PART TWO: INTERIOR DEPARTMENT: A CULTURE OF MANAGEMENT IRRESPONSIBILITY AND LACK OF ACCOUNTABILITY?

HEARING

BEFORE THE

COMMITTEE ON GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED NINTH CONGRESS

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CONTENTS

	Page
Hearing held on September 14, 2006	1
Statement of:	
Scarlett, P. Lynn, Deputy Secretary, U.S. Department of the Interior, accompanied by Johnnie Burton, Director, Minerals Materials Management Service, U.S. Department of the Interior	43
Letters, statements, etc., submitted for the record by:	
Cummings, Hon. Elijah E., a Representative in Congress from the State of Maryland, prepared statement of	37
Davis, Chairman Tom, a Representative in Congress from the State of Virginia:	
Prepared statement of	3
Prepared statement of POGO	10
Issa, Hon. Darrell E., a Representative in Congress from the State of California, prepared statement of	33
Maloney, Hon. Carolyn B., a Representative in Congress from the State of New York, prepared statement of	18
Markey, Hon. Edward J., a Representative in Congress from the State of Massachusetts, prepared statement of	41
Scarlett, P. Lynn, Deputy Secretary, U.S. Department of the Interior, prepared statement of	47
Waxman, Hon. Henry A., a Representative in Congress from the State of California, prepared statement of	7

PART TWO: INTERIOR DEPARTMENT: A CULTURE OF MANAGEMENT IRRESPONSIBILITY AND LACK OF ACCOUNTABILITY?

THURSDAY, SEPTEMBER 14, 2006,

HOUSE OF REPRESENTATIVES,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The committee met, pursuant to notice, at 10:30 a.m. in room 2154, Rayburn House Office Building, Hon. Tom Davis (chairman of the committee) presiding.

Present: Representatives Tom Davis, Waxman, Cummings, Davis of Illinois, Duncan, Gutknecht, Bilbray, Mica, Issa, Kucinich, Maloney, Norton, and Watson.

Also present: Representative Markey.

Staff present: David Marin, staff director; Larry Halloran, deputy staff director; Keith Ausbrook, chief counsel; Anne Marie Turner and Thomas Alexander, counsels; Michael Galindo and Benjamin Chance, clerks; Leneal Scott, computer systems manager; Larry Brady, subcommittee staff director; Phil Barnett, minority staff director/chief counsel; Karen Lightfoot, minority communications director/senior policy advisor; Alexandra Teitz, minority counsel; Shaun Garrison, minority professional staff member; Earley Green, minority chief clerk; and Jean Gosa, minority assistant clerk.

Chairman TOM DAVIS. Good morning.

Yesterday, our Subcommittee on Energy and Resources held its fourth hearing on natural gas royalties for the Federal offshore leases. Inspector General Earl Devaney discussed why price thresholds were omitted from deepwater leases in 1998 and 1999. Mr. Devaney also cited numerous times during his 7-year tenure at the Department of examples of waste, fraud and abuses uncovered by the Office of the Inspector General and subsequently ignored by the Department.

During Mr. Devaney's testimony, we learned of the massive departmental confusion surrounding the deepwater leases in 1998 and 1999. Not only were price thresholds omitted from deepwater leases during those 2 years, those within the Department of Interior aren't even clear on when the omission was discovered. E-mails from 2000 show that upon the discovery, a decision was made at the Associate Director level of the Minerals Management Service to keep silent the omission, a silence that lasted for another 5 years.

Despite the lack of managerial oversight, Devaney testified that no one within the Department of the Interior has been fired, suspended or reprimanded as a result of the multi-billion dollar cover-

up. Unfortunately, as the Inspector General found, the deepwater lease issue is not an exception at the Department of the Interior. The OIG has issued countless reports citing cases of ethics failures and ineffective management and policies within the Department.

These failings permeate employee morale, as the Inspector General's office found in 2004 that 46 percent of employees within the Department believe that discipline was administered fairly only sometimes, if ever. There are reasons to look on the bright side. In May, Dirk Kempthorne took the reins. In the 4 shorts months of his tenure, Secretary Kempthorne has already shown signs that the status quo at Interior is unacceptable. Mr. Devaney testified that he met with Secretary Kempthorne on the Secretary's first day regarding the OIG's work.

Additionally, the Secretary sent a memorandum to all Interior employees instructing them to cooperate with the Office of the Inspector General.

Will changes be implemented? It is too soon to tell. I don't know. If the culture of waste, fraud and abuse continues in the Department of Interior, it will never be able to wrap its arms around the problems of deepwater leases. But I also know that for changes to occur, they have to start from the top down.

I have a personal connection with the Department of the Interior. After serving as the Attorney General of Nebraska, my grandfather moved to DC to become Solicitor for the Interior Department. He subsequently went on to serve as the Department's Under Secretary and Acting Secretary. It is my grandfather's career at Interior that caused my family to move from Nebraska to northern Virginia. This move ultimately resulted in my career in the House of Representatives.

It is with deep disappointment that I hold this hearing today, given my fond memories of the Department of the Interior and the hard work of those in decades past. I know they would also be disillusioned by the culture of waste, fraud and abuse at the Department and would echo my call for immediate reforms.

I would now recognize our distinguished ranking member, Mr. Waxman, for his opening statement.

[The prepared statement of Chairman Tom Davis follows:]

Statement for Chairman Tom Davis
Committee on Government Reform
"Interior Department: A Culture of Managerial Irresponsibility and Lack of Accountability? Part 2"
September 14, 2006

Good morning and welcome to the Committee on Government Reform's hearing on the U.S. Department of the Interior. Yesterday, our Subcommittee on Energy and Resources held its fourth hearing on natural gas royalties from federal offshore leases. Inspector General Earl Devaney discussed why price thresholds were omitted from deep water leases in 1998 and 1999. Mr. Devaney also cited numerous times during his seven year tenure at the Department that examples of waste, fraud, and abuse were uncovered by OIG and subsequently ignored by the Department.

During Mr. Devaney's testimony we learned of the massive departmental confusion surrounding the deep water leases in 1998 and 1999. Not only were price thresholds omitted from deep water leases during the two years, those within the Department of the Interior aren't even clear on when the omission was discovered. E-mails from 2000 show that upon the discovery, a decision was made at the Associate Director level of the Minerals Management Service to keep silent the omission -- a silence that lasted for another five years. Despite this lack of managerial oversight, Devaney testified that no one within the Department of the Interior has been fired, suspended, or reprimanded as a result of this multi-billion dollar cover-up.

Unfortunately, as the Inspector General has found, the deep water lease issue is not an exception at the Department of the Interior. The OIG has issued countless reports citing cases of ethics failures and a history of ineffective management and policies within the Department. These failings permeate employee morale, as the Inspector General's Office found in 2004 that forty-six percent of employees within the Department believed that "discipline was administered fairly only 'sometimes,' if ever."

There are reasons to look on the bright side at the Department of the Interior. In May, Dirk Kempthorne took the reins. In the four short months of his tenure, Secretary Kempthorne has already shown signs that the status quo at Interior is unacceptable. Mr. Devaney testified that he met with Secretary Kempthorne on the Secretary's first day regarding the OIG's work. Additionally, the Secretary sent a memorandum to all Interior employees instructing them to cooperate with the OIG. Will changes be implemented? It is too soon to tell. I do know that if the culture of waste, fraud, and abuse continues, the Department of the Interior will never be able to wrap its arms around the problems of deep water leases. I also know that for changes to occur, they must start from the top, down.

I have a personal connection to the Department of the Interior. After serving as the Attorney General of Nebraska, my grandfather moved to D.C. to become the Solicitor for the Interior Department. He subsequently went on to serve the Department as Under Secretary and Acting Secretary. It was my grandfather's career at Interior that caused my

family to move to Northern Virginia. This move ultimately resulted in my career in the House of Representatives. It is with deep disappointment that I hold this hearing today, given my fond memories of the Department of the Interior and the hard work of those in decades past. I know they would also be disillusioned by the culture of waste, fraud, and abuse at the Department and would echo my call for immediate reforms.

Mr. WAXMAN. Thank you very much, Mr. Chairman.

Today, the committee has the opportunity to investigate several important problems at the Department of Interior. This shouldn't be the last of the series of hearings on what went wrong in 1998 and 1999 for leases. It should be the first in a series of hearings on how the Department of Interior is broken and how we can fix it.

The majority has held four previous hearings investigating who was responsible for the omission of price thresholds for royalty relief in oil and gas drilling leases signed in 1998 and 1999. I think we all recognize this was a huge and unacceptable mistake. Already the House has taken action to correct this costly mistake. Earlier this year, the House passed legislation barring the award of leases to any company that refuses to renegotiate its leases to include price thresholds for royalty relief. That is a powerful incentive for companies to come to the table.

The Senate has included similar language in committee. While these provisions were sponsored by Democrats, every Member should insist that they be retained in the final Interior appropriations bill.

Unfortunately, the 1998 and 1999 leases are only a small part of what is wrong at the Department. What we really need to focus on are the broader problems within Minerals Management Service and the Department of Interior as a whole that allowed this mistake and many, many others to happen. The Inspector General testified yesterday that the underlying problems still haven't been corrected. That is an invitation for future failures and losses.

Since the late 1990's, 12 major oil companies have paid over $400 million to settle lawsuits brought by private parties alleging the companies had systematically cheated the Government on royalties. Why were all these claims left to private parties to initiate? Where was MMS? A Colorado oil executive currently has 73 lawsuits pending against more than 300 energy companies. He is accusing them of cheating the Government out of roughly $30 billion in royalties. If they have merit, MMS should be pursuing these claims.

And the problem isn't just that MMS is failing to act. MMS may actually be collaborating with the oil industry to discourage MMS's own auditors from recovering money owed to the Government. A former senior MMS auditor sued Kerr-McGee for $12 million in unpaid royalties after MMS refused to pursue the claim. MMS fired that auditor a few weeks later.

Another senior auditor fired by MMS alleges that under the Bush administration, agency managers pressured him not to collect on unpaid royalties when oil and gas companies complained. State and tribal auditors are protesting MMS pressure on them to scale back their auditing efforts in favor of more superficial compliance reviews which won't reveal deliberate cheating. This looks like an agency that has been captured by the industry it is supposed to oversee, with the American taxpayers footing the bill.

I have been disappointed by the refusal thus far to hear from witnesses on these allegations. I hope that Chairman Davis and Chairman Issa will reconsider and investigate these issues. The Interior IG's explosive testimony yesterday highlights even greater

problems at the very highest levels of the Interior Department. Inspector General Devaney stated that "ethics failures on the part of senior Department officials, taking the form of appearances of impropriety, favortism and bias, have been routinely dismissed with the promise not to do it again." And he described how the former Secretary of Interior refused to hold high-level officials accountable for their misdeeds.

This committee has the responsibility to investigate Government misconduct. We should not ignore what Inspector General Devaney said yesterday. There are serious problems at the top of the Department of Interior, and we have an obligation to investigate these matters and hold officials accountable for ethical lapses.

In closing, I want to thank the chairman for holding today's hearing and request unanimous consent to insert into the record testimony from the Project on Government Oversight, which details some of the issues I have raised today.

[The prepared statement of Hon. Henry A. Waxman follows:]

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INDEPENDENT

Opening Statement of
Rep. Henry A. Waxman, Ranking Minority Member
Committee on Government Reform
Hearing on Royalties Issues and
Management Problems at the Department of Interior

September 14, 2006

Today, the Committee has the opportunity to investigate several important problems at the Department of Interior. This shouldn't be the last in a series of hearings on what went wrong in 1998 and 1999 Gulf oil leases – it should be the first in a series of hearings on how the Department of Interior is broken and how we can fix it.

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Already, the House has taken action to correct this costly mistake. Earlier this year, the House passed legislation barring the award of new leases to any company that refuses to renegotiate its leases to include price thresholds for royalty relief. That's a powerful incentive for companies to come to the table. The Senate has included similar language in committee. While these provisions were sponsored by Democrats, every member should insist that they be retained in the final Interior Appropriations bill.

Unfortunately, the 1998 and 1999 leases are only a small part of what's wrong at the Department. What we really need to focus on are the broader problems within Minerals Management Service, and the Department of Interior as a whole, that allowed this mistake, and many, many others, to happen. The Inspector General testified yesterday that the underlying problems still haven't been corrected. That's an invitation for future failures and losses.

Since the late 1990s, 12 major oil companies have paid over $400 million to settle lawsuits brought by private parties alleging the companies had systematically cheated the government on royalties. Why were all these claims left to private parties to initiate? Where was MMS?

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A Colorado oil executive currently has 73 lawsuits pending against more than 300 energy companies. He is accusing them of cheating the government out of roughly $30 billion in royalties. If they have merit, MMS should be pursuing these claims.

And the problem isn't just that MMS is failing to act. MMS may actually be collaborating with the oil industry to discourage MMS's own auditors from recovering money owed to the government.

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State and tribal auditors are protesting MMS pressure on them to scale back their auditing efforts in favor of more superficial "compliance reviews," which won't reveal deliberate cheating.

This looks like an agency that has been captured by the industry it is supposed to oversee, with the American taxpayers footing the bill. I've been disappointed by the majority's refusal thus far to hear from witnesses on these allegations. I hope that Chairman Davis and Chairman Issa will reconsider and investigate these issues.

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In closing, I thank the Chairman for holding today's hearing and request unanimous consent to insert into the record testimony from the Project on Government Oversight, which details some of the issues I have raised today.

Chairman TOM DAVIS. We will include the POGO's comments in the record.

[The information referred to follows:]

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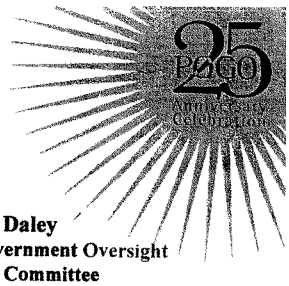

Written Testimony of Beth Daley
Director of Investigations, Project On Government Oversight
to the House Government Reform Committee

Interior Department: A Culture of Managerial Irresponsibility and Lack of Accountability?
September 14, 2006

The Project On Government Oversight (POGO) applauds the efforts of House Government Reform Chairman Tom Davis and House Energy and Resources Subcommittee Chairman Darrell Issa to take a much-needed look at the Department of Interior's oil and gas leasing and royalty collections. In addition, we applaud the efforts of Ranking Member Henry Waxman and Committee member Representative Carolyn Maloney who have conducted investigations and led many initiatives over the years to ensure that the oil and gas industry pay their fair share for royalties on federal and Native American leases.

We sincerely hope that yesterday's and today's hearings are the beginning of more Congressional oversight to come, particularly given the history of these issues and indicators today that point to the need for much more vigorous efforts to protect Native Americans and the taxpayers from waste, fraud, abuse.

Founded in 1981, POGO is a nonpartisan and independent nonprofit organization that investigates and exposes corruption and other misconduct in order to achieve a more accountable federal government. POGO is committed to honest, accountable, and open government.

Department of Interior (DOI) Inspector General Earl Devaney's testimony yesterday outlined in part how an "institutional culture of managerial irresponsibility and lack of accountability" – as the Subcommittee put it – allowed a complacent Minerals Management Service (MMS) to fail to collect royalties owed to the taxpayer. In POGO's experience spanning more than a decade of investigating in this topic area, aggressive Congressional and watchdog oversight has played a central role in ensuring that the MMS adequately protects the financial interests of the federal government and Native Americans.

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The Oil and Gas Industry: a History of Fraud

In the 1990's, POGO issued a series of investigative reports documenting how the oil industry had shortchanged the government by as much as several billion dollars in oil royalties. Some of that money was ultimately recovered as a result of a False Claims Act lawsuit filed by POGO and whistleblowers as well as by audits conducted by MMS. In 1998 to 2001, companies reached settlements totaling roughly $500 million with the Justice Department in lawsuits alleging that they shortchanged on oil and gas royalties owed to tribes and the federal government.[1]

In 2002, POGO identified more than $11 billion in lawsuit settlements that the oil and gas industry had reached with states, tribes, the federal government, and private parties concerning royalty underpayments.[2] Dozens of cases involving gas and oil royalty underpayments illustrate that a variety of players in the oil and gas industry may be engaged in widespread oil and gas royalty fraud.

Auditing and Enforcement: How is MMS Doing?

Since 1981, the Minerals Management Service has operated an auditing and compliance division which conducts audits and oversight of mineral leases. Collections from the auditing and compliance division of MMS have declined in recent years. In the four years from 2002 to 2005, MMS's auditing and compliance program collected an average $48 million annually, less than half the average $115 million collected annually in the division's first 20 years.[3]
The decline in funds collected has occurred on the heels of changes in the way the MMS compliance programs provide accountability and oversight over royalty collections. Since 2000, MMS has altered its priorities, shifting resources away from auditing to a computerized checking system based upon information provided from the industry, known as "compliance review." In FY 2000, $22 million was spent on auditing and $12 million was spent on compliance review. By comparison, in FY 2005, the priorities were reversed: just $12 million was spent on auditing while $22 million was being spent on compliance review.[4]

The most recent budget from MMS indicates that since 2001 it has reduced its auditing and compliance

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[1] "Unocal to Pay U.S. More Than $21 Million for Underpayment of Oil Royalties," Justice Department Press Release, December 3, 2001 , and Shell Oil to Pay United States $56 million for Underpayment of Gas Royalties, September 28, 2000. http://www.usdoj.gov/opa/pr/2001/December/01_civ_624.htm & http://www.usdoj.gov/opa/pr/2000/September/571civ.htm

[2] Federal Natural Gas Royalty Underpayment Litigation, Project On Government Oversight, January, 2002. http://pogo.org/p/environment/ea-020101-gas.html

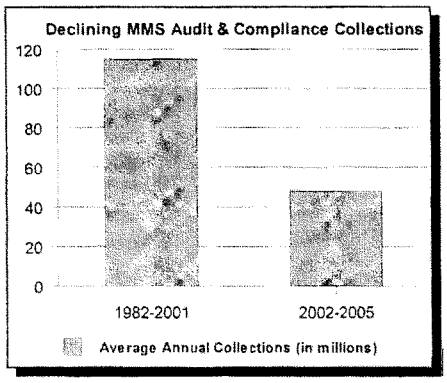
[3] In deriving this figure, POGO analyzed auditing and compliance revenue collections from FY 2002 through FY 2005 then compared that to collections for the twenty-year period from FY 1982 to FY 2001. Auditing and compliance revenue collections from FY 1998 to FY 2001 were larger due to collections made in part as a result of POGO's investigations, outside litigation, and effective audits performed by MMS.

[4] Letter to Representative Carolyn Maloney from MMS Director Johnnie Burton, May 17, 2006.

staff by 65 full-time employees, or 26% of its then-total staff of 250.[5] While POGO supports efforts to make the government more efficient, cut back in the number of auditors at this particular juncture is hard to justify given the evidence of underpayments which surfaced in the late 1990s.

MMS argues that the growing use of Royalty-in-Kind has minimized royalty uncertainty and resulted in the need for fewer audits. This may or may not be true. An independent analysis of this issue would ensure that MMS' assumptions on this point are correct.

