an estimated annual decrease in royalty collections of between \$60.1 million and \$74.8 million. ONRR projects that these decreased royalties will result in a \$67.4 million benefit to industry. ONRR also concluded that states and local governments that receive royalties will "incur a decrease in royalty receipts."

Related Litigation

In December 2016, after the 2017 Valuation Rule was promulgated but before it took effect, several coal, oil and gas industry associations, and individual companies challenged the rule in three separate lawsuits in the U.S. District Court for the District of Wyoming. The plaintiffs argued that the rule had a number of

fundamental flaws, including on valuation procedures and cost deductions, and would be unreliable and difficult to implement.

In February 2017, citing this litigation, ONRR suspended implementation of the 2017 Valuation Rule. Subsequently, the states of California and New Mexico filed a lawsuit in the U.S. District Court for the Northern District of California seeking a declaratory judgment that ONRR unlawfully postponed the effective date of a rule that had already gone into effect and requesting reinstatement of the 2017 Valuation Rule.

The Repeal likely renders moot the December 2016 challenges to the 2017 Valuation Rule. It is likely, however, that California and New Mexico will continue their efforts to ask the court to invalidate the Administration's actions to undo the 2017 Valuation Rule.

Further Royalty Rate Reforms to Come?

The reestablishment of the RPC under the Federal Advisory Committee Act to advise ONRR on royalty-related issues signals that further reform is likely coming to the Federal government's approach to royalty valuation and reporting. According to the Preamble to the Repeal, the RPC will provide a forum for engaging with key stakeholders and the public on many of the same issues that were covered by the 2017 Valuation Rule.

Early in the summer, the Bureau of Ocean Energy Management ("BOEM") also signaled future royalty reforms in announcing a royalty rate reduction in Lease Sale 249. In that announcement, BOEM stated that "we are analyzing a price-based royalty system and will be engaging stakeholders on this concept later this year." The announcement further explained that "BOEM's concept of a price-based royalty system would provide an incentive to lessees through lower royalty rates in times of lower oil prices, while also ensuring the Federal government receives a greater return for Outer Continental Shelf resources when prices are high."

For more information

With litigation continuing and additional reforms likely to come, a number of legal and policy decisions related to royalty valuation and reporting will be in play. Van Ness Feldman's team of regulatory and administrative law experts is available to provide counsel to companies and others as they assess potential legal strategies. For further information and analysis, please contact [Michael Farber](#), [Jonathan Simon](#), or [R. Scott Nuzum](#) at 202-298-1800.

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