In addition, as will be discussed later, a variety of whistleblowers have raised substantial questions about whether the Interior Department is meeting its full potential in overseeing royalty collections.



In response to questions about how many random and referal audits are conducted, MMS replied in a letter to Representative Carolyn Maloney (D-NY): "While we remain committed to the strategies, MMS has not yet made full use of random audits and referrals as means to improve our compliance process. As we continue to adapt and refine our processes, we expect to make greater use of these approaches in the future."[6]

MMS added: "During FY 2002, MMS initiated 13 such random audits – 1 Indian, 9 offshore, and 3 onshore. The MMS has 49 more such random audits underway or planned for FY 2006-2007, including 1 Indian, 15 onshore, and 33 offshore...Additional random audits are performed periodically as resources are available. For example in FY 2003, 15 Federal onshore properties were selected for audit randomly from those states without delegated compliance and audit authority."[7] One unresolved question is whether this minimal amount of audit activity has a deterrent effect against possible fraud for the 27,000 producing federal and Indian mineral leases under MMS' jurisdiction.

Since 2000, the MMS has not published on its web site its annual "Report on Royalty Management and Delinquent Account Collection Activities," which had previously outlined the agency's activities to audit,

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[5] Budget Justifications and Performance Information Fiscal Year 2007, U.S. Department of Interior Minerals Management Service. http://www.mms.gov/PDFs/2007Budget/FY2007BudgetJustification.pdf

[6] Letter to Representative Carolyn Maloney from MMS Director Johnnie Burton, May 17, 2006.

[7] Ibid.

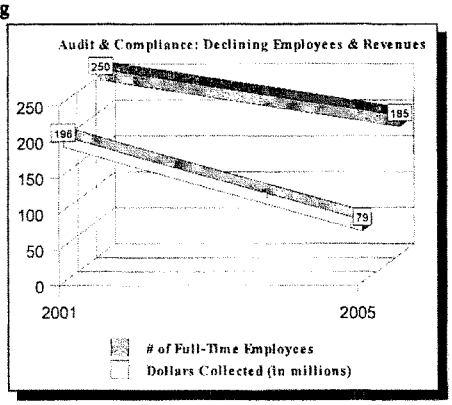
monitor, and enforce collection of royalties for products taken from federal and Indian lands. Congress should consider requesting that the MMS revive the annual web publication of this document so that appropriate oversight can be conducted.

Congress should also examine incentives which are being used in the auditing and compliance division of MMS. Are MMS' employees rewarded for actually finding underpayments? Or are they rewarded for fulfilling meaningless quotas? Preliminary information received by POGO suggests that the bonus systems could be altered to be more closely aligned to outcomes that benefit the taxpayer. Bonuses for MMS increased in 2005 with 15 Senior Executives receiving $77,000 or an average of $5,000 each.

Whistleblowers, States, Tribes Raise Concerns: Is Anyone Listening?

A variety of industry and government whistleblowers, states, and tribes have come forward to express concerns about oil and gas royalty underpayments and the MMS' commitment to exposing and correcting those underpayments. In recent years, two senior Interior Department auditors were fired after they sought to improve royalty collections. Retaliation against whistleblowers may be part of a wider cultural problem within the agency of silencing voices who would seek to strengthen the agency's ability to fairly collect what is owed from the oil and gas industry.

In September 2004, Bobby Maxwell, a senior auditor in MMS' Offshore Auditing and Compliance, filed a False Claims Act lawsuit alleging that Kerr-McGee underreported the value of the oil it had drilled from federal lands from 1999-2003. That lawsuit has now passed all its legal hurdles and is poised to go to trial in federal court in November, 2006. POGO applauds the efforts of Mr. Maxwell, an auditor with MMS since 1983 who had received numerous awards for his federal service. Mr. Maxwell was fired by the MMS just a few weeks after his False Claims Act lawsuit was unsealed and made public. Mr. Maxwell's case suggests that MMS may not be issuing demands to pay to oil and gas companies in cases where there are substantial audit findings. In correspondence to Congress, MMS has indicated that despite its maintenance of data on audits and compliance reviews, it "does not maintain statistics on the numbers or amounts of orders [referring to orders to pay issued to companies] issued.[8]



[8] Ibid.

Finally, attention should be paid to the firing of whistleblower Kevin Gambrell, the former director of the Federal Indian Minerals Office in Farmington, New Mexico from 1996 to 2003. Mr. Gambrell was a talented and successful auditor within MMS until he was pushed out for raising concerns about whether MMS was fulfilling its duty to collect royalties for Indians. While in his position, Mr. Gambrell was able to renegotiate settlements between MMS and the oil industry so that Navajos would receive eight times more than MMS had determined was owed. According to Mr. Gambrell, MMS had not relied on audits to determine what the oil industry owed the Navajos. In February 2003, Mr. Gambrell began disclosing his concerns to the Court-appointed Special Master overseeing the Indian Trust Fund. In September 2003, MMS fired Mr. Gambrell.

In a June 2006 segment on PBS, Mr. Gambrell said: "I think the American taxpayers are losing billions of dollars....I don't think the American people should walk away from this. I think they need to really question the government that is currently auditing oil and gas royalties and make sure that they do it correctly. I think there needs to be independent review, I mean separate from the government, a review of the agencies that collect royalties, manage the oil and gas properties. There needs to be better oversight and there needs to be independent audits of these agencies."[9]

Oil industry tycoon Jack Grynberg has also filed a False Claims Act lawsuit, this one alleging more than a dozen ways that companies can underpay gas royalties, particularly by manipulating the volumes of gas downward. Mr. Grynberg estimates that oil and gas companies may end up owing $35 billion as a result of his lawsuit.[10]

Native Americans are also concerned. In a May 2006 *Washington Post* article, Roger Fragua, deputy director of the Council of Energy Resource Tribes said: "We are convinced that there is serious underreporting of production and serious underpayment of royalties owed to the tribes...The federal government, at least in this administration, is not protecting our interests. So we are looking for ways to go after the companies ourselves."[11]

In 2006, the Minerals Management Service has stifled criticism from states and Indian tribes which have questioned the wisdom of replacing auditing with computer checks, called "compliance review" in a series of letters.[12] At a meeting of state and Indian auditors in August 2006, the MMS informed the

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[9] "Crude Awakening," PBS NOW, June 16, 2006. http://www.pbs.org/now/shows/224/indian-oil-royalties.html

[10] "Independent Oilman Takes on Oil Giants," National Public Radio, May 31, 2006. http://www.npr.org/templates/story/story.php?storyId=5441272

[11] "Firms Harvesting Energy From Public Land May Owe U.S.: Under the False Claims Act, Groups Sue for More Fees," Washington Post, May 7, 2006. http://www.washingtonpost.com/wp-dyn/content/article/2006/05/06/AR2006050600905.html

[12] Letter to Lucy Querques Dennett, Associate Director, Minerals Management Service from State and Tribal Royalty Audit Committee, February 2, 2006. http://www.pogo.org/m/ep/ep-StateandTribal-02202006.pdf

group that it was eliminating the ability of the states and tribes to meet independently, a move that some felt was designed to gut the organization and silence its criticisms A September, 2006 letter from concerned members of Congress concluded: "MMS is retaliating against STRAC [State and Tribal Royalty Audit Committee] for voicing its concerns to Congress about dysfunction in the royalty management program."[13]

State and tribal participation in audits was authorized by Congress in 1982 after congressional findings that Interior was operating the royalty program as an "honor system," under which federal lessees (oil companies) were allowed to report and pay whatever they wanted. An independent commission, whose findings Congress adopted, told Interior to implement independent cross checks of industry representations and to avoid blind acceptance of industry "bookkeeping."[14]

POGO urges incoming Interior Secretary Dirk Kempthorne to change the dynamic at the Interior Department described by Inspector General Devaney where those responsible for the failures to do their job collect what is owed the American taxpayer are held accountable. However, we would urge Secretary Kempthorne to take that suggestion one step further and seek out and reward whistleblowers who bring forward evidence of negligence, waste, fraud, or corruption. Firings such as that of Mr. Gambrell and Mr. Maxwell have a chilling effect on employees at the MMS, re-enforcing a culture where wrong-doing is covered up rather than addressed.

Finally, POGO urges the Congress and Secretary Kempthorne to investigate the concerns of states and tribes and do everything possible to ensure that their concerns are being adequately addressed by MMS.

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[13] Letter to the Honorable Johnnie Burton, Director, Minerals Management Service, from members of Congress August 31, 2006. http://www.pogo.org/m/ep/ep-08312006-Burton.pdf

[14] "Comments on Proposed Federal Oil Valuation Rule," Project On Government Oversight, November 10, 2003. http://www.pogo.org/p/environment/el-031101-oil.html

Chairman TOM DAVIS. Mrs. Maloney.

Mrs. MALONEY. I want to thank the chairman for holding this very, very important hearing at a time when we have an $8 trillion debt, soaring deficits, the largest trade deficit in history, to find out that we are missing billions and billions of dollars that are owed to the American taxpayers for oil extracted from land that is owned by the American people is inexcusable. It is wrong and we have to correct it.

Yesterday's hearing was tremendously disturbing. The Department of Interior's Inspector General, Mr. Devaney, testified that at the top levels of the agency, widespread ethics failures and abuses, cronyism, have become commonplace. This is absolutely unacceptable. He testified that at the Interior Department's Office of Ethics, they dismissed 23 out of 25 potential ethical breaches, and then he noted that he found that investigators had missed millions of dollars in underpayments. His office uncovered evidence that agency auditors had lost key files, then tried to fool investigators by forging and back-dating the missing documents. He noted that the agency gave a bonus to the official who came up with the false papers.

I find this outrageous. I request unanimous consent to place in the record two articles on MMS and the Interior Department from my hometown newspaper, the New York Times, and also on the huge royalties that Chevron is avoiding.

Mr. DAVIS. Without objection, the articles will be placed in the record.

Mrs. MALONEY. I just want to say that MMS, as Mr. Waxman just said, they seem to be captured by the industry they are supposed to oversee. I had someone call me last night, Mr. Chairman, and say it is a revolving door, that half the people who work at MMS are from the oil industries. I don't know if that is true or not, but I would like to join you in a GAO report request to find out is it a revolving door. I would like to look at how many people presently and in the past have been put there by the oil industry, because they certainly are not serving Government. They are not serving ethics. They are not serving what they are supposed to be doing.

The allegations that have been made are absolutely almost criminal. What I would like to know, and I find it difficult because I am supposed to be chairing or be ranking member at another meeting for the Democrats right now, but I want to know, and this is a question I want to know and I want to place it in writing. I will come back and hopefully have a chance to ask more question.

But I want to know why since 2001, there has been a plunge in the royalty money collected from these companies. This has been found from the auditing and compliance review. How do you explain the differences in the average from 1989 through 2001 at $176 million per year? And from 2002 through 2005, when it has been less than $50 million? How do you drop so much?

Something is wrong. MMS is not doing its job. I specifically would like that question answered. I will get it to you in writing. It is based on auditing that I have read.

I just want to add that the Government Accountability Office estimates that because price thresholds were not included in the

deepwater leases from 1998 and 1999, the Government, that is the American taxpayers, will lose approximately $10 billion in revenue. The GAO further estimates that the Government could lose as much as $60 billion over the next 25 years if the Kerr-McGee Corp. wins its lawsuit challenging the price thresholds set on its leases from 1996, 1997 and 2000.

At a hearing that Mr. Issa had earlier in July, we learned from witnesses, from Chevron, that they had raised the issue of the missing price thresholds with officials from MMS on several occasions in 1998 and 1999, that for some reasons these officials took no action. We have to look into what happened there.

These "mistakes" have cost the American taxpayers literally billions and billions of dollars. We as a Government cannot afford these types of errors. We must ensure that this never happens again. Personally, I believe the whole Department should be abolished and the whole oversight should be moved out of Interior to a different, independent department or some other place in Government because clearly they cannot get it right. This is just one of a long series of serious mistakes, possibly criminal actions, that have taken place where the American taxpayer has not been protected, and been abused on oil extracted from land owned by the American people.

I look forward to the testimonies. Thank you, Mr. Chairman.

[The prepared statement of Hon. Carolyn B. Maloney follows:]

Representative Carolyn B. Maloney (NY-14)
"Interior Department: A Culture of Managerial Irresponsibility and Lack of Accountability"
2154 RHOB – 10:30 A.M.
September 14, 2006

Thank you Chairman Davis
and Ranking Member Waxman
for holding this very important hearing today.

I also want to commend Chairman Issa
and Ranking Member Watson
of the Subcommittee on Energy and Resources
for all of their work on this issue.

It is indisputable that the American taxpayers
are losing billions of dollars in royalties
due to them by the oil and gas companies
who are taking valuable resources
out of federal lands.

The Government Accountability Office
estimates that because price thresholds
were not included in deepwater leases
from 1998 and 1999,
the government will lose
approximately $10 billion in revenue.

The GAO further estimates

that the government could lose
as much as $60 billion
over the next twenty-five years
if the Kerr-McGee Corporation
wins its lawsuit challenging the price thresholds set
on its leases from 1996, 1997, and 2000.

At a hearing in July, we learned from witnesses from
Chevron that they had raised the issue
of the missing price thresholds
with officials from MMS on several occasions
in 1998 and 1999.

Yet for some reason,
those officials and MMS took no action
to correct this oversight.

This mistake has cost the taxpayers billions
of dollars.

We cannot afford these types of errors,
and we must ensure that they never happen again.

Yet just this week, *The New York Times*
reported that leases signed in July of this year could
also cost the government billions of dollars.

I joined with Representatives Hinchey, Markey,
George Miller, and others in passing
an amendment
to the FY07 Interior Appropriations bill
that would prohibit any funding
in the bill from being used to carry out
the deepwater royalty relief provisions already
in statute.

While this was an important first step,
we must do more.

We must pass H.R. 4749,
the "Royalty Relief for American Consumers Act"
which would ***force*** the MMS
to renegotiate those leases
that lack price thresholds.

I would like to hear
from the Department of Interior
about its plans to ensure that the states
have the necessary funding to conduct audits.

An amendment that I attached
to the Interior Appropriations bill
directed $1,000,000 of the overall appropriation for
the MMS to States and Tribes
for auditing purposes.

For several years, the total funding
that the MMS has provided for audit funds
was held static at about $9 million
with no increases for inflation.

In FY2005, the MMS began cutting allocations
to some States and Tribes
while reallocating funds.

The Department of Interior
should be working
to improve its auditing programs,
and I hope to hear what steps are being taken
in that direction.

Specifically, I want to know
why since 2001, there has been a plunge
in the money collected
from auditing and "compliance review."

How do you explain the differences
in the average from 1989 through 2001
at $176 million per year,
and from 2002 through 2005,
when it has been less than $50 million?

Finally, at yesterday's hearing

the Department of Interior
Inspector General testified that at the top levels
of the agency, widespread ethics failures
and abuses have become commonplace.

That is simply unacceptable.
I expect to hear from today's witnesses
about what immediate reforms
the Department will be undertaking
to clean up the way it is conducting
business on behalf of the American people.

After a summer of skyrocketing fuel prices,
the public is demanding answers.

Thank you.

Jamie Rose for The New York Times

Earl Devaney, the Interior Department inspector general, told a House hearing, "short of a crime, anything goes" at high levels of the agency.

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By EDMUND L. ANDREWS
Published: September 14, 2006

WASHINGTON, Sept. 13 — The Interior Department's chief official responsible for investigating abuses and overseeing operations accused the top officials at the agency on Wednesday of tolerating widespread ethical failures, from cronyism to cover-ups of incompetence.

Skip to next paragraph

Small Business

Go to Special Section »

"Simply stated, short of a crime, anything goes at the highest levels of the Department of the Interior," charged Earl E. Devaney, the Interior Department's inspector general, at a hearing of the House Government Reform subcommittee on energy.

"I have observed one instance after another when the good work of my office has been disregarded by the department," he continued. "Ethics failures on the part of senior department officials — taking the form of appearances of impropriety, favoritism and bias — have been routinely dismissed with a promise 'not to do it again.' "

The blistering attack was part of Mr. Devaney's report on what he called the Interior Department's "bureaucratic bungling" of oil and gas leases signed in the late 1990's, mistakes that are now expected to cost the government billions of dollars but were covered up for six years.

While these leases were the specific focus of the hearing, Mr. Devaney directed most of his criticism at what he called a broader organizational culture at the Interior Department of denial and "defending the indefensible."

He expressed particular fury at the willingness to dismiss two dozen potential ethical lapses by J. Steven Griles, a former industry lobbyist who served as deputy secretary of the interior during President Bush's first term.

Mr. Griles resigned after allegations surfaced that he pushed policy decisions that favored some of his former oil and gas industry clients and that he tried to steer a $2 million contract to a technology firm that had also been one of his clients.

In a 145-page report in 2004, the inspector general described Mr. Griles as a "train wreck waiting to happen." But on Wednesday, Mr. Devaney said he was appalled that the Interior Department's office of ethics dismissed 23 out of 25 potential ethical breaches against Mr. Griles and that Gale A. Norton, then secretary of the interior, decided not to act on the two remaining allegations.

Mr. Griles is once again a lobbyist in Washington. Efforts to reach Mr. Griles on Wednesday evening at his lobbying firm, Lundquist, Nethercutt & Griles, were unsuccessful.

Mr. Devaney said that case was typical of a much broader "culture of managerial irresponsibility and lack of accountability" in the top reaches of the Interior Department.

"I have unfortunately watched a number of high-level Interior officials leave the department under the cloud of O.I.G. investigations," Mr. Devaney said, referring to the Office of Inspector General.

"Absent criminal charges, however, they are sent off in the usual fashion, with a party paying tribute to their good service and the secretary wishing them well, to spend more time with their family or seek new opportunities."

That was almost exactly what happened to Mr. Griles, who was never charged with any wrongdoing, though he admitted to using bad judgment in some cases.

Dirk Kempthorne, who succeeded Ms. Norton as interior secretary earlier this year, said Wednesday that he took the inspector general's allegations "very seriously" and had sent a letter to all employees on his first day at the department on the need to follow ethical guidelines.

Mr. Kempthorne declined to say what additional actions he might take until he saw Mr. Devaney's final report.

Mr. Devaney, a burly man who began his career as a police officer in Massachusetts, is no stranger to combative investigations or confrontations with top officials.

He spent more than 20 years as a special agent in the Secret Service, specializing in white-collar crime, eventually being put in charge of the service's fraud division. In the 1990's, he became director of criminal enforcement at the Environmental Protection Agency.

He was named inspector general at the Interior Department in 1999, just as whistle-blowers outside the government were pressing huge lawsuits alleging that oil companies were fraudulently underpaying royalties.

Three years ago, Mr. Devaney scathingly criticized the Interior Department's auditing program for oil and gas royalties.

Beyond finding that investigators had missed millions of dollars in underpayments, his office uncovered evidence that agency auditors had lost key files, then tried to fool investigators by forging and backdating the missing documents. In an acid rebuke of the agency, Mr. Devaney noted that the agency gave a bonus to the official who came up with the false papers.

Mr. Devaney's broadside against the Interior Department's culture dovetailed with his tentative conclusions in his most recent investigation, into how the department had managed to sign 1,100 leases for offshore drilling that inadvertently let energy companies escape billions of dollars in royalties on gas and oil produced in the Gulf of Mexico.

The leases, signed in 1998 and 1999 during the Clinton administration, allow companies to escape normal federal royalties — usually 12.5 percent of sales — on the tens of millions of barrels of oil on each lease.

The royalty break was intended as an incentive for deepwater drilling, but it was also supposed to end if oil prices climbed above a "threshold" level of about $34 a barrel. The leases at issue omitted that restriction, and department officials kept quiet about their mistake for six years after they discovered it.

The problem was first disclosed by The New York Times in March. Government officials now estimate that the mistake could cost the Treasury as much as $10 billion over the next decade.

"The Interior Department holds our natural resources in trust for the American people," said Representative Darrell Issa, Republican of California and chairman of the House Government Reform subcommittee

on energy and resources. "It squandered billions instead."

Mr. Devaney said the error, a result of compartmentalized thinking within the department, might have remained buried if senior officials had had their way.

"We do not have a 'smoking gun,' " Mr. Devaney said. "We do, however, have a very costly mistake which might never have been aired publicly absent The New York Times, the interest of this committee, the Senate Committee on Energy and Natural Resources and several other interested members of Congress."

Felicity Barringer contributed reporting.

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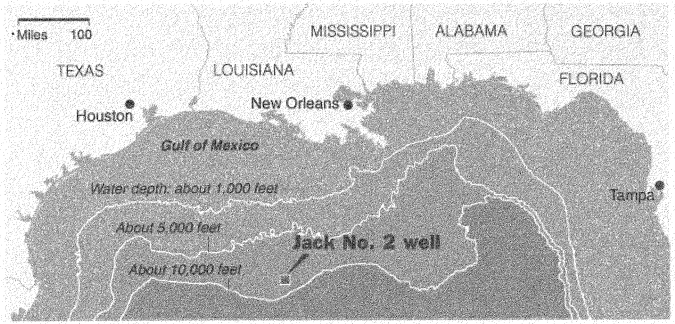
Chevron Could Avoid Huge Royalties on New Field



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By EDMUND L. ANDREWS
Published: September 12, 2006

WASHINGTON, Sept. 11 — A group of oil companies led by Chevron, which said last week that they had discovered a huge new oil field in the Gulf of Mexico, could avoid more than $1 billion in royalty payments to the federal government for the oil.

Skip to next paragraph

Small Business

Go to Special Section »

The potential bonus to Chevron and its partners stems from a mistake the Interior Department made in signing offshore leases in the late 1990's for drilling in federal waters. The magnitude of the oil discovery — estimated in a range of 3 billion to 15 billion barrels — is likely to intensify a battle in Congress over incentives for drilling in publicly owned waters.

Under pressure from lawmakers, Chevron and other big producers have said that they would renegotiate their leases. But they have not said how much they are willing to give up, and the Interior Department has virtually no bargaining power under current law.

Chevron and its partners, Devon Energy and Statoil ASA of Norway, have six leases in the Jack oil field, about 175 miles off the coast of Louisiana. Two of the leases allow the companies to avoid royalties on as much as 87.5 million barrels of oil per lease.

The benefit, known as royalty relief, was supposed to be halted if the price of oil climbed above $36 a barrel. But that restriction was omitted on all leases signed in 1998 and 1999, including the two held by Chevron and its partners.

The exact value of the potential break on federal payments will depend both on the price of oil and how much of it comes from the two leases. At $70 a barrel, the Chevron group could save about $1.5 billion in royalties if the government agreed that both leases were contributing to Chevron's production.

But the actual savings would be much lower if oil prices slumped to $40 a barrel. And the savings would disappear if the government insisted that none of Chevron's output was coming from the two leases, but from the four not eligible for the break.

A spokesman for Chevron, Don Campbell, said Monday that "any conjecture about forgone royalties" would be "pure speculation and an academic exercise."

The Chevron leases are the biggest, but hardly the only leases that allow oil companies to avoid royalties regardless of how high energy prices climb.

Even before Chevron and its partners confirmed the discovery last week, the Government Accountability Office, the investigative arm of Congress, had estimated that the Treasury could lose as much as $20 billion over the next 25 years.

On Wednesday, the House Committee on Government Reform will begin two days of hearings on how the original calculation came to be. Republicans have been eager to blame the Clinton administration, which was in office when the leases were signed.

But the Interior Department's inspector general is expected to testify that the Bush administration may be in danger of making exactly the same move on new leases.

According to Congressional aides, the inspector general has uncovered evidence that midlevel Interior Department officials warned as recently as July that a new batch of leases could cost the government billions of dollars beyond the original misstep.

Republican lawmakers are also angry about the Interior Department's response to the problem, which was first disclosed by The New York Times in March.

Representative Thomas M. Davis III of Virginia, chairman of the Committee on Government Reform, complained of "systematic delays" and said the Interior Department had withheld large volumes of "critical information" from Congressional investigators.

Chevron's huge potential savings highlight a dispute about how to remedy the leases signed in the late 1990's. The Bush administration and many Republican leaders argue that those leases are binding contracts that cannot be changed except through an agreement by the companies.

Democrats acknowledge that the contracts are binding, but support a measure that would punish companies that refuse to renegotiate their contracts by prohibiting them from acquiring additional oil and gas leases.

The House passed the Democratic proposal, over objections from Republican leaders, as an amendment to the Interior Department's spending bill. The Senate Appropriations Committee attached a similar measure to its bill, but the overall measure has been stalled for months.

The hearings this week are expected to focus on how the Interior Department blundered on the leases. The inspector general, Earl E. Devaney, has concluded that the leases were a mistake rather than a result of any collusion with industry.

But Mr. Devaney is also expected to say that the Interior Department continues to suffer from a "lack of accountability." Investigators have combed through 5,000 e-mail messages and are believed to have found some written as recently as this summer in which frustrated midlevel officials warned that the Interior Department had not fixed the bureaucratic and procedural problems that led to the original mistake.

Representative Davis and Representative Darrell Issa, Republican of California and chairman of the Government Reform energy and resources subcommittee, accused the Interior Department in August of deliberately obstructing their investigation.

"We are deeply concerned that the department may have intentionally withheld critical information from the subcommittee," the two lawmakers wrote in a letter on Aug. 3 to Dirk Kempthorne, the new Interior secretary. "If this is the case, then it has intentionally impeded this duly authorized Congressional investigation."

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Chairman TOM DAVIS. Thank you.

Mr. Kucinich.

Mr. KUCINICH. All across this country, the American people have been aware of the power of the oil companies. Over this past summer, however, they were able to squeeze consumers by raising the price of gasoline far over $3 per gallon. What is reflected here is that the Government has stood back while the oil companies have continued to aggregate, monopolize the restraint of trade necessarily has produced market conditions which have put a squeeze on the consumers, jacked up the price of oil, and people are basically at the mercy of the oil companies which are now anticipating the elections, trying to protect some of their friends, putting the price of oil down a little bit.

You can look at this picture and you could find 100 things wrong with it. Let me just talk about a few of them. It is absolutely impossible to imagine that this condition could have been created without the oil companies being intimately involved in the construction of the system which resulted in them being able to basically steal $10 billion from the American people in terms of royalties which were not paid. I think it would be interesting for this committee to know who actually wrote the leases, and each iteration of a lease. Government attorneys or industry attorneys handing it over to the Government? It would be very interesting to find out.

Also, I think that this committee in its work ought to come to a conclusion that says that these leases should be canceled and renegotiated. I mean, obviously, there is an element of either fraud or misfeasance here. That is something that needs to be done in order to protect the public interest.

Furthermore, action ought to be taken by this Government, if it is capable of doing it, to sue to recover at least $10 billion that was due the American people and not paid for. Furthermore, there should be a criminal investigation of those individuals who are responsible for overseeing the contracts. We can't just leave this to some idea of a "mistake." How is it that mistakes are made and the oil industry ends up with $10 billion more? That is a mistake? A mistake?

If there was ever a call for a new energy policy, this is it. If we had invested a fraction of the amount of money that the American people have been deprived of here, and alternative energies, we would be less reliant on oil and wouldn't be in a situation where the oil companies are actively trying to cheat the Government out of royalties that are due to the American people.

So Mr. Chairman, I am glad to see us reviewing this leasing process. There is a line in the Bible that says that which is crooked cannot be made straight. Nothing is going to be made straight about this energy policy until we start to move away from non-renewable sources of energy to more sustainable sources.

Thank you, Mr. Chairman.

Chairman TOM DAVIS. Thank you.

Mr. Duncan.

Mr. DUNCAN. Well, Mr. Chairman, very briefly, thank you for calling this hearing. This is a very important matter.

You know, ever since I started following Government and political issues closely as a teenager, over all these years I have read so many examples of waste, fraud and abuse and mismanagement at the Federal level that you almost just get immune to it, so that almost nothing surprises us anymore.

After so many years of reading and hearing about these types of things, you begin to wonder if the Federal Government can do anything in an economic, efficient way. People aren't held accountable for big mistakes. They don't even get worried about since it is not coming out of their own pockets, so we hear about mistakes all the time that, if they happened in the private sector, people would be fired and major changes would be made.

But when I read, as I read in the Congressional Quarterly Today publication that came to us this morning, that the Inspector General of the Energy Department testified yesterday, saying that he "conceded he has no evidence that the mistake over the royalties was anything more than classic bureaucratic bungling, with a process that required plenty of signatures, but no individual to assume final responsibility."

And then in another companion article, it says that Chairman Davis said it was unacceptable that the bungled leases failed to surface for 5 years. And it also says that nearly 30 people signed off on all this. I mean, this is one of the worst cases I think I have ever heard of. I am just stunned.

If we end up just letting this go by excusing it as classic bureaucratic bungling, then we have accepted something that we shouldn't accept.

So I appreciate your holding this hearing and I hope that we determine or arrive at some really strong action to take in regard to this.

Thank you very much.

Chairman TOM DAVIS. Thank you.

I would ask unanimous consent that Mr. Markey be allowed to sit in on today's hearing. Without objection, so ordered.

Ms. Watson.

Ms. WATSON. I want to thank the chairman for convening this hearing. The Subcommittee on Energy and Natural Resources, which I am the ranking member, has held four hearings on this subject. So I am really pleased to see the Deputy Secretary of Interior and the Director of Minerals Management here in attendance. This should be a very informative session to finally start talking about how to fix the errors and the larger issues the Inspector General identified at yesterday's subcommittee hearing.

I was unfortunately unable to attend yesterday's hearing, and we know of the major problems. Several of the oil companies were at the previous hearings and are ready to work with us to address the errors.

I am particularly incensed when we know that in the year 2005 oil companies registered over $110 billion in profits and oil prices are now close to $70 a barrel. This is the only industry here whose made those types of profits. And so our Government has given the oil companies tremendous benefits, and not to pay back in terms of the contractual agreement the kinds of sums that should have come to the U.S. Government is just unthinkable.

So this problem still persists today. The American consumer is suffering and continues to suffer. We can't have these kinds of profits without some responsibility on the part of our Government to follow through. The errors that occurred during 1998 and 1999 could cost our Government an estimated $20 billion within the next 25 years. This should not be happening, but it is not the only problems at the Minerals Management Service and the Department of Interior.

We have a duty as Congress to the American taxpayer. One of our duties is not to allow these companies to misuse public assets, and we must protect American people's money. So the House had passed the Hinchey amendment to fix this problem in the Interior appropriations bill, and I hope that my colleagues will support this provision in the final bill that will come in front of us soon.

This committee has heard much about larger problems at the Department of Interior over the many hearings, and we have an obligation to investigate them, certainly our subcommittee has.

So I want to thank the Chair again, and I want to thank the witnesses for being willing to come and address this problem. Thank you so much, Mr. Chairman.

Chairman TOM DAVIS. Thank you very much.

Mr. Issa.

Mr. ISSA. Thank you, Mr. Chairman.

Chairman TOM DAVIS. You started all this.

Mr. ISSA. Thank you, Mr. Chairman.

I am very pleased that our subcommittee has been able to move this discovery along, and thank you and Ranking Member Waxman for holding this important hearing today on the Interior Department's culture of managerial irresponsibility and lack of accountability. I also want to thank the witnesses for taking time to appear here before the full committee.

Over the past 7 months, the Subcommittee on Energy and Resources has conducted an investigation of the Interior Department and the Minerals Management Service. I sought to find out how and why the thresholds were missing in deepwater leases in 1998 and 1999. I conducted four hearings at which Interior Department employees and oil company officials testified. These witnesses shed a great deal of light on the issue and to a great extent the culture of the Interior Department. I believe that is what we are here for today.

I would again like to thank Chevron and its staff for their candor before the subcommittee. It was in fact their testimony that was a breakthrough in our discovery. Yesterday, we heard testimony from the Interior Department's Inspector General, Earl Devaney. He detailed the results of his own investigations into the missing price threshold issue. The fact that the thresholds were missing for 2 years was only the beginning of the problem. The central issue from yesterday's hearing was the coverup. I would paraphrase him by saying, the multiple D's: delay, denial. That is in fact part of the culture that not only are there mistakes made, but there is inherently a pattern of coverup.

Department employees discovered the missing price thresholds apparently through oil company executives telling them, in 2000. Some e-mails even authenticated the fact that there was that dis-

covery. Some personnel even told their executives and made changes on their own. Yet, the Department made an affirmative decision not to notify their superiors. Had they notified their superiors and amended the contracts at no cost to the oil companies, because the price thresholds at that time were low, we would have no reason for this investigation. Instead, they allowed the problem to fester and become a $10 billion-plus wound. As Mr. Devaney said, this was but an example of the bureaucratic bungling and stovepiping of responsibility.

We are here today to discuss the bigger issue. There appears to be a culture of irresponsibility, unaccountability that pervades the entire Department. Officials are here from the Interior Department today. I regret, however, that the Secretary is not. I would hope, very much hope, that we would soon have the ultimate responsible cabinet officer here.

Make no mistake: The American people are watching today. The Interior Department owes the American people a fiduciary duty to them and holds this Nation's valuable resources in trust for the American people. The Department has let them down and they have not accepted, and the American people will not accept, the wink and the nod of, well, that was just a mistake.

Mr. Chairman, I want to thank you for this. I look forward to our witnesses, but I hope that my opening statement has set a bipartisan tenor that this is something that has gone on before this President and if we don't change it here and over the next several years, it will go on after this administration.

With that, I yield back.

[The prepared statement of Hon. Darrell E. Issa follows:]

Opening Statement of Rep. Darrell Issa for September 14, 2006
Government Reform Committee

Interior Department: A Culture of Managerial Irresponsibility and Lack of Accountability?

Thank you Mr. Chairman and Ranking Member Waxman for holding this important hearing on the Interior Department's culture of managerial irresponsibility and lack of accountability. I also want to thank the witnesses for taking time to appear before the full Committee.

Over the past seven months, the Subcommittee on Energy and Resources has conducted an investigation of the Interior Department and the Minerals Management Service. It sought to find out how and why price thresholds were missing in deep water leases in 1998 and 1999.

I conducted four hearings at which Interior Department employees and oil company officials testified. These witnesses shed a great deal of light on this issue, and to a greater extent, the culture of the Interior Department. I would again like to thank Chevron and its staff for their candor with the Subcommittee.

Yesterday we heard testimony from the Interior Department's Inspector General, Earl Devaney. He detailed the results of his own investigation into the missing price thresholds issue.

The fact that price thresholds went missing for two years was only the beginning of the problem. The central issue from yesterday's hearing was the cover-up that ensued.

Department employees discovered the missing price thresholds in 2000, yet they made an affirmative decision not to notify their superiors. Had they notified their superiors and amended the contracts – at no cost to the oil companies because the price of oil was low – we would have had no reason for this investigation. Instead, they allowed the problem to fester into a $10 billion wound.

As Mr. Devaney said, this was but one example of bureaucratic bungling and stove-piping of responsibilities.

We are here today to discuss the larger issue. There appears to be a culture of irresponsibility and unaccountability that pervades the entire Department. Officials are here from the Interior Department today. I regret, however, that Secretary Kempthorne is not here to detail how he will correct the culture of irresponsibility.

Make no mistake that the American people are watching today. The Interior Department owes a fiduciary duty to them, and it holds this Nation's valuable resources in trust for them. The Department has let them down and they will not accept a wink and a nod at this Committee's demand for complete accountability.

Chairman TOM DAVIS. Thank you very much.

The gentleman from Baltimore.

Mr. CUMMINGS. Thank you very much, Mr. Chairman.

I, too, thank you for holding this vitally important hearing to examine reports of mismanagement in the way the Department of Interior's Minerals Management Service [MMS], collects royalties from oil companies that drill on public property.

As you know, MMS is the Federal agency that is charged with ensuring that all moneys derived from mineral leasing and production activities on Federal and Indian lands are collected properly, accounted for, and distributed. This is no small task. Federal onshore and off-shore mineral leases generate almost $6 billion annually, comprising one of the Federal Government's largest sources of non-tax income.

This revenue supports a vast array of essential Government functions providing 90 percent of funding for the Land and Water Conservation Fund and 100 percent of funding for the National Historic Preservation Fund. It also generates millions of dollars for individual States. My home State of Maryland, for example, in fiscal year 2002 received $195.9 million. On average, States received about $200 million annually.

Additionally, agency collections from off-shore leases called Outer-Continental Shelf [OCS], lands, play a significant role in our Nation's energy picture. OCS lands provide more than 25 percent of the natural gas and 30 percent of the oil produced in the United States. In total, MMS administers about 7,300 active leases on 40 million acres of the OCS.

Given the important of the MMS royalty collection program, the need for it to run as effectively and efficiently as possible is abundantly clear. Unfortunately, recent reports indicate that goal has not been achieved and that mismanagement and waste are prevalent.

In this morning's New York Times, Interior Department Inspector General Earl Devaney is quoted from his testimony at the hearing of the Subcommittee on Energy as saying "Simply stated, short of crime, anything goes at the highest levels of the Department of the Interior." I find it troubling that MMS's mismanagement is reportedly costing taxpayers millions of dollars or even billions of dollars.

Equally troubling are reports that MMS leadership has reacted with hostility when employees have the courage to blow the whistle on the problems that exist. Specifically, in 2003, two MMS auditors who were reportedly among the agency's most successful and aggressive, were fired. Others report that MMS management pressured auditors not to pursue companies that cheat on royalties. As a long-time advocate for the rights of whistleblowers, I find these reports to be deeply troubling and shocking to the conscience.

Pressure for reform has been applied through media publicity, investigations by the Office of Inspector General, as well as hearing of the Subcommittee on Energy Resources. I look forward to hearing from today's witnesses on how MMS has responded to that pressure. In May, Dr. Kempthorne was appointed as the new Secretary of the Interior. I look forward to hearing what his response

to these reports has been and whether he has begun to implement the reforms that are necessary to turn the agency around.

I want to thank our witnesses for being here today, and I look forward to hearing your testimony.

[The prepared statement of Hon. Elijah E. Cummings follows:]

U.S. House of Representatives
109th Congress

Opening Statement

Representative Elijah E. Cummings, D-Maryland

Full Committee Hearing:
"Interior Department: A Culture of Managerial Irresponsibility and Lack of Accountability?"
Committee on Government Reform

September 14, 2006

Mr. Chairman,

Thank you for holding this vitally important hearing to examine reports of mismanagement in the way the Department of Interior's Minerals Management Service (MMS) collects royalties from oil companies that drill on public property.

As you know, MMS is the federal agency that is charged with ensuring that all monies derived from mineral leasing and production activities on Federal and Indian lands are collected, properly accounted for, and distributed. This is no small task.

Federal onshore and offshore mineral leases generate almost $6 billion annually, comprising one of the federal government's largest sources of non-tax income.

This revenue supports a vast array of essential government functions, providing 90 percent of funding for the Land and Water Conservation Fund and 100 percent of funding for the National Historic Preservation Fund.

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Additionally, agency collections from offshore leases, called Outer Continental Shelf or OCS lands, play a significant role in our nation's energy picture.

OCS lands provide more than 25 percent of the natural gas and 30 percent of the oil produced in the United States. In total, MMS administers about 7,300 active leases on 40 million acres of the OCS.

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In May, Dirk Kempthorne was appointed as the new Secretary of the Interior. I look forward to hearing what his response to these reports has been, and whether he has begun to implement the reforms that are necessary to turn the agency around.

I want to thank our witnesses for joining us today and yield back the balance of my time.

Chairman TOM DAVIS. Mr. Markey, would you like to make an opening statement? Thanks for being with us.

Mr. MARKEY. Thank you, Mr. Chairman. I very much appreciate your graciousness in allowing me to testify here today.

As you know, the Department of Interior admitted market-based price thresholds for the suspension of royalty relief on leases issued in the late 1990's in the Gulf of Mexico. I am here today to remind my colleagues that the House of Representatives has already acted on a bipartisan basis to fix this problem when it passed the Hinchey-Markey amendment last May.

As long as we protect the House language in the Interior appropriations bill, and pass that bill this fall, we will head off yet another glaring subsidy to companies which already have incentives, and more than they have ever dreamed of, in the spectactularly high world oil prices of today.

This past May 18, just 3 months ago, a bipartisan majority of the House voted 252–165 for the amendment which Mr. Hinchey and I proposed on the House floor. Despite the controversy surrounding the issue, the House recognized that this amendment threaded the legislative needle by neither abrogating existing contracts nor ignoring a public rip-off. It does so by giving every affected company a simple choice: either renegotiate the old royalty-free leases or accept the fact that your company will be barred from any future leases from the Federal Government.

The amendment creates strong incentives for those companies to renegotiate at a time when oil prices are high and oil companies are making record profits, but will leave current contracts unamended if the company chooses not to renegotiate. The Senate has subsequently included similar language in their version of the bill.

The recently reported discovery of the new reserves in the so-called Jack Field in the Gulf of Mexico, estimated by Chevron to be between 3 million and 15 million barrels of oil, has further highlighted the need to take immediate action to correct those leases. This week, as we know, the New York Times reported that Chevron and its partners hold six leases in the new Jack Field, two of which would allow the companies to avoid royalties on as much as 87.5 million barrels of oil per lease. The Times estimated that those leases alone could result in the loss of as much as $1.5 billion in unpaid royalties at $70 a barrel.

However, the Bush administration and the oil companies have been fighting the amendment, which has now passed the House and the Senate. The oil industry has offered a number of arguments against our amendment, each of which has been demonstrated to be completely false. For example, the oil industry has argued that our amendment would violate the sanctity of the contracts in question and force an abrogation of those contracts.

However, the Congressional Research Service clearly stated in a memo dated May 18, 2006 "enactment of this amendment would not constitute a taking of existing leaseholders' rights, but would merely establish a new qualification for potential lessees. It has long been recognized that the Government has broad discretion in determining those firms with which it will enter into contractual agreements."

The oil industry has also argued that blocking a large number of companies from purchasing new leases would hinder production. However, our amendment provides companies that still desire to purchase new leases with a simple solution: renegotiate their old leases to add a price threshold that cuts off royalty relief whenever prices get high.

However, the administration and the Department of Interior have opposed the amendment, seeking instead to attempt to cajole oil companies to voluntarily come back to the table to renegotiate. I will be sending a letter again, with Mr. Hinchey, to Secretary Kempthorne and other sponsors of the amendment urging the Department of Interior to immediately support the amendment. We must ensure that all oil companies holding these leases renegotiate, not just the small percentage that are feeling particularly generous and public spirited, leaving the bad actors in a position to take unfair advantage.

Our amendment is a very simple way to correct these leases and recover the billions of dollars which American taxpayers stand to lose in the coming decades, that received strong bipartisan support in Congress. With gas prices hovering still between $2.50 and $3 a gallon, the American people are again watching today to see if the administration, the Department of Interior, will again side with big oil over the American people. It is time for big oil companies to pay their fair share to drill on public land, and I urge Secretary Kempthorne and the Interior Department to immediately come out in support of the Hinchey-Markey amendment now pending before the House and Senate.

I thank you, Mr. Chairman.

[The prepared statement of Hon. Edward J. Markey follows:]

Statement of Rep. Edward J. Markey
Committee on Government Reform
September 14, 2006

Mr. Chairman, thank you for the opportunity to participate in today's hearing. As you know, the Department of Interior omitted market-based price thresholds for the suspension of royalty relief on leases issued in the late 1990's in the Gulf of Mexico. Now, at a time when oil prices are hovering around $60-70 per barrel, the American taxpayers should not be subsidizing big oil companies to drill for oil on public land. Subsidizing a big oil company to drill for oil on public land is like subsidizing a fish to swim – it just doesn't make sense. Indeed, the Government Accountability Office has estimated that this error could result in the loss of as much as $20 to the federal treasury over the next 25 years. I am here today to remind my colleagues that the House of Representatives has already acted on a bipartisan basis to fix this problem when it passed the Hinchey-Markey Amendment last May. As long as we protect the House language in the Interior Appropriations bill, and pass that bill this fall, we will head off yet another glaring subsidy to companies which already have all the incentives they every dreamed of in the spectacularly high world oil prices.

This past May 18, a bipartisan majority of the U.S. House of Representatives voted 252-165 for our amendment. Despite the controversy surrounding this issue, the House recognized that this amendment threaded the legislative needle by neither abrogating existing contracts nor ignoring a public rip-off. It does so by giving every affected company a simple choice – either renegotiate the old royalty-free leases or accept the fact that your company will be barred from any future leases from the federal government. The amendment creates a strong incentive for these companies to renegotiate at a time when oil prices are high and oil companies are making record profits, but leaves current contracts unamended if the company chooses not to renegotiate. The Senate has subsequently included similar language in their version of the bill.

The recently reported discovery of new reserves in the so-called Jack field in the Gulf of Mexico, estimated by Chevron to be between 3 and 15 billion barrels of oil, has further highlighted the need to take immediate action to correct these leases. This week, the *New York Times* reported that Chevron and its partners hold six leases in the Jack oil field, two of which, would allow the companies to avoid royalties on as much as 87.5 million barrels of oil per lease. The Times estimated that those leases could result in the loss of as much as $1.5 billion in unpaid royalties at $70 a barrel.

However, the Bush Administration and the oil companies have been fighting our amendment. The oil industry has offered a number of arguments against our amendment, each of which has been demonstrated to be completely false. For example, the oil industry has argued that our amendment would violate the sanctity of the contracts in question and force an abrogation of those contracts. However, as the Congressional Research Service clearly stated in a memo dated May 18, 2006:

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Bush Administration officials in the Department of Interior have opposed our amendment – seeking instead to attempt to cajole oil companies to "voluntarily" come back to the table to renegotiate. I will be sending a letter today to Secretary Kempthorne along with Representative Hinchey and the other sponsors of our amendment urging the Department of Interior to immediately support our amendment. We must ensure that *all* oil companies holding these leases renegotiate, not just a small percentage that are feeling particularly generous and public-spirited, leaving the bad actors in a position to take unfair advantage.

Our amendment is a very simple way to correct these leases and recover the billions of dollars American taxpayers stand to lose in the coming decades that received strong bipartisan support in Congress. With gas prices hovering around $3 a gallon and oil prices near $70 a barrel, the American people are again watching today to see if the Bush Administration will once again side with big oil over the American people. It is time for big oil companies to pay their fair share to drill on public land and I urge Secretary Kempthorne and the Interior Department to immediately come out in support of the Hinchey-Markey amendment.

Chairman TOM DAVIS. Thank you very much, Mr. Markey.

Members will have 7 days to submit opening statements for the record. We are now going to get to our panel. We have the Honorable P. Lynn Scarlett, the Deputy Secretary of the Department of the Interior, and the Honorable Johnnie Burton, the Director of the Minerals Materials Management Service, Department of Interior. Thanks for your patience.

I understand you have one statement for the two of you. We will give you whatever time you need. It is our policy that witnesses be sworn before you testify, so if you could just rise with me and raise your right hands.

[Witnesses sworn.]

Mr. DAVIS. Thank you.

All right, who is going to give the statement? OK, Ms. Scarlett. Thanks for being with us.

STATEMENT OF P. LYNN SCARLETT, DEPUTY SECRETARY, U.S. DEPARTMENT OF THE INTERIOR, ACCOMPANIED BY JOHNNIE BURTON, DIRECTOR, MINERALS MATERIALS MANAGEMENT SERVICE, U.S. DEPARTMENT OF THE INTERIOR

Ms. SCARLETT. Thank you, Mr. Chairman and members of the committee. Thank you for the opportunity to discuss the lack of price thresholds for the 1998 and 1999 leases in the deepwater of the Gulf of Mexico.

The committee has also asked that I address issues raised in testimony by our Inspector General regarding the Department's ethics, accountability and management. With me today, as you have noted, is Johnnie Burton, Director of the Minerals Management Service, who also served, I might add, as Acting Assistant Secretary of the Land and Minerals Management.

On behalf of the 70,000 employees of the Department of the Interior, let me say that I believe the Department's employees, both senior managers and their staff, are dedicated public servants. They put their lives at risk fighting wildland fires to save communities. They perform extraordinary search and rescue missions, including round-the-clock efforts after Hurricane Katrina. Often when I come to work I find senior managers and their staff in the budget and finance offices working 12, even 14 hours a day and on weekends.

They are dedicated to the Department's multifaceted mission and to serving the American people. Our senior leaders share that dedication.

From his comments, there appear to be disagreements over recommendations that the Inspector General has made and subsequent decisions of the Department regarding those recommendations. Let me underscore that we take extremely seriously any and all instances in which we find waste, fraud, ethical violations, and other inappropriate actions. We strive to address these matters consistent with statutory authorities, available resources, and requirements to treat employees fairly and through due process.

Secretary Kempthorne underscored during his very first day at the Department his unwavering and unequivocal commitment to maintaining an ethical, accountable and effective work force in

service to the American public. We are dedicated to fulfilling that expectation.

Over the past 5 years, I believe our record is one of significant management improvements and commitment to integrity in the Department. We recognize that each day brings new challenges and requires renewed vigilance. We remain today, as in the past, committed to that vigilance.

Let me turn first to the matter of off-shore leases and the missing price thresholds in the 1998 and 1999 leases that occurred under the previous administration. Royalty incentives were established in the Deepwater Royalty Relief Act passed by the Congress in 1995 to encourage development of new supplies of energy by promoting investment, particularly in high-cost, high-risk areas.

Deepwater leases issued by the Minerals Management Service in 1996, 1997 and 2000, after the enactment of the act, included price thresholds. Leases in the 1998 and 1999 leases during the previous administration did not. All deepwater leases issued since March 15, 2000 do include price thresholds that eliminate royalty relief when oil and gas prices are high. At today's prices, royalties are due on any production from these leases. Every lease issued in this program under this administration includes price thresholds.

The Inspector General's investigative report may shed more light on the timing and awareness by all relevant individuals of the actions taken in 1998 and 1999. We look forward, as you do, to that report.

Under our supervision, the situation that occurred in 1998 and 1999 has not happened again, and we are working to make certain that it will not happen during any future administration. Currently, under new practices that we have invoked, each proposed and final notice of sale and associated royalty suspension provisions document now receive detailed review and scrutiny to ensure completeness and accuracy, especially from a price-threshold perspective.

The Minerals Management Service has formalized a process of conducting all reviews in writing through the use of e-mails and places paper copies of those e-mails in its official lease sale file as a record of these reviews and decisions. As Secretary Kempthorne recently told Chairman Davis, the Department has no interest in hindering in any way the investigation into this matter, which occurred under the previous administration and which we look forward to receiving the IG's report on.

We believe we have in place a system today under which the events of 1998 and 1999 would not occur. If there are recommended improvements that we have not yet made, we certainly and absolutely will consider them. The Inspector General's testimony uses the 1998 and 1999 royalty relief issue as a context to raise broader assertions about the Department of the Interior and its management culture. The Department takes seriously any matters in which accountability and integrity of employees and the Department are questioned.

We strive to address these matters consistent with specific circumstances and in accordance with the law. We take seriously recommendations identified in audits. Let me give you some examples. Consider financial management. In 2001, we inherited 170 mate-

rial weaknesses in program or financial controls. Since that time, four new weaknesses have been identified, but we have corrected or downgraded 170 weaknesses. In addition to financial audits, we record all management and other recommendations generated by Interior's Office of the Inspector General, and we track those actions to address those recommendations. We strive to address these recommendations issued by the Office of the Inspector General.

Recently, when the Inspector General raised to me personally concerns whether corrective actions were being fully completed to address his office's findings, I immediately asked the department's Office of Financial Management, which tracks those recommendations, to provide a status of them for those recommendations issued in 2004 and 2005, and to work with the IG to reconcile any differences.

Many issues raised by the Inspector General pertain to ethics. When Secretary Norton assumed office in 2001, the Inspector General reported to her the results of a 1999 management assessment of the ethics program. Subsequent to that, and in consultation with the Office of Government Ethics, the department made significant changes to its ethics program. A new director of the departmental ethics office was selected and the office was moved to the Office of the Solicitor.

During this administration's tenure, the department's ethics office has grown in stature from being an office centered on narrow delivery of service to individual employee questions, to a broader mission of ensuring soundness of all bureau ethics programs and departmental initiatives. Under the leadership of Secretary Kempthorne, the Department continues to strengthen these efforts to meet the highest standards of ethical conduct.

Among Secretary Kempthorne's very first actions on day one in the department was a meeting with the ethics office and with our Inspector General. Over the past 5 years, I and other senior department leaders, have met regularly with the IG and have advanced many management improvements based on his reports and our own initiative.

For example, in 2002 the Inspector General found fault with the Department's appraisal methodology for land transactions. The Department concluded that significant restructuring was necessary and consolidated the appraisal functions performed by bureaus in a new departmental office, responding to criticisms that have endured previously for some 50 years. The new unified Office of Appraisal Services enhances consistency and efficiency, and guards against conflict of interest problems.

Among matters of particular interest to the Inspector General are those pertaining to conduct and discipline. We take seriously workplace infractions and inappropriate conduct. The Inspector General has noted a perception by employees that a significant amount of misconduct is not being reported, and that discipline is administered inconsistently and unfairly in the department. We take these findings very seriously and have prepared a comprehensive action plan to address the Inspector General's recommendations. With a large and dispersed work force, we know that we must constantly strive for and we are dedicated to that effort.

We are also committed to maintaining an efficient work force that operates with integrity. For example, the Interior Department has created a detailed policy regarding Government-issued credit cards. We have put system controls on all accounts, require training for all card-holding officials and established reports to monitor activity.

We have a process in place to refer suspicious activity to the Inspector General. We have created account controls by placing authority and spending limits on accounts. The department's charge-card management team also worked with a bank to create a series of electronic reports that help us identify potential misuse, manage delinquency and track spending.

When problems are identified, the Department takes the appropriate action, including removing employees from Federal service. I believe that our overall record has yielded significant management improvements that benefit the American public. In an organization with the size and reach of the Interior Department, indeed a size that rivals that of a small city, unanticipated and unacceptable decisions and actions may sometimes occur. We take those actions seriously and take actions to address them.

I would be happy to answer any questions you might have at this time.

[The prepared statement of Ms. Scarlett follows:]

STATEMENT OF
LYNN SCARLETT
DEPUTY SECRETARY
ACCOMPANIED BY JOHNNIE BURTON
DIRECTOR, MINERALS MANAGEMENT SERVICE
UNITED STATES DEPARTMENT OF THE INTERIOR
BEFORE THE
COMMITTEE ON GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES

September 14, 2006

Mr. Chairman and Members of the Committee, thank you for the opportunity to appear here today to discuss the lack of price thresholds for the 1998 and 1999 leases in the deep water in the Gulf of Mexico. This issue has been of great concern to this Administration and the Department of the Interior in particular. On January 25, 2006, after questions were raised concerning these leases, the Director of the Minerals Management Service (MMS), Johnnie Burton, asked the Department's Inspector General, Earl Devaney, to investigate the absence of these thresholds in 1998 and 1999.

On Tuesday of this week, I received a letter from the Committee asking that I submit testimony on Wednesday, yesterday, addressing the testimony of the Inspector General for Interior. The Inspector General did not make his testimony available to the Department until yesterday. He makes broad and serious, yet vague, allegations. On behalf of the 70,000 employees of the Department of the Interior—both managers and their staff, I can affirm that the Department's culture is one of dedication to its multifaceted mission; a strong work ethic in behalf of the American people; and a commitment to accountability, efficiency, and effectiveness. The Department disagrees with the IG's broad-brush characterization. We take seriously any and all instances in which we find—whether through our own management efforts or from IG investigations—waste, fraud, ethical violations, and other inappropriate actions. We strive to address these matters consistent with available budget resources, statutory authorities, and requirements to treat employees fairly and through due process.

I will first discuss what we as a Department know and have done about the missing price thresholds in the 1998 and 1999 leases. I will then share with you what I believe is a story of significant management improvements over the last six years at Interior. Our efforts are a journey, not a final destination. We recognize that each day brings new challenges and requires renewed vigilance. Secretary Kempthorne underscored, during his very first day at the Department, his unwavering and unequivocal commitment to maintaining an ethical, accountable, and effective workforce in service to the American people. We are dedicated to fulfilling that expectation.

Royalty incentives were established in the Deep Water Royalty Relief Act of 1995 (Act) to encourage development of new supplies of energy. The purpose of this incentive was to promote investment in a particularly high-cost, high-risk area.

This Administration has taken a conservative approach to implementing royalty relief for deepwater leases:

- Once the royalty relief established by the Act became discretionary in 2001, we reduced the amount of royalty relief allowed on new leases.

- The Administration opposed the mandatory royalty relief provisions in the Energy Policy Act of 2005. A June 14, 2005, Statement of Administration Policy on the energy bill stated, "The President believes that additional taxpayer subsidies for oil-and-gas exploration are unwarranted in today's price environment, and urges the Senate to eliminate the Federal oil-and-gas subsidies and other exploration incentives contained in the bill."

- We have ensured that price thresholds limiting royalty relief when oil and gas prices are high have been included in all deep water leases we have issued.

Deep Water Royalty Relief Act and Mandatory Relief for Leases Issued in 1996-2000

The Deep Water Royalty Relief Act of 1995 (Act) (Pub.L. No. 104-58), enacted on November 28, 1995, was designed to encourage development of new supplies of energy. It included incentives to promote investment in a particularly high-cost, high-risk area, the deep waters of the Gulf. These deep Gulf waters were viewed as having potential for large oil and gas discoveries, but technological advances and multi-billion dollar investments would be needed to realize that potential.

Since the enactment of the incentive, the deep waters of the Gulf of Mexico have become one of the most important sources of domestic oil and gas production. Just this month, Chevron announced that it had a successful production test for oil in the Gulf of Mexico's deep waters, in what could be one of the most significant economically recoverable finds for the domestic oil industry in a generation. The successful well, known as Jack 2, reached a record total depth of 28,175 feet, located in 7,000 feet of water and more than 20,000 feet under the sea floor.

The Act authorized the Secretary, in his or her discretion, to allow royalty relief for deep water projects and to adjust the amount of royalty relief, as appropriate, when oil and gas prices rise. However, for the first five years following enactment, the Secretary's discretion to allow royalty relief was restricted. During this time period, the Secretary was required to suspend royalties for certain volumes of production on all leases in more than 200 meters of water issued in the central and western Gulf of Mexico. These royalty suspension volumes (i.e., specified volumes of royalty-free production) ranged from 17.5 million to 87.5 million barrels of oil equivalent, depending on water depth. The royalty

suspension incentive was intended to provide companies that undertook these investments specific volumes of royalty-free production to help recover a portion of their capital costs before starting to pay royalties. Once the specified volume has been produced, royalties become due on all additional production. This was not a matter of agency discretion.

The Act also gave the Secretary authority to condition royalty relief on price levels, i.e. price thresholds. When oil exceeds a specified price on the market (i.e. the price threshold set in the lease), under the Act companies would then begin to pay a royalty for production. For leases that qualified for royalty relief and were issued prior to the enactment of the Act, price thresholds were mandatory. As stated above, the Act left it to the discretion of the Secretary whether to include price thresholds in leases issued after the enactment of the Act. In other words, both the inclusion and amounts of those thresholds were discretionary.

All deep water leases issued by the MMS in 1996, 1997, and 2000 after the enactment of the Act included price thresholds. Leases issued in 1998 and 1999 did not.

In February 1996, during the development of the regulations promulgated to carry out the Act, MMS asked the public in its advance notice of proposed rulemaking the following: "for tracts offered in upcoming sales, should price ceilings affect suspension volumes as for existing leases and units (pre-Act leases and units for which price ceilings were mandatory under the Act)?" A number of commenters responded that they believed the ceiling prices only applied to existing leases and that price ceilings should not affect new royalty relief.

Despite this commentary, there was no discussion of these comments or the issue at all in the interim rule issued March 1996. The one comment received on the interim rule did not address the issue of price thresholds. And again, the issue of price thresholds was not addressed in the final rule issued in January 1998. The final rule primarily focused on the policy decision made by the last Administration to award suspension volumes on a field basis rather than a lease basis. This interpretation did not later withstand court challenge.

The Subcommittee on Energy and Resources has referred to the final rule as a "faulty regulation" because price thresholds were not addressed. However, the documents gathered for this Committee's investigation show that the previous Administration made a policy decision not to address price thresholds in the regulations, but rather to include these thresholds in individual lease sale documents. The previous Administration decided instead to reserve to the MMS the discretion to vary royalty suspensions under the Act in any manner it saw fit so long as the price thresholds, if any, were specified in the Notice of Sale published in the *Federal Register*

Based on the documents we have before us, it appears as though it was not until February 2000 that the missing price thresholds for 1998 and 1999 leases were noticed by the MMS. In an e-mail provided to the Committee dated February 22, 2000, Marshall Rose,

Chief Economist for MMS, mentions to Ms. Kallaur that the issue of the missing price thresholds in the 1998 and 1999 leases should be raised the next day at a meeting with the Director. Shortly thereafter the proposed addendum for Lease Sale 175 was revised to include specific price thresholds. Less than a year later, Ms. Kallaur provided the explanation quoted above. However, the Inspector General's investigative report may shed more light on the timing and awareness of all appropriate individuals.

Discretionary Relief for Deep Water Leases Issued Beginning in 2001

The mandatory provisions of the Act expired in 2001. The Department chose to continue deep water royalty relief, with modifications, for Gulf of Mexico lease sales under the Act's discretionary provisions, but has taken a conservative approach. The amount of royalty relief allowed on new leases was reduced. With some revisions in subsequent years, the royalty relief program was changed to eliminate relief in shallower water depths (200-400 meters) and to set suspension volumes of 5 million to 12 million barrels of oil equivalent for each lease, depending on water depth. These relief volumes are substantially less generous than those offered under the mandatory provisions of the Act. In all deep water leases issued since March 15, 2000, price thresholds have been included that eliminate royalty relief when oil and gas prices are high. At today's prices, royalties are due on any production from these leases.

Deep Water Royalty Relief Mandated under the Energy Policy Act of 2005

In 2005, in the Energy Policy Act, Congress extended and expanded the deep water royalty relief program. It affirmed the suspension volumes the Department had set administratively, mandated a greater volume of relief for the deepest waters (16 million barrels of oil equivalent in water depths greater than 2000 meters), and required that MMS use these suspension volumes for leases issued in sales held during the next 5 years. It also continued the policy of limiting royalty relief based on market prices, and expressly reaffirmed the Secretary's authority to do so.

Improvements at the Department of the Interior

As I mentioned above, since 2000, all leases issued with deep water royalty suspension provisions have included lease addenda that specifically include price thresholds. Today, addenda text for each Gulf of Mexico Region (GOMR) lease sale is finalized only after a thorough review and consensus process is completed and documented. In addition, each Proposed and Final Notice of Sale and associated Royalty Suspension Provisions document receive detailed review and scrutiny by several offices in the GOMR, MMS Headquarters, and the Office of the Solicitor to ensure completeness and accuracy, especially from a price threshold perspective.

For recent sales, MMS has formalized a process of conducting all reviews in writing through the use of emails. Furthermore, MMS is placing paper copies of those emails in its official lease sale file as a record of these reviews and decisions. MMS is developing written standard operating procedures to ensure that these improved processes continue,

even if staff changes occur for reasons such as job reassignment or retirement. In addition for better documentation of the review process, we will also require that the Regional Director be formally briefed on the proposed contents of a notice of sale at both the proposed and final notice stages. This briefing will focus on any new items added to the sale notice, any removals from previous sales, and any modifications of language.

The Department is also ensuring that price thresholds are included in its regulations. Price thresholds were included in the 2002 Deep Gas in Shallow Water final rule and appropriate thresholds will be included in the regulations for any future royalty relief changes, including implementation of the royalty relief provisions of the Energy Policy Act of 2005.

In summary, under our supervision the situation that occurred in 1998 and 1999 has not happened again, and we are working diligently to make certain that it will not happen during future administrations.

Negotiation of Revisions to Leases

The terms of a lease on the OCS are issued by the MMS and are not subject to negotiation by prospective lessees. Before a lease sale, MMS publishes the terms of the lease; first, at least 90 days before the sale in the Proposed Notice of Sale and then in the Notice of Sale issued at least 30 days prior to the sale. In the Notice of Sale, MMS provides a listing and a map of blocks available for lease, along with the terms of the sale. The terms include the per-acre minimum bid, the per-acre rental rate (which is charged until production begins), the royalty rate, any royalty relief and the terms thereof, including applicable price thresholds, and any stipulations as to environmental or other restrictions tied to specific blocks. After the sale, usually within 90 days, companies that submitted the high bids are notified whether their bid is accepted or rejected as inadequate. If accepted, the lease document is created by including the lease terms that were published in the Final Notice of Sale. The lease document is signed by the MMS OCS Regional Director and a representative of the lessee.

The Administration believes that the federal government must be a reliable business partner and must honor its contractual obligations, even when in retrospect the terms of those contracts appear unfavorable. The Administration, in a Statement of Administration Policy on H.R. 4761, the proposed "Deep Ocean Resources Act of 2006," strongly opposed efforts in the Congress to force certain companies to renegotiate these contracts or face a "conservation fee." The Department is engaged in voluntary negotiations with regard to the 1998 and 1999 leases that lack price thresholds. On June 30, 2006, MMS Director Burton sent letters to all 55 companies that own interests in these leases, inviting each of them to come in and talk to MMS to see if we can reach a mutual agreement that would resolve the price threshold problem. Approximately 20 of the recipients responded to the letter. To date, approximately half of those have met or have scheduled meetings with Departmental representatives.

Overall there were 1,032 deep water leases issued in 98-99. Our most recent data indicates that approximately 17 of these leases are currently producing; approximately 27 leases have indications of discovery that are not yet producing; over 500 leases are still active with no indications of discovery at this time, and over 450 leases have been relinquished or have expired at the end of their lease term. If a lease is not producing or has not had an appropriate level of activity that may lead to production, it will automatically expire at the end of its term, unless an approved suspension is issued.

As a result of our early discussions and, in preparation for follow-up meetings and further initial meetings with more lessees, we have developed proposed terms. We believe that a voluntary negotiation process is a fair and appropriate way to resolve the price threshold problem for the 1998 and 1999 leases and is consistent with the overall objectives of the Act.

Responsive to the Committee

I wish to address the August 3, 2006 letter sent by the Committee and Subcommittee on Energy and Resources which alleges that the Department of the Interior might not share the Committee's sense of urgency with regard to its investigation of the missing price thresholds. That letter also alleges that critical information might have been deliberately held back from the Subcommittee. Neither allegation is correct. As Secretary Kempthorne told Chairman Davis when he called him immediately upon receipt of this letter, the Department has no interest in hindering in any way the investigation into this matter. In mid-August, full Committee staff met with MMS Director Burton and with Departmental staff and was briefed on our efforts with regard to the production of documents. We believe those briefings have put this issue to rest.

The Department looks forward to reviewing the report of the Inspector General and this Committee. We believe we have in place a system today under which the events of 1998 and 1999 would not reoccur. If there are recommended improvements that we have not yet made, we are open to considering and implementing them.

Department of the Interior Management and Ethics

We recognize that problems of accountability and inappropriate performance do surface in individual instances across a bureau that spans 2,400 locations, thousands of contractors, and 70,000 employees who manage one in every five acres of the United States. The Department takes such actions seriously and strives to address them consistent with specific circumstances and in accordance with the law.

In particular, Interior takes seriously recommendations identified in audits, whether from internal or external auditors. We also actively seek to identify problems in ethics, accountability, and management.

Consider financial management. In 2001, we inherited 170 material weaknesses in program or financial controls. Since that time, four new weaknesses have been identified,

while we have corrected or downgraded 170 material weaknesses. These weaknesses, identified through the annual financial audit, are reported in the Department's Performance Accountability Report. Five years ago, the Department required nearly 5 months to complete its annual audit; for the past two years, the Department has completed the audit within 45 days of the close of the fiscal year and received an unqualified clean opinion. We continue to implement corrective actions for the 4 material weaknesses that remained as of the end of FY 2005; however, they are more complex to resolve, involving issues such as Indian trust as well as agreements between the Department and other agencies.

In addition to financial audits, we record all management and other recommendations generated by Interior's Office of the Inspector General and track our actions to address those recommendations. As of June 7, 2006, actions on 90 percent of all recommendations issued by the Office of the Inspector General (OIG) in FY 2005 had been initiated. The Department, on a quarterly basis, works with the Inspector General to reconcile the Department's data base with the Inspector General's data base pertaining to the number of outstanding recommendations and actions taken.

Recently, when the Inspector General raised concerns regarding whether corrective actions were being taken to address his office's findings, I immediately asked the Department's Office of Financial Management to provide a status of recommendations issued by the Inspector General in 2004 and 2005 and work with the Inspector General to reconcile any differences. We are continuing to work on this reconciliation. We are also expanding our review and oversight related to internal control issues to ensure follow up and additional supporting information related to corrective actions. These efforts will continue to improve our management environment and the consistency of our data with that of the Inspector General.

The Department established a management excellence performance goal that annually requires implementation of 100 percent of the audit recommendations scheduled for completion in that fiscal year. This performance goal includes recommendations from the Inspector General, Government Accountability Office, and financial audit. The goal is included in Senior Executive Service performance agreements of Chief Financial Officers and executives in all bureaus and offices responsible for program management. We report results for this goal annually.

Ethics. When Secretary Norton assumed office in 2001, the Inspector General reported to her the results of a 1999 management assessment of the ethics program. Subsequent to that and in consultation with the Office of Government Ethics, the Department made significant changes in its ethics program. A new director of the Departmental Ethics Office was selected, and the office was moved to the Office of the Solicitor. Weekly meetings now occur between the Departmental Ethics Office and the Chief of Staff, Deputy Chief of Staff, and the Deputy Solicitor to discuss ethics issues of both an individual or programmatic nature. The Department's Ethics Office has impressed upon Interior's bureaus the importance of having full-time ethics program managers at the headquarter level who, in turn, work with duly delegated ethics officials in field offices in

the management of the program and delivery of services to employees. In the last four years, a number of the bureaus have designated full-time headquarters ethics program managers.

In December 2004 and January 2005, the Office of Government Ethics conducted a programmatic review on the Department's Ethics Office, as well as the ethics programs at the U.S. Geological Survey, Minerals Management Service, and Bureau of Reclamation. The final report specifically stated that all written ethics advice reviewed during the audit was consistent with the law and responsive to employees' needs. The Department's Ethics Office has implemented all program efficiency recommendations contained in the report and is continuing work on an additional recommendation concerning the revision of supplemental ethics regulations. The three bureaus covered in this report also completed all of the Office of Government Ethics' recommendations for improvement.

In late 2005, the Office of Government Ethics initiated a program review of the National Park Service's (NPS) ethics program, issuing a report earlier this year. The recommendations contained in this report have been fully implemented where possible, and others are near completion. The review pointed out that the NPS program exceeds requirements for employee ethics training. Additionally, Interior has contracted to perform internal assessments for the Bureau of Indian Affairs, the Fish and Wildlife Service, and the Office of Surface Mining Reclamation and Enforcement. With this work, all of Interior's bureaus will have been reviewed formally by the Office of Government Ethics or internally by the Department's Ethic Office within the last two years.

A major component of a robust ethics program is training, including the required annual ethics training for employees. Interior provides a variety of mechanisms for employees to meet the annual training requirement: live classroom, computer-based modules, written materials, and live satellite broadcasts. In 2005, our ethics office also developed and delivered training geared to investigators and auditors in the Office of Inspector General in order to ensure a better understanding of the elements of statutory and regulatory violations. Finally, in support of a stronger Department-wide ethics program, the Department's Ethics Office conducted two "Train the Trainer" sessions for field ethics counselors in Denver and Phoenix early in 2006, reaching about 75 ethics counselors across bureau jurisdictions. The goal of these programs was to ensure consistent management of the ethics program and consistent interpretation of the ethics rules in response to employee inquiries.

In short, during this Administration's tenure, the Department's Ethics Office has grown in stature from being an office centered on narrow delivery of service to individual employee questions to a broader mission of ensuring soundness of all bureau ethics programs and Departmental initiatives. Interior employees are now afforded ample access to qualified officials who give consistent advice. In raising the visibility of this office and making ethics a part of the workplace, this office is now consulted in a variety of matters where it previously was not. This leads to a coordinated and thoughtful review

of ethics issues at all levels of the Department, ensuring the operation of a robust ethics program.

Under the leadership of Secretary Kempthorne, the Department continues to strengthen its efforts to meet the highest standards of ethical conduct. Among his first actions on day one in the Department was to meet with the Ethics Office and the Inspector General. Secretary Kempthorne meets regularly with the IG. Over the past five years, I and other senior departmental leaders have also met regularly with the IG and have strived to advance management improvements based on his reports and recommendations.

Appraisals. Our performance process has resulted in significant management improvements. In 2002, the Inspector General found fault with the Department's appraisal methodology. The Department then created an interdepartmental body, the Land Transaction Working Group, comprising of assistant secretaries and bureau directors with land management responsibilities. It promulgated a set of broad land transaction principles underscoring the need for integrity, good faith, transparency, and other basic considerations necessary to assure public confidence. These principles were approved by the Secretary and are now in effect.

The Working Group concluded that significant restructuring was necessary and recommended the consolidation of appraisal functions performed by bureaus in a new Departmental office. Secretary Norton approved this recommendation and announced the Department's intent on June 19, 2003. She cited the need for "fundamental reform," stating that "our new organization will change the way we do business and will gain the respect of both the public and the dedicated professionals in our appraisal and realty programs." The reorganization was widely praised as addressing an issue that had been repeatedly raised by auditors and others for some 50 years.

The Department now has a new Office of Appraisal Services (OAS). Appraisers working in bureaus were transferred to the new office. The Office is headed by a Departmental chief appraiser – a new position – to whom all appraisers in the field report through a regionally based structure, including seven regions, each headed by a regional supervisory appraiser. This change in reporting structure—appraisers reporting to appraisers rather than to those responsible for making transactions—is a crucial change. Through the creation of the appraisal office, the Department met important management objectives to:

- enhance or restore public confidence in the Department's appraisal functions and land transaction processes in general;
- respond to bureau realty priorities;
- promote good government;
- avoid disruption to employees; and
- assure the efficient use of taxpayer dollars.

Law Enforcement. In March 2001, Secretary Norton asked the Inspector General to conduct a comprehensive assessment of law enforcement within the Department to

identify organizational and management strategies that might be adopted to address issues that affected law enforcement across the Department. The Department has nearly 4,000 law enforcement officers assigned to seven distinct organizational units within five bureaus: the National Park Service, Bureau of Land Management, Bureau of Indian Affairs, Bureau of Reclamation, and US Fish and Wildlife Service.

The Inspector General conducted the assessment and issued its report in January 2002. It found that having seven different programs had created a lack of organizational structure, which led to a void of leadership, coordination, accountability, and central point of contact at the Department level. The law enforcement programs had no single advocate and no informed senior law enforcement official to offer advice and recommendations to senior management. Without a centralized facilitator, Departmental initiatives had not been implemented, and coordinated law enforcement efforts were rare.

The bureaus had been operating their programs with minimal Departmental oversight and direction. Each bureau had near total autonomy with the ability to determine law enforcement priorities, funding, and investigative direction. In addition, in the three years prior to the January 2002 report, Interior had spent in excess of $1.5 million to have law enforcement programs assessed by consultants only to have the thoughtful recommendations advanced by these professional law enforcement and management experts largely ignored.

The Inspector General's report confirmed and validated the findings of many of the reviews, evaluations, and assessments that preceded it. The report made 25 recommendations for improvement. To accomplish one of her principal objectives—"develop and maintain the most professional, modern, and effective law enforcement capability in a civilian government agency"—Secretary Norton convened a Law Enforcement Review Panel, comprising of senior leadership of the Department and bureaus, to evaluate the report and make recommendations to the Secretary regarding implementation.

In July 2002, Secretary Norton approved the 25 recommendations of the Review Panel and directed that the Department and bureaus implement them. Also in July, the Department created and filled the Deputy Assistant Secretary for Law Enforcement and Security position, essentially creating the Office of Law Enforcement and Security, the entity charged with implementing all of the remaining Secretarial Law Enforcement Directives.

In August 2003, the Inspector General issued a progress report on implementation. The progress report found eight directives had been fully implemented and seventeen ranged from limited to reasonable progress made. It concluded that significant progress had been made; the establishment of the Deputy Assistant Secretary for Law Enforcement and Security and increased staffing within the office had served to professionalize the Department's law enforcement programs, as well as the establishment of senior law enforcement managerial positions in all the bureaus. However, accountability for programs and personnel remained to be adequately addressed. Other concerns included a

lack of the development of staffing models, efforts to increase officer safety, and the lack of attention to initiating internal affairs programs.

In April 2006, the Inspector General issued a second progress report finding that nine of the directives had been fully implemented, twelve were in progress, and three showed inadequate progress. The report concluded the Department has continued to improve its law enforcement programs, though not at the pace the Inspector General would like. The Department still must balance its role of providing policy and oversight of bureau law enforcement, security, and emergency management programs with the mission specific needs of each law enforcement entity. The Inspector General pointed out that some of the bureaus need to fully commit themselves to full implementation of a number of directives.

Overall, however, in tackling the issues related to law enforcement, this Administration has taken on a deficiency that existed in the Department for many years. We have made significant progress in establishing a professional law enforcement and security program.

Conduct and Discipline. Based on a recent evaluation of conduct and discipline at Interior, the Inspector General has noted a perception by employees that a significant amount of misconduct is not being reported and that discipline is administered inconsistently and unfairly in the Department. The Inspector General reported that disciplinary measures are not taken when needed and that, without intervention, inconsistent discipline would become increasingly problematic for the Department.

We took these findings seriously and immediately prepared a comprehensive action plan to address the Inspector General's recommendations. Using that action plan, we have:

- Sent a memorandum to each employee communicating the steps to be taken in addressing the Inspector General's findings in order to better implement our Conduct and Discipline policies;
- Updated our Conduct and Discipline policy and published it in the Departmental Manual on the Interior website.
- Planned for 2007 a comprehensive strategy for managing conflict and resolving disputes that arise in the workplace. Through ongoing education, training, and resources, we expect to reduce confusion and miscommunications that surround conduct and discipline issues.

Currently, the Department is conducting training sessions for supervisors and senior managers regarding the use of the new Conduct and Discipline policy. In fact, this topic will be addressed in multiple sessions at the Department's Human Capital Training Conference next week that will be attended by approximately 400 of its human resources, civil rights, and employee development professionals.

Meanwhile, the results from the Federal Human Capital Survey administered by the Office of Personnel Management shows that the response by Interior employees to questions about fair resolution of complaints and grievances and fear of reprisal in the

workplace were not significantly different from several other Cabinet level agencies. For example, when asked whether complaints were fairly resolved in the employees' work unit, our employees' responses placed us in about the middle and well ahead of eight other large Federal agencies. When asked whether they could report a suspect violation without fear of reprisal, Interior's response placed it behind of some agencies and again well-ahead of several others. This is not to say that Interior is without problems. It does signal, however, that when Interior identifies a problem, whether in morale, conduct and discipline, appraisals, or in any of the other examples highlighted in my response and the many more which I could have highlighted, time permitting, Interior works proactively to solve the problem and its efforts place it well within the mainstream of other Federal agencies.

Worker's Compensation. In May, 2005, the Inspector General released its evaluation of the Department's implementation of the Workers Compensation Program. Overall, the Inspector General found that Interior must assume more active responsibility for management of its own workers' compensation cases. Costs have continued to rise, exceeding $58 million for the last two fiscal years. Increases are due to three factors: (1) payroll increases and increased medical costs; (2) increases in the total number of people receiving workers' compensation, and (3) limited success analyzing and managing short- and long-term disability cases.

The Inspector General's findings and recommendations are being aggressively pursued. The Department has hired a full-time, national program manager at the Department level to focus on this program. We are also creating consistent and comprehensive policies and procedures for use throughout the Department, emphasizing accountability for workers' compensation costs at the field level. We plan to train existing employees to better perform their jobs and focus on maintaining fully documented, up-to-date case files.

Facilities Management. This Administration has undertaken a major effort with respect to facilities management. Interior's real property inventory includes approximately 46,200 buildings and 101,890 structures, a portfolio second only to the Department of Defense. Our facilities portfolio includes wastewater treatment plants, dams, electric generating facilities, hotels, campgrounds, roads, boat docks, stables, and even landfills. In 2001, we realized there was no objective measure for determining the condition and needs of the assets we held. Indeed, the Department had never developed a complete inventory of its facilities.

The infrastructure of the National Park System alone includes more than 26,000 historic structures and other buildings, an estimated 8,500 monuments, over 12,000 miles of trails, some 1,200 water systems, about 1,400 wastewater treatment plants, and more than 5,000 employee housing units. The road network consists of nearly 5,500 paved miles of road, an estimated 6,000+ miles of unpaved roads, and some 1,700 bridges.

An investment in a state-of-the-art facility management software system has allowed the National Park Service to develop a facility management strategy for the 21st century and

generate information about its assets across the organization. Its first cycle of assessments should be completed by the end of 2006. In addition to software investments, the National Park Service now is developing an inventory of all assets and cyclic evaluation of the condition of those assets. Parks are able to identify any deficiencies that need to be addressed in order to bring a facility to a satisfactory condition and extend the useful life of the asset. The software links to an industry-standard, cost-estimating tool so that the cost to repair the asset is determined immediately. We are now able to evaluate the impact of particular funding levels on asset performance and condition. This capability is transforming our asset management to the great benefit of the American taxpayer and visiting public.

This information allows the National Park Service to measure progress against the industry-standard measure of a facility condition index for buildings and the pavement condition rating for roads. We now can gauge the results of investments in our assets.

In addition, building on a five-year effort, the Department has now issued a Departmental asset management plan. The plan presents a strategic vision and plan of action for managing owned and leased buildings, structures, linear assets, motor vehicles, and non-stewardship land used for administrative purposes.

We have made great strides in facilities and asset management. Serving the public well means knowing what we have and managing it well. Using the tools mentioned above, the National Park Service has completed, undertaken, or planned some 6,000 projects to improve its facilities and roads. The Bureau of Indian Affairs is now using similar information to plan and manage school construction and maintenance projects.

Integrated Charge Card Program. Beginning in 1998, because of changes made by the General Services Administration to the credit card program, Interior saw an opportunity to re-engineer our business practices. A cross-functional team was established that is still functioning. Since that time, we have created a detailed policy regarding government-issued charge cards. We have put system controls on all accounts, required training for all cardholders and approving officials, and established reports to monitor activity. In addition, we have a process in place to refer suspicious activity to the Office of Inspector General.

Interior's integrated charge card program is unique in the Federal government. By combining three separate charge card programs—purchase, travel and fleet—into one program, we were able to:

- Eliminate redundant accounting processes;
- Improve monitoring by combining all account transactions into one data base; and
- Solve the problem of reconciling burdensome airline ticket invoices.

We have taken aggressive action to minimize the potential for misuse and fraud. We have created account controls by placing authority and spending limits on accounts. We have developed and instituted three on-line training courses for cardholders, approving officials, and agency or organization program coordinators participating in the integrated

charge card program. Each training program instructs participants in their roles and responsibilities and the proper use and management of the charge card. We appoint approving officials that assist in carrying out duties under the program.

In addition, to assist in managing the program, the Department's Charge Card Management Team worked with Bank of America to create a series of electronic reports. These reports help us identify potential misuse, manage delinquency, and track spending. We also require bureaus and offices to perform periodic reviews (no less than biennially) of the program. Specifically, they are to examine whether the number of cardholders with purchase authority and cardholder spending limits should be adjusted. A review of the charge card purchase business line is included in bureau acquisition management reviews.

When problems with this program are identified, the Department takes the appropriate action, including removing employees from Federal service. Several cases have been successfully prosecuted, and the employees involved have had to make restitution and serve jail time. As a result, the delinquency rate for Interior travel charge cards is well below that of the government-wide average.

Centralization versus Decentralization. Questions have been raised as to whether a Department with eight distinct bureaus having sometimes very divergent missions can be properly managed. I believe the answer is yes. While our bureaus have distinct missions, those missions also share many common programmatic and administrative features. We house within the Department of the Interior the National Park Service, the U.S. Fish and Wildlife Service, the Bureau of Land Management, the Minerals Management Service, the Office of Surface Mining, the Bureau of Indian Affairs, the U.S. Geological Survey, and the Bureau of Reclamation. Each of these bureaus has a need for specific skill sets to carry out its mission.

One of the challenges of the leadership at Interior is balancing between the need to coordinate the activities of these bureaus while ensuring that the mission specific requirements of the bureaus are met and are met in a way that recognizes the needs and concerns of our partners on the ground, including Indian tribes, local and State governments, and the broad range of groups and individuals affected by our actions. Each of our bureaus has statutory authority vested in the Director of that bureau to carry out varying activities and programs.

In determining the appropriate organizational and management structure to carry out shared functions such as law enforcement, appraisals, human resource training, financial management, and so on, we carefully evaluate the benefits of fully centralizing functions versus maintaining coordinated policies that are then implemented through individual bureau structures. For some information technology systems and management, we have moved toward centralized purchasing to achieve economies of scale and improved security. For appraisal services, we have created a centralized office with regional affiliates. For law enforcement, we have created a departmental coordinating structure while retaining law enforcement structures within the relevant bureaus. Each of these structures was carefully selected based on an evaluation of management efficiency and

programmatic and functional effectiveness. Consider law enforcement. The U.S. Park Police has a different mission and therefore different needs than the Bureau of Reclamation's law enforcement officers. We apply common management principles to all law enforcement, but each of these forces needs to be particularly attendant to its respective mission. Our bureaus must be able to connect with their customers and work effectively with their partners on the ground.

All large, multi-unit organizations faced challenges of finding the right balance between centralization and decentralization. Any book on management theory will tell you that centralizing control of operations can sometimes result in cost reduction, reduced duplication, and improved consistency. However, there are disadvantages as well. The flexibility of an organization to respond to local issues and needs is often compromised; centralization can result in cumbersome processes and detachment from on-the-ground management needs. By removing control from bureaus, a shift may occur in decision making that results in decisions made by managers far removed from the realities on the ground. Obviously, every organization needs to operate with a balance between these two tensions and finding that balance can be difficult.

You should know Mr. Chairman that these are issues the leadership at Interior grapple with on a daily basis. This Administration has brought much needed management change to the Department of the Interior. I believe that record has yielded significant management improvements that benefit the American public. In an organization with the size and reach of the Interior Department, unanticipated and unacceptable decisions and actions may sometimes occur. We take such actions extremely seriously and strive to address them. I would be happy to answer any questions you might have at this time.

Chairman TOM DAVIS. Thank you very much.

In your written testimony, you state the price thresholds are discretionary for deepwater leases. If this is the case, what legal review occurred with the 1998 and 1999 deepwater leases? What I am asking is were there attorneys at Interior who analyzed the leases themselves to determine whether the Secretary had exercised his discretionary authority to include price thresholds? Or if the Secretary had deliberately decided not do to so?

Ms. SCARLETT. Mr. Chairman, I will ask Johnnie Burton, the Director of Minerals Management Service, to answer the detailed questions about the 1998 and 1999 leases.

Chairman TOM DAVIS. That is fine.

Ms. BURTON. Thank you, Mr. Chairman.

We are not sure what happened. We did look at it, and we arrived at some conclusions, but because we could not actually be sure what happened in 1998 and 1999, this is why we asked the Inspector General to run an investigation and tell us what he could find. We don't have his report yet, but I can tell you what we saw from our perspective.

What we did see was in 1995, Congress passed a Deepwater Royalty Act and it had to be amended right away. There was an interim rule that was put together where the price threshold had to be determined. That takes quite a bit for the Economics Division to arrive at the proper level, and so they had decided at that time in 1996, shortly after the bill was passed, to put the price threshold in an addendum to the lease. By the way, someone asked who writes the lease. The lease is a form we get from OMB. We don't write it. This is a standard Government form.

So if we have very specific provisions for that lease, which is the case for royalty rate, for a cap on what is acceptable as a bid, for rental, etc., we put that in an addendum to the lease. So in 1996, it was put in an addendum to the lease prior to the rule, but as the rule was being developed, it also was placed there in 1997.

By early 1998, January 1998, the rule was final. The rule was issued. Now, this is all conjecture on our part, but what we can see is that in 1998 when the rule was issued, there were no thresholds in the rule. The staff had been used to putting the threshold in the lease. However, when the rule became final, that same staff assumed that the threshold would be in the rule because it had been discussed. What they didn't know is that the associate director of the off-shore program had made the decision not to have the threshold in the rule, but continue having it in the lease. And there was, so far as we can tell, miscommunication between those two units.

What I wanted to know is whether or not that miscommunication was intentional or not. This is why I asked the Inspector General to run an investigation. He has kept me apprised.

Chairman TOM DAVIS. We had him up here yesterday.

Ms. BURTON. So you know he has not finalized it.

Chairman TOM DAVIS. A critical question that this just begs is whether the Secretary at the time intended not to exercise his authority to include the thresholds. Do we know the answer to that?

Ms. BURTON. We do not, sir. I don't know what Secretary Babbitt decided at that time.

Chairman TOM DAVIS. OK. We have the IG report coming and we are going to be doing more on that. You are present now at lease negotiations, aren't you?

Ms. BURTON. Yes, sir.

Chairman TOM DAVIS. Would you have been in a better negotiating position had you renegotiated the leases when the missing price thresholds were discovered in 2000?

Ms. BURTON. I am not sure I can answer that question, sir. I don't know what the previous directors did.

Chairman TOM DAVIS. Let me ask you this. Would we have been in a better position had we disclosed these problems in 2000 instead of hiding them for 5 years?

Ms. BURTON. I suppose we could have been in a better position if they had realized what mistake had been made. It seems to me that when they realized it in 2000, I don't know how they handled it. Did they think it was a mistake? Was that done by the Secretary? I don't know.

Chairman TOM DAVIS. Can you give me the status? Mr. Markey raised this in his comments. Mr. Issa has raised it. What is the status now of negotiations with oil companies concerning the lease price thresholds? They came before the subcommittee under oath and, oh yes, we will renegotiate. What is the status right now? Can you give us a broad status?

Ms. BURTON. Yes, sir. I have been contacted either by phone, by letter, or in person by roughly 20 companies. I think I have personally spoken, I mean, they came to the department maybe about 10 of them. We have developed an agreement, a standard agreement for them to come to attach to their share of the lease. They are thinking about it, and we are still talking to them, so we are right in the middle of the discussions.

Chairman TOM DAVIS. Does this include all the companies? I mean, some of these have leases that aren't producing anything. Some have leases that are producing a lot. Does this include everybody? Is there anybody who isn't coming to the table?

Ms. BURTON. Out of 55 companies, we had about 20 that contacted us. Now, what I don't know at this point is whether the others that did not contact us, whether their leases have been relinquished, whether they have expired, so I don't know.

Chairman TOM DAVIS. We need an inventory of all these leases, who is renegotiating, when they expire, and that will give us a pretty quick line, and then Congress can decide if we need to take action. We may not be able to come back and look at the current leases, but we have power over future leases and other things we can do.

I just think it is just, with the price of oil having gone up so significantly, and the companies making record profits and so on, that this is an appropriate time for them to show some faith and give back a little bit for the royalties and the omissions in the earlier leases. We can exhaust it ad infinitum today, but what we need is a chart showing the status of this, who is talking, who isn't talking, and then we will work with you I think to completion.

Ms. BURTON. And you might be interested, Mr. Chairman, in knowing that about 17 of those leases are producing today. Roughly 27 have indication of discoveries, but we don't know whether they

are producible or not, and nothing has happened on the others. Over 400 have already been turned back into the pool, which means they will be released.

Chairman TOM DAVIS. And all the new ones, of course, you have priced thresholds in?

Ms. BURTON. Oh, yes, sir. And we have thresholds on all of them since 2000.

Chairman TOM DAVIS. I would note there is an ongoing IG investigation on the Oregon issue, and GAO is doing an in-depth review of raw data and assumptions in the MMS revenue projection, so hopefully we can all work together to get to the bottom of this. This literally is millions of dollars for the Federal treasury, literally, so we are trying to get this resolved as quickly as possible.

Mr. Waxman.

Mr. WAXMAN. Thank you, Mr. Chairman.

Yesterday, the Inspector General for the Department of Interior, Mr. Devaney, issued a scathing indictment of senior officials in charge of the department. He discussed ethics failures on the part of senior department officials. He discussed department leaders' refusal to take any action against those officials or to change the ethical culture of the department. He discussed how top Interior officials disregard the IG's findings, responding to serious allegations by trying to discredit or undermine his office's work. He discussed the ongoing evasive and corrosive nature of these problems and how they are destroying the morale of agency employees and the trust of the American people.

Ms. Scarlett, in your testimony, you say you disagree with the IG's characterization of your department. Let's take his concerns about ethics failures in high-level officials. What has the department done in response to specific incidents raised by the Inspector General?

Ms. SCARLETT. Yes, thank you, Congressman. I meet regularly with the IG every week or every other week. We go through various of his recommendations and vigorously strive to implement them as fully as we can. While I can't talk in this public setting about the specific personnel matters which seem to be at the root of some of his comments yesterday, concern about recommendations made on the disposition of investigations of individuals, I will say, for example, that in one recent instance where he investigated various people associated with a programmatic failure and recommended actions on eight individuals, three of the individuals actually left the department before we had an opportunity to act, but in the other cases we took actions on all five.

Mr. WAXMAN. Let me ask you this. You say you can't discuss some of these matters because they are personnel matters and are not public. But the Inspector General thought some of the conduct was so egregious that it was appropriate to make the matter public so the names and violations are already out there. Are you trying to tell us that you can't publicly discuss the department's response to some of these public allegations?

Ms. SCARLETT. I am not aware in his testimony that he addressed specific individuals.

Mr. WAXMAN. Well, let me tell you about specific cases. For example, in November 2005, the IG released a report on the tragic

death of a 16 year old at the Chemawa Indian Boarding School. The IG found that the inaction on the part of senior officials was a significant factor in the death, and he recommended administrative sanctions. According to the IG, there was a historical pattern of inaction and disregard for human health and safety at this Government facility. He pointed to senior officials in the Bureau of Indian Affairs who were repeatedly told of these problems, but failed to take action that might have prevented this death, as well as the endangerment of countless other students. Was anyone fired in that incident?

Ms. SCARLETT. That is the specific incident actually that I was referring to. In that particular instance, there were eight individuals that were identified. As I noted, several left before the report was completed, and we took action in the instance of the other five. We proposed dismissal actions. As you are aware, through due process requirements, employees have an opportunity to appeal, and through that process some alterations in the ultimate disposition occurred, but we believe we followed through on the IG's actions as appropriate.

Mr. WAXMAN. So none of them were actually fired because they asked for their due process rights, and then you had a plea agreement with them?

Ms. SCARLETT. I believe that there were some recommendations for dismissal, but I would have to go back and check specifically.

Mr. WAXMAN. Was anybody suspended without pay?

Ms. SCARLETT. I would have to check on that specific matter.

Mr. WAXMAN. Anyone demoted?

Ms. SCARLETT. Again, as I said, we took action on all eight, including recommendations for dismissal. I would have to go back and see the specifics of how many were either dismissed and/or demoted.

Mr. WAXMAN. Well, it is curious that you knew about this specific incident, but aren't prepared to give us the facts of it. A girl died and there were no real consequences. I think the IG's concerns about the Department's lack of response are pretty compelling.

Let me ask you about another example. Earlier this year——

Ms. SCARLETT. Congressman, I have it right in front of me. Specifically, discipline actions were proposed on five of the eight employees named in the IG report. In the other three cases, no actions could be taken because the subject employees no longer worked for the Bureau of Indian Affairs. Indian Affairs proposed the removal of two other supervisory employees in addition to those listed as culpable in the IG report. After the appeal period, one was exonerated and the second was removed. So that is the detail of that specific case.

Mr. WAXMAN. So one was actually fired, successfully?

Ms. SCARLETT. No, sir. I said five of the eight had actions taken against them. Of the two supervisory, one was found not culpable and one was dismissed. The details of the five others, I would have to find, sir, specifically the actions.

Mr. WAXMAN. Well, my time is up, so perhaps you could put it into the record. I would like to know what actions were actually taken in the incident.

Ms. SCARLETT. We will do that for you.

Mr. WAXMAN. Thank you.

Mr. ISSA [presiding]. Thank you, Mr. Waxman.

I am sure we are going to need a second round here. This is informative for us, and I hope you will understand that we share in the responsibility. I don't think on this side of the dais, anyone is implying that your failures aren't also the failures of our oversight committee, of the laws and rules and regulations, even the process for terminating employees.

On one question, though, on those eight employees, as far as you know, all of those employees would be eligible to work in the Federal Government today? None of them are barred from starting somewhere else and continuing their Federal career. The ones who quit, the ones who had reprimands, even the one who was fired can basically go somewhere else and be back in the Federal system in a substantially similar role. Isn't that true?

Ms. SCARLETT. Sir, I don't know the details of that. In response to Congressman Waxman's larger question, we will add that response as well.

Mr. ISSA. I appreciate that, because that may be part of our oversight we need to change.

Director Burton, in what year did you learn of the failure of these price thresholds to be in the contracts?

Ms. BURTON. In 2006.

Mr. ISSA. OK. So basically you were one of those high-ranking executives that never got the word because it was sequestered at a lower level. Is that correct?

Ms. BURTON. I am not sure I would phrase it that way, sir. I think I would say that I didn't know about it because I arrived at the department in 2002, which was 4 years after this happened.

Mr. ISSA. And 2 years after the discovery had been made that they were missing, at lower levels.

Ms. BURTON. But the people that knew about it were no longer at the Department.

Mr. ISSA. Your Solicitor, Milo Mason, is at the Department today, madam.

Ms. BURTON. Yes, he is. He doesn't work for me. He works for the Solicitor. I did not review all the contracts that were issued before I arrived at the Department and there was no reason for me to ask of those specific years. I had no idea something was wrong with them.

Mr. ISSA. Isn't it true that, based on what the IG told us yesterday, that there were three people who were suspected of knowing it? There was testimony that one of the three had been told. My understanding is one of the individuals made a sworn statement, took a polygraph and passed it, saying I am not the one who knew. One made a sworn statement and refused to take a polygraph, and one refused to make a sworn statement and refused to take a polygraph. Aren't all three of those individuals, as far as you know, still working, and in this case, they are under your side of this problem?

Ms. BURTON. I do not know who they are.

Mr. ISSA. We will get you the names.

Ms. BURTON. I found out about this by reading the IG's testimony yesterday, but I don't know who they are. I assume if he said they are still working there, they are.

Mr. ISSA. This is one of my concerns, is that they continue to be in a position. This is something for our committee to look at, I am sure, as much as you. When somebody refuses to make a sworn statement before this committee, we don't let them testify. To be honest, as far as we are concerned, they shouldn't work any longer for the Federal Government if they are not willing to tell the truth under oath.

It appears as though that is not the case, under current rules of some of your fiduciaries that you deal with every day that have these responsibilities.

Mr. BILBRAY. Will the gentleman yield?

Mr. ISSA. Yes.

Mr. BILBRAY. It is not that they just refuse to testify. They are at the epicenter of the coverup.

Mr. ISSA. Absolutely.

Mr. BILBRAY. They are at the epicenter of the coverup. They fingered three people. One did testify, not only under oath, but took a lie detector. One testified, but wouldn't take a lie detector, and one refuses to do anything. I think the astounding thing to all of us on both sides here is we have a multi-billion mistake, albeit it was made before your watch, but nobody has been fired. Nobody has been reprimanded.

Mr. ISSA. I will give you just two of the names. We are going to get the third one for you, but Marshall Rose and Larry Slaznick. Do you recognize those names?

Ms. BURTON. Marshall Rose, certainly. He is the chief of the Economics Division. The other person, sir?

Mr. ISSA. Larry Slaznick.

Ms. BURTON. Slavsky.

Mr. ISSA. Slavsky, yes.

Ms. BURTON. OK.

Mr. ISSA. We will get you the third name. We are concerned because when there is that kind of clout, and I am only talking about the two who refused to take a polygraph, and certainly the one who refused to even give a sworn statement. I would have a hard time, and I have different rules for my employees, but I would have a hard time allowing somebody to be in that kind of position of trust when they basically say, oh no, I am not going to take a statement for which I could be held to a perjury standard. I can understand that. I just can't understand them still working for me in those positions of trust.

I realize you don't have the ability to terminate Milo Mason, but I am very concerned about something that the Secretary said. I am sorry, that Director Burton said, you said that a Deputy Director made the decision not to put it into the regulations. What was the name of that Deputy Director?

Ms. BURTON. The only thing I know, sir, is that I read a letter that was written, I think in 2001, by a lady named Carlita Colauer, who was there before I was there, so I don't know her, but she was Associate Director for OffShore. There is a paragraph in her letter that says that the decision was made not to put the threshold in the rule, to preserve flexibility to follow the market, so something to that effect. I am paraphrasing because I don't know the exact.

Mr. ISSA. OK. We would like to have that letter.

Ms. BURTON. Sir, it was sent to you.

Mr. ISSA. OK. We would like to have a copy of it so we can compare it with the stack of papers, because it appears as though we are, and I will tell you specifically that Milo Mason did not under oath, was not able to give us the name of somebody who said that this wasn't to be included. Just the opposite, he talked in terms of policy as though policy preempted the orders of the Congress. He wasn't able to give us the names. He talked in terms of, and to be honest, this is, Madam Secretary, why your statement that you have made reforms doesn't work.

The Solicitor today is still basically telling us when he testified here that you walk down the hall and you tap somebody on the shoulder and you ask them for a legal opinion, they give it to you, and you record nothing in writing. That is what was said here. I am paraphrasing, but that is what was said here. No, there are no e-mails. No, there are no memorandums of record. No, we don't keep paper on it. That is part of our problem at this committee. When we ask for a paper trail or something from the fiduciary, the lawyer who works for the U.S. Government, for the people of America, says, no, as a matter of course, we don't keep the paper.

So that is our challenge, is that is not corrected as of testimony before my subcommittee just a matter of about a month ago, with Congresswoman Watson who, since my time is up, I am going to grab a second round, but I very much want her to ask her questions because we have worked on this together hand in hand. I am going to close just by reminding you, from this Member's perspective, this is not about the oil. It is not about the money. It is about the trust of the American people in the agency that you operate.

We will work with you hand in hand to recover substantially all of the money that might otherwise have been lost in whatever way necessary, working within contract sanctity, with the oil companies. That is a promise from this person, and I have a better than average chance of being reelected, so I expect to be here. But we have to move beyond the question of the money on both sides of the aisle. This is about you leaving the agency that you are responsible for, and the entire Department of Interior as a place in which people can be proud, that coverups don't happen, that when a problem occurs, a mistake happens, it is quickly rectified.

With that, I would yield to the gentlelady from California, Ms. Watson.

Ms. WATSON. Mr. Chairman, I just want to thank you for identifying the issue. You remember we had that conversation several weeks ago. We got on it. We have had four hearings. What is confounding me is that this goes back 8 years. Why have we not corrected this and addressed this issue? And why have we not been able to recap those dollars that belong to the public?

I just can't understand why this bureaucracy cannot resolve this issue and get the money back. Can one of you respond? What is the inertia there?

Ms. SCARLETT. Congresswoman, I believe we are responding. There are several issues that you allude to. First, all leases——

Ms. WATSON. Wait a minute. Would you address the 8 years that it has taken to come to today, please?

Ms. SCARLETT. Yes, that is exactly what I intend to do.

As soon as it was discovered that the 1998 and 1999 leases had no price thresholds in them, all subsequent price leases have included, since 2000, price thresholds. So that part of the issue, as soon as it was illuminated, has been rectified. All leases that we now undertake do address that.

With respect to any renegotiation of the past leases, we do not have authority in a mandatory way to do that. But what we did do as soon as we, again, found that those 1998 and 1999 leases had no price thresholds, we began to appeal for the companies to come in and discuss with us renegotiation of those leases. That process, as Johnnie Burton described, is underway. So those are the two issues.

Ms. WATSON. Again, let me ask about that, because in our last hearing I was very pleased that at least one of the large oil companies did step forward. I mentioned it after their testimony. If several of the companies are willing to start sitting down and negotiating, what is your perspective on the time it would take? It just seems to me irresponsible that it has taken so long. We know the issue. We hear it over and over, every time we have had a hearing, the same thing.

I am getting a little tired of it. Tell us when we can resolve this?

Ms. SCARLETT. I appreciate the concern. Let me say that we are actively at the table discussing renegotiation of the leases as we speak. Because we are doing this in a voluntary context, it is a back and forth, and I cannot give you a precise date. We are actively in those negotiations. I will turn to Johnnie to give you more detail.

I will also underscore that when the 1998 and 1999 lease issue came to our attention, which was, as Johnnie Burton said, just in 2006, we immediately asked for an IG investigation so that we could understand what went wrong and rectify or remedy the processes that led to that.

Ms. WATSON. Let me just stop you. We know all that. We have heard it over and over again. I am wondering why the administration is opposing giving Congress, or giving you the right to leverage, to be able to renegotiate? Where is the inertia? Who is stopping you? Why is it that the witnesses would not come and testify? What do you think?

Ms. SCARLETT. Well, we are actively renegotiating on a voluntary basis those leases. The administration has significant concerns, and indeed sent up a statement of administration position opposing mandatory renegotiation.

Ms. WATSON. Hold on. Why do you think they have done that?

Ms. SCARLETT. I am about to describe the justification for that. These contracts, like all contracts, reside at the bedrock of a reliable Federal Government as they enter into, whether it be a contract to supply weaponry equipment, whatever it might be. It is very important that we uphold the sanctity of those contracts so that the Federal Government and its word when it signs a contract can be relied upon.

Now, we are very actively engaged in voluntary negotiations.

Ms. WATSON. Yield, please, on that point, the sanctity of these negotiations. Explain what you mean.

Ms. SCARLETT. No, I said, the negotiations. Of the contract itself, a contract is a written and signed agreement, and it is extraordinarily important because those contracts are part of many, many, many other contracts that the Federal Government makes. As a reliable business partner, anybody who enters into any future contracts with us has some sense of security that contract in fact will be honored.

Ms. WATSON. Yield, please. On that issue, we are talking about 1998 and 1999.

Ms. SCARLETT. And on the 1998 and 1999 leases, we are actively working on renegotiating on a voluntary basis those leases.

Ms. WATSON. Yes, Johnnie.

Ms. BURTON. May I add something, Congresswoman? As I said, I have been talking to several companies. I didn't want to give any names because when you are in negotiation, it is not always smart to do that. However, I know one of the companies is very close to signing an agreement, and that is Shell Oil. They are one of the major owners of leases offshore. The lawyers are now finalizing the agreement. So we are working on it.

The reason it takes so long is because it is such a complex type of contract that has many partners in it. So the companies have to check with their, you know, they have to worry about their shareholders. They have to worry about their partners, etc.

Ms. WATSON. I need to ask the Chair a question.

Chairman TOM DAVIS [presiding]. Sure.

Ms. WATSON. Does the renegotiation void old contracts? Would not the old contract apply? We just want to be back——

Chairman TOM DAVIS. Well, the old contract is law. That was the underlying law that governs at this point. Should they renegotiate and reach a new agreement, of course, that would abrogate the old agreement. There is no legal obligation to do that. There are certain incentives that either we or Interior can offer them.

Plus, I think the light that shines on this can be a great disinfectant on this whole thing, and bring them back to the table. I mean, they are making record profits at this point, if they have a loophole in here that they claim under oath here they didn't intend, that this didn't come from them. So hopefully, they are in good faith.

Did you want to add anything to that, Ms. Burton?

Ms. BURTON. I think you are absolutely right, Mr. Chairman. We are not renegotiating the contract. We are having a separate agreement that will be attached to that contract, and the agreement will be that the company agrees to come back under the threshold and pay royalties.

Ms. WATSON. Yes, what I understand, and I can be corrected on this, the Markey legislation would say, well, if you don't want to renegotiate, then you shouldn't get a new contract.

Chairman TOM DAVIS. That is right, but current contracts would stay in effect. What we are working on right now is trying to look at the current contracts and come back. The oil companies, many of them have expressed a willingness to do this. So that is why I asked where it was. That is why I have asked for the chart.

Before I proceed, I just want to share my grave concern that we have employees who may or may not have made the mistake, ei-

ther in the original negotiations or in the coverup. But people make mistakes, OK? I make mistakes. I know Mr. Issa, I don't know if you do, but the rest of us, I mean, we make mistakes.

The key here is it is done, but what we are trying to find out is what happened and get information. If an employee who has been fingered as being part of that mistake then refuses to give a statement under oath or to take a lie detector test, that is a grave concern to us. I understand their lawyers are probably telling them a lot of different things, but at the end of the day we have to be able to govern accordingly. We have to have employees to fess up, then we can move on, that's all, and somebody can be fired.

Somebody who refuses to cooperate in investigating a coverup, that is a major, major problem that I think may be systemic throughout the Department, and may not be just to these leases.

All right. We are ready for a second round. I will start with you, Mr. Issa, and then I have more questions.

Ms. ISSA. Thank you. I will just pick up where we left off. I appreciate this, Mr. Chairman.

Just a quick statement. From my recollection, some of the oil companies who were most willing to renegotiate explained to us, and Ms. Watson probably will remember this as I say it, that they have in fact entered into some negotiations where these thresholds not being there meant that their partner in the actual drilling or in some other aspect, had a contractual expectation of receiving money from dollar-one that envisioned not having a 12.5 percent payment to us.

So I certainly can understand why it is complex, that they have to either get their partners onboard or in some cases I imagine, I don't want you to disclose your negotiations, but I would imagine they maybe saying we can't give you a royalty on the part that we have already given away to a sub, but we will pay you on everything else. I can understand that. When we make a contract that is faulty, they may have in good faith, up until 2000, we could have just said, look, it is faulty; let's fix it.

Unfortunately, we reiterated in a sense that they were good with those contracts for a number of years. They relied on, oh, it's OK to act on those contracts the way they are, looking back. That is why we are having this investigation now, it is that in 2000, when it was discovered, nobody said, oops, we are going to have to renegotiate that; we are going to have to figure out a way.

Because as a businessman, 20 years in business, when it would have cost me nothing, and I am on the board of a public company, when it would have cost the company nothing other than a hypothetical what if, because the price threshold hadn't been met, it would have been easy to say, oh, we always thought it was; let's correct it. I am not even sure it would have come to a public company's board to make those corrections.

I can imagine in no uncertain terms that every public company's board is dealing with this personally on every one of these leases. There is no chance under Sarbanes-Oxley that the board is not figuring out who is going to sue them for settling with us, which I do expect that some lawyer will sue these companies for giving in to the Government the 12.5 percent that they really do owe.

I have a couple of questions. First of all, the third name, so you have it, is Dan Henry.

Ms. BURTON. That doesn't ring a bell. I am sorry.

Mr. ISSA. Well, that is the third name, from our records, of the three that we are dealing with. I think publicly we will not say which ones took and didn't take, but obviously there is one good, one mediocre, and one bad out of that crowd, in our view.

I want to go back to the policy question, though. This letter, which I checked with my staff, I am sure we received it, but in the pile we did not pick out that one paragraph, and we now want to focus on that paragraph, of that letter. If an associate at some level, upper-management, but certainly not in 1996 and 1997, 1998, 1999, the Secretary of the Interior, said that was policy. If I understand correctly, at that level, you don't make policy. Policy comes from the top down. Is that correct?

Ms. BURTON. Associate directors are really upper-management. They usually run their policy calls to the director. If it is a substantial policy call, it is run up through the Secretary. At least that is the way we work now.

Mr. ISSA. Exactly. So in light of what we see today and how you work today, the idea of not putting something in that clearly Congress said we want to have these price thresholds, we want to empower you to have them, but basically saying you get a free ride, period, no matter where the price went, at least potentially in the rulemaking, that policy could well have gone to Secretary Babbitt at the time. Is that right?

Ms. BURTON. Yes.

Mr. ISSA. So we need to find out where that policy came from, and that is why it is helpful if we can have this associate director's name, which we will get out of it. To be honest, we now want to continue up and find out where that policy decision was made.

Ms. BURTON. Mr. Congressman, we have not been able to trace it beyond that letter. That is the only thing we found.

Mr. ISSA. Is that person still alive?

Ms. BURTON. No.

Mr. ISSA. Oh.

Ms. BURTON. She wrote that letter to a company in response to a company complaining that we, the Government, Department of Interior, did not have the right to put thresholds in. She answered saying they are not in the rule because we made the decision not to have them in the rule. They would be in the leases, but the Secretary has the discretion to decide what the thresholds will be and whether there will be any.

Mr. ISSA. Was that Kerr-McGee that sent the letter?

Ms. BURTON. No, but it was the same issue. It was before Kerr-McGee, and this was another company.

Mr. ISSA. OK.

Thank you, Mr. Chairman.

Chairman TOM DAVIS. Thank you very much.

Mr. Markey.

Mr. MARKEY. Thank you, Mr. Chairman, very much.

Ms. Scarlett, I have a list of the 56 companies that hold 576 leases let in 1998 and 1999 that remain active. Which of these 56

companies are the 20 that you say have actually responded to your letter inviting them to renegotiate?

Ms. SCARLETT. Yes, I will turn to Johnnie for that, who has been actively discussing with those companies that issue.

Ms. BURTON. Congressman, I think I was asked by another member to provide, and by the chairman, to provide a matrix of all those companies and where we stand.

Mr. MARKEY. We have asked for that, but if you can answer that.

Ms. BURTON. Off the top of my head, I can give you some names, but I know I am going to leave some out.

Mr. MARKEY. Let's move down to the next level. Which of the 20 who have responded favorably so far, of the 20 who did respond, how many of them have responded favorably to you? Yes, they will renegotiate?

Ms. BURTON. I know Shell Oil is ready to sign. That is Shell. BP is close behind. I can't really tell you because the others we are still talking. I don't know how close they are. It is difficult when you are negotiating.

Mr. MARKEY. I understand. But you are saying that, who are the 10 of the nearly 10 that have actually met with you on scheduled meetings? Do you have those off the top of your head?

Ms. BURTON. I can give you some names, but I am not sure that it is appropriate to give you names when I am still negotiating with them. They may walk away. I don't know.

Mr. MARKEY. I guess what I am trying to get at here, there are 56 companies altogether, and they range from A, Amerada Hess, to W, Woodside Energy. So you have 56 companies, 20 have responded, 10 have met with you, and what you have said so far, 2 it sounds like, are renegotiating with you, out of 56.

Ms. BURTON. We are talking to nearly 20. We have been contacted by nearly 20 companies. We are talking to about 10.

Mr. MARKEY. Yes, so less than half have responded, and of those so far you are only able to name two who are renegotiating.

Ms. BURTON. The only reason I named two is because I know these two companies have told me I could say it. The others have not given me that permission, and because I am negotiating——

Mr. MARKEY. Well, tell me, how many other companies are renegotiating, without giving their names? Are actually renegotiating, how many others?

Ms. BURTON. Those 10 are at the table.

Mr. MARKEY. Are all negotiating?

Ms. BURTON. Yes.

Mr. MARKEY. OK. So one-fifth of the companies are renegotiating, and I guess you could say 10 out of 56, maybe 1 out of 5 ain't bad in some realms of life, but here when you are talking about potentially billions of dollars of taxpayers' money, if all they recover is 1 in 5, that would not be a good situation.

So I guess what, in response to a question from Chairman Davis, you said right now 17 of the leases that lacked priced thresholds are producing today, and an additional 27 leases have indications of oil or natural gas being present, meaning that they could start producing soon. How many of these 44 leases have been renegotiated to include price thresholds?

Ms. BURTON. I am sorry. I am not sure I understood your question. You want to know how many have been renegotiated? Well, none. We are talking right now.

Mr. MARKEY. Exactly. OK.

Ms. BURTON. You know, some of the folks we are talking to hold a good deal of those leases, so it depends on who we are going to reach an agreement with that may cover more or less of the production in the leases. They don't have exactly the same amounts.

Mr. ISSA. Would the gentleman yield?

Mr. MARKEY. I would be glad to yield.

Mr. ISSA. Would you give us an estimate of the 700 leases, because you said 400 of the 1,100 were turned back in, of the 700 leases, these 10 companies roughly, how big a part of those 700 leases do they represent? A substantial portion, disproportionate perhaps for the total number?

Ms. BURTON. It is probably a fairly good amount of the leases are represented by those. The ones that have been relinquished obviously are no longer in play. The companies we are dealing with are most likely the ones holding the leases that are still active, or most of them active, but I can't give you a number at this point.

Mr. MARKEY. I thank the gentleman.

So we are looking at 1998 and 1999. We are trying to find out what went wrong, and that is very important to us, to find out what went wrong. Now, you have less than 20 percent of these oil companies who are negotiating with you. So my question to you, Ms. Scarlett, is why does the Department of Interior and the Bush administration continue to object to the Markey-Hinchey amendment, to give you the leverage you need to get every one of these companies to the table, so that you can provide the relief?

I mean, there was a big mistake that was made. We have to get to the bottom of that. But you also need a solution. What I am hearing today is I don't hear a solution. I hear something that is very nice, but without the leverage that the Government would need in order to bring them all to the table.

Why do you continue to object to this language that was passed in a bipartisan manner in the House and in the Senate?

Ms. SCARLETT. Congressman, let me first underscore a point that Congressman Issa made and that Johnnie Burton was making. While there are 55 companies and 20 of them have come forward to us and we are actively discussing with 10 of them, that does not represent 1 in 5 of the actual production activity.

We believe that the companies we are negotiating with, of the active leases still covered by the absence of price thresholds, that we have likely the majority of production. So this constitutes significant progress if we successfully renegotiate these leases.

Mr. MARKEY. I think that is the key phrase: If you successfully conclude negotiations. So what I am asking you is, why don't you want this additional leverage? That will help your negotiating position. It won't affect any of these companies since they are going to reach an agreement with you anyway. Why do you object to getting this extra leverage? Otherwise, these negotiations could go on for years before you actually resolve it.

You don't have any guarantee that you are going to reach a deal with any of these companies. In fact, it is very likely they are try-

ing to run out the legislative clock this year so that this bill doesn't pass. They stop it, and then they just drag it on for another 2 years. Why don't you want the leverage? What is it about the Bush administration's relationship with oil companies that stops you from saying, give us the leverage to correct this huge injustice against the American taxpayer?

Ms. SCARLETT. Congressman, I appreciate your concerns. We are actively renegotiating the leases. We believe we will be successful.

Mr. MARKEY. Why are you objecting to this additional leverage? Why don't you want it?

Ms. SCARLETT. We do have concerns, as indicated in the statement of administration policy, about any actions that would in a mandatory fashion either directly undermine contracts. We think the honoring of contracts itself is an important bedrock principle of law.

Mr. MARKEY. Again, let me just re-state it one more time. This does not change any existing contract. It only deals with future contracts. OK? You keep saying that this is going to deal with the reliability of existing contracts. It does not. This amendment only says that you now have the discretion in future contracts as to which companies you are going to deal with. Why don't you want that leverage?

Chairman TOM DAVIS. I think you have asked, and I think she has given the answer she is going to give, but I appreciate the question. The gentleman's time has expired.

Your testimony describes common tensions between centralized control of the bureaus and their mission-specific needs. That is something the IG has dwelt on. Would a more centralized control at Interior be beneficial to managing the department's programs?

Ms. SCARLETT. As I indicated in my written testimony, the tension in any large organization between deciding how much centralization and how much decentralization is a constant and common management challenge.

Chairman TOM DAVIS. It is. But look, at Interior you have had problems on the Indians in terms of Indian recognition rights. This has been well documented. You have had problems here. I mean, it just looks to me like there needs to be adult supervision across the board here. Am I missing something?

Ms. SCARLETT. Congressman, we have many, many, many different programs, some of them very specific to particular statutes and particular missions. We have taken steps to centralize those activities where we believe the activity would benefit from that kind of coordination. Specifically, through 25 recommendations made by our Inspector General, we actually created a centralized department Office of Law Enforcement and Security to bring common practices and procedures for all of our law enforcement entities within the department, which number some close to 4,000.

I did not the appraisal services, which used to be distributed throughout our bureaus. We centralized that into a single office. Likewise, with our information technology, we have done significant centralization of purchasing and management, again to address some of the IT security issues that have been noted.

So we are looking at specific management problems and taking that management tack, whether it be centralization or strengthened coordination, that seems appropriate to the task at hand.

Chairman TOM DAVIS. I believe we have expressed the concerns in terms of what has happened. We haven't really satisfactorily explained the coverup. Ms. Burton, when did you first learn about this? You came in 2002, right?

Ms. BURTON. I came in 2002, and I heard about those 2 years with no threshold in early 2006, maybe at the very end of 2005.

Chairman TOM DAVIS. Did you ask why it took so long to come up to you through the ranks?

Ms. BURTON. I don't think the ranks realized that they needed to tell me about it. This was an issue that happened previously, and they felt the Secretary, it was not an illegal issue.

Chairman TOM DAVIS. No, but it cost Americans billions of dollars.

Ms. BURTON. Absolutely.

Chairman TOM DAVIS. And let me just say this, on something like this as you go through a review, to me it is incredible that someone wouldn't have brought this to the attention. Evidently, they brought it to the New York Times before they brought it up through the ranks. Maybe they felt they couldn't do it with the current department structure.

Ms. BURTON. Oh, no.

Ms. TOM DAVIS. Well, tell me about it. The earlier you learn about this, the earlier you can renegotiate. In fact, if we were renegotiating in 2004 instead of 2006 before the oil prices came up, think of the billions of dollars that we would have gotten.

I also want to add, for Mr. Markey, we have asked for a chart in terms of all of the different leases, which ones are actively being drilled, which ones aren't, and we will be happy to share that with you when we get it, and then have an idea of whose negotiating, just to try to get some handle on this.

I guess the concern is ordinarily we would say that the department do what it will, but in this particular case, obviously, without I think additional congressional oversight, a lot of this would not have been done, without the increased scrutiny.

It is difficult for us to get up here and have to make tough choices over money for school lunch programs, over money for student loans, over money for additional transportation, just by the way, because someone somewhere within the Department of Interior decided they didn't want to have price thresholds on this thing and billions of dollars are now out the window. That is the concern. I think we would not be doing our job if we weren't here asking the questions.

To me, the fact that some of the employees involved in this won't at least come forward and talk about what happened so that we can figure out and make it quit from happening again. And then what Mr. Markey is talking about is if you can't get these leases renegotiated, I think Congress is going to have to re-think, House and Senate, in terms of putting pressure on these companies to do something else.

If you come forward and you renegotiate the leases without Mr. Markey's amendment, that is great. I mean, I think we can pre-

serve the contract integrity and everything else. But if you are unsuccessful, believe me, with this much money on the table, I think the legislation may be even more to your un-liking, because this is just a lot of money. Do you understand what I am saying?

Ms. BURTON. I certainly do, Mr. Chairman. We share your concern, believe me.

Chairman TOM DAVIS. Ms. Burton, look, we are both aware that GAO is conducting an in-depth review of the royalty revenue projections and the loss of royalties as a result of the 1998 and 1999 mistakes. GAO is doing that. The projections you have made are based upon raw data and assumptions provided to GAO. My understanding is that an initial read of those data and assumptions probably does not bode well for the department.

You tell me today that you are going to do whatever is necessary so the American people get what is owed to them in this course, because these resources at the end of the day, these are the American people's resources. Will you tell me you will do everything you can to try to get this right?

Ms. BURTON. Absolutely, sir. And we are working hard on it, and we appreciate your help to get there.

Chairman TOM DAVIS. OK. Thank you.

We have another round. Mr. Markey.

Mr. MARKEY. I thank the chairman very much.

Again, I just want to zero in on this issue. We have to look to discover whether or not there was a coverup. But we also have to make sure that we don't have an ongoing stick-up of the American taxpayers. We have to solve this and solve it now. The Department of Interior only began this process under pressure from the Congress. This had sat there as an issue for years.

So I remain perplexed at the reluctance of the administration to accept this leverage, which the Congressional Research Service makes quite clear does not violate in any way the contract and would serve as the answer to the question which you have in terms of this problem. Let me read to you again on this issue. The Congressional Research Services says this on May 18th: "As we stated in our telephone conversation of May 17, there do not appear to be any constitutional impediments to the proposed amendment. Enactment of this amendment would not constitute a taking of existing leaseholders rights, but would merely establish a new qualification for potential leases. It has long been recognized that the Government has broad discretion in determining those firms with which it will deal."

Again, I continue to hear your objection to receiving this leverage, while I don't hear from you any agreed-upon deals with any of these oil companies. From a taxpayer's perspective, I just think that it is irresponsible to refuse to support the additional leverage which would enhance the likelihood that these oil companies would come to the table, so that you can protect the taxpayers.

It just seems inexplicable from a public interest perspective that you would oppose having this additional leverage, because the oil companies are still in a situation where they only have to voluntarily come in, knowing that a terrible deal was cut back in the 1990's. I still haven't heard a good explanation from you why you don't want to do that.

Ms. BURTON. Congressman, we agree this is not a taking. What it is is a strong leverage, as you call it, to essentially change the terms of a contract in order to continue business in this country. And this administration feels that this goes to the heart of the sanctity of contracts.

Mr. MARKEY. Again, I just read to you from the Congressional Research Service.

Ms. BURTON. You are talking about two things, sir.

Chairman TOM DAVIS. This is a policy call. I mean, their policy call is, as I understand it, is the inequality of bargaining power balanced here. Is that the administration's view?

Ms. BURTON. That is correct, sir.

Chairman TOM DAVIS. I think it boils down to, if they can renegotiate these leases without it, great. But let's see what happens.

Mr. MARKEY. We have already seen the results. They are sitting there. They have no results.

Chairman TOM DAVIS. They are still working on it.

Ms. SCARLETT. I think the most important results we have to underscore are, from 2000 and forward, including every single lease in this administration, we have had those price thresholds. Therefore, for the taxpayers, those revenues are forthcoming as we speak on all those issues. And that is a critical point.

Mr. MARKEY. I will say this right now. We will have a solution to the Middle East crisis before you get BP and Shell to agree to a $36 a barrel threshold. That will never happen unless you accept this additional leverage. Never.

I think you are sitting down there continuing a policy that allows the oil companies to maintain the whip hand in the negotiations with the public. I think that this administration should put their thumb on the scale to even-out this negotiation process because otherwise they are enjoying windfall profits that are historic and unlikely to be discontinued unless you accept this additional power on behalf of the public.

I just think that you are operating in a completely delusional way, reflecting the likelihood of these oil companies surrendering these huge profits. In fact, they have a fiduciary relationship. They have a fiduciary responsibility to their shareholders not to surrender those profits. Whereas you have a fiduciary responsibility to the American taxpayers to reclaim them.

I don't think in the absence of your accepting this power and removing your objection to the passage of the legislation, just waiting for your say-so, that you will have to show a little responsibility of losing billions of additional dollars that could have been used to provide education and healthcare for the American people. I think that will be on your shoulders.

Chairman TOM DAVIS. Let me ask, before I let Mr. Issa sum up, let me ask very briefly. Are we close to any agreements with these companies?

Ms. BURTON. I believe we are very close with Shell and BP. I don't know about the others yet.

Chairman TOM DAVIS. OK. How much active drilling are they doing at this point?

Ms. BURTON. They are very active in the Gulf, both companies. I don't know how many on those particular leases. I am trying to get all the companies who have leases——

Chairman TOM DAVIS. That is fine. We need the chart. We just need to have a chart so we can follow it.

Ms. BURTON. Yes. I will get that to you, Mr. Chairman.

Chairman TOM DAVIS. And the leases that have been negotiated from 2004 is great, but most of those aren't being used at this point. It takes time once the lease is signed, doesn't it, and to get the oil from the ground. Is that right? So this would be in the future.

Mr. Issa.

Mr. ISSA. Thank you. I will try to sum up.

There is a famous quote: What did you know and when did you know it? We certainly remember that from our youth. I know you are too young to remember the 1960's, but I sort of do.

Ms. SCARLETT. I might even remember the 1950's. Thank you, Congressman.

Mr. ISSA. It doesn't show.

I would appreciate if, as you are going through your own evaluation, Director Burton, you told me that you didn't know until 2006. I would like to know, and I would really appreciate it if you would provide us with a similar chart of who knew when. Now, the IG is going to provide quite a bit, but I think the fact that people clearly knew and made the changes, and yet we have this whole void of people who, between the ones who made the changes when the discovery was made, and the time it got to you in 2006. I find it hard to believe that there wasn't a chain bubbling up of an awareness by more and more and more people of this, even if it was at the water cooler.

So I would appreciate if we could get an understanding of how this thing morphed to where in 2000, people figured out there was a change, under the previous administration, a problem. They changed it, and it took until 2006 to bubble up to you. So I would appreciate understanding that better because that has been one of the illusive things is who knew what and when, and we would like to fill in what we don't have.

Madam Secretary, I think particularly, the Solicitor does fall under your watch. Is that correct?

Ms. SCARLETT. The Solicitor is in the Office of the Secretary, of which I am a part.

Mr. ISSA. OK. I need to know when you are going to do the reform of that office, because this committee and my subcommittee found it very clear that reform has not happened yet, that they are still doing water cooler, no memo for the record, kind of dealing. That clearly was one of the points at which this failure occurred and would not otherwise have occurred in spite of all the other things that happened.

Ms. SCARLETT. Congressman, we are in fact looking at the Office of the Solicitor and its management and those processes, and how to improve them in terms of that approval process.

Mr. ISSA. And now I will use one other quote that I am probably not qualified for, and that is, and now the other part of the story. I voted against Mr. Markey's amendment, as I recall. I believe in

contract sanctity and I don't believe his solution is fair. What I do believe, though, from the discovery of our committee, is that this is much less like a contract that you negotiated, and now you are back saying, but the deal changed because the price changed. This is much more like a triple-net lease for a building, and then the roof falls in, and you are trying to figure out, well, did you think the triple-net meant you fix the roof? Or did you think this was a triple-net where you thought the landlord was going to fix the roof?

Before our committee, multiple oil companies, perhaps some of the largest by far, testified that they thought the thresholds were in the contracts when they signed them, meaning that they paid a price to the Government, sort of like how much you lease a building for, depending upon whether or not you think you are going to have to fix the roof. They bid on these contracts transparently as though they were still in, because the bidding prices in their own testimony didn't change.

So when you are negotiating, and Johnnie, I think you are probably face to face with these people, I disagree with Mr. Markey because I don't think it is about whether the price went in. I don't think it is about cajoling them. I think it is about saying, come on, folks, if you believe that it was in there, you believe you signed it. We believe that the Government was supposed to have it in. We believe this is the kind of a failure that should not be taken advantage by either party.

I would hope that in your negotiations, you would say, look, if the Government thought it was supposed to work this way, and it was to your favor, and you came back to us, we would be having the discussion exactly the same, which is, the intent of a contract is part of the contract. And you go back often, even though you have a written agreement, and I was recently deposed on one where I had an agreement in court codified by a U.S. Federal judge in which I gave a license to somebody. And wouldn't you know it, they wanted to have me testify as to what I thought I gave them 8 years later, because it does matter. What you think you got and what you think you gave matters.

So I believe that is a strong point, and that is the reason I didn't vote for Mr. Markey's amendment, is I believe you have the ability to negotiate in good faith, based on original intent of both parties. I believe you will be successful, and I also believe world peace will come in the Middle East. But I believe that your settlements will come sooner because I believe one company signs, that will be the model for all of them.

Thank you, Mr. Chairman. And thank you for holding this important hearing.

Chairman TOM DAVIS. Thank you.

And Mr. Markey, thank you as well.

I would just add, I am not sure where I was on Mr. Markey's amendment. As I recall, I had other interests to protect in that bill. You did vote for it? OK. I get it right once in a while.

The purpose here is to give you some leverage as you sit down, and also to give the companies, who I think want to do the right things, but have that fiduciary duty he talked about to their shareholders, to be able to come forward and get the right thing done.

But good luck as we move forward. I look forward to getting the charts from you.

Ms. BURTON. Yes.

Chairman TOM DAVIS. This is an issue we are going to continue to, well, we will watch it, continue to investigate, and probably do further hearings.

Thank you very much. The hearing is adjourned.

[Whereupon, at 12:30 p.m. the committee was adjourned.]