The Federal Coal Leasing Amendments Act of 1976 and Prior Federal Coal Leases: Putting New Wine into Old Bottles

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I. INTRODUCTION

The Federal Coal Leasing Amendments Act of 1976 (FCLAA),1 enacted August 6, 1976, is a watershed in the law and history of federal coal leasing. By that Act, Congress made fundamental changes in the management and leasing of federally owned coal deposits.2 FCLAA is generally oriented toward the planning and issuance of new federal coal leases.3 However, at the time of FCLAA’s enactment there were in existence 533 federal coal leases (pre-FCLAA leases) covering 782,878 acres and including approximately 16 billion tons in estimated reserves.4 Application of the new policies of FCLAA to those pre-FCLAA leases has been a nagging problem since FCLAA’s enactment, but for several reasons the problem has become more acute in recent years. This Article is a review of that problem, with particular emphasis on the minimum royalty and diligent development provisions of section 6 of FCLAA,5 and the provisions of section 3 affecting holders of non-producing leases.6 The following discussion, of course, is not without a point of view. That view is that mandatory application of section 6 to pre-FCLAA leases is not legally required and provides no particular public benefit, and that the objectives of section 3 can be accomplished more effectively and beneficially by other means.

II. OVERVIEW OF THE FEDERAL COAL LEASING PROGRAM

The present federal coal leasing program and its controversies have their origin in the Mineral Lands Leasing Act of 1920 (1920 Act).7 This 1920 legislation, which provided for royalty leasing as the means of disposing of coal deposits owned by the United States, represented a significant departure from the prior, traditional entry and location procedures.8 Under the 1920 Act, federal coal deposits were

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3 See, e.g., 30 U.S.C. § 201(a) (1982) (concerning lease sales and land use planning); id. § 201(b) (concerning issuance of exploration licenses for lands not under lease); and id. § 208-1 (comprehensive exploratory program).
6 30 U.S.C. § 201(a)(2)(A) (1982). This Article does not address issues arising from pending preference right lease applications (PRLAs) made prior to FCLAA. See generally COAL LAW AND REGULATION, supra note 2, at § 82.04[6].
8 See COAL LAW AND REGULATION, supra note 2, at § 82.01.
leased for "indeterminate periods upon condition of diligent development and continued operation" and with the lease terms subject to readjustment every twenty years.9

The terms of the early coal leases required the lessees to spend a stated dollar amount in investment during the initial years of the lease and thereafter to produce a specified annual minimum tonnage.10 These provisions were a way of defining and implementing the statutory conditions of "diligent development" and "continued operation." As allowed by the 1920 Act, the lease terms also permitted the lessee to pay an advance royalty on the fixed annual production in lieu of actual production.11 Due to the general decline in coal production after World War II, the lease forms were later revised to relax these development obligations.12 In the revised leases, no fixed amount of investment was required and the continued operation obligation was altered to require annual production sufficient to generate a royalty equal to the annual rental.13 Since the 1920 Act provided that rental paid for any year was to be credited against royalties for that year,14 these changes permitted the lessee to hold a nonproducing lease without payment of any advance royalty in excess of the annual rental.15 Between the late 1950s and the early 1970s, a substantial number of federal leases were issued with such terms and typically with annual rentals of $1.00 per acre and production royalties ranging between 15¢ and 20¢ per ton.16

As a result of a 1970 Bureau of Land Management (BLM) study,17 the Department of the Interior (DOI) became concerned about the significant amount of federal coal reserves under lease but the relatively small number of leases actually producing coal. An informal and unannounced moratorium on any further issuance of coal leases was imposed by the Secretary of the Interior (Secretary) in May 1971.18 This was followed by a more formal moratorium order issued in February 1973.19 Beginning with these administrative orders, the federal coal program entered a particularly confusing and tumultuous period, from which it has yet to emerge, as Congress, the courts, and three different administrations began taking related but frequently inconsistent steps to develop and implement a new federal coal manage-

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13 Id.; see, e.g., 21 Fed. Reg. 6545-46 (1956); Bureau of Land Management, U.S. Dep't of Interior Coal Lease, Form 4-696 (December 1958); Bureau of Land Management, U.S. Dep't of Interior Coal Lease, Form 4-696 (January 1964).
15 Solicitor's Letter, supra note 12, at 3-4.
16 Id.; Coal Law and Regulation, supra note 2, at § 82.02[2] n.50.
18 Coal Law and Regulation, supra note 2, at § 82.03[2].
19 Id.
ment program. By and large, these efforts were directed at a program for issuing new federal coal leases, but policies concerning the management of the existing leases were necessarily entangled.

Concluding that there was a need to further define and enforce the general "diligent development" requirement of the 1920 Act, DOI promulgated on May 28, 1976 regulations providing that unless 2½% of the coal reserves on any existing federal lease were produced before June 1, 1986 (ten years from the effective date of the regulations), the lease would be subject to cancellation. Shortly thereafter, on August 4, 1976, Congress enacted, over President Ford's veto, FCLAA, which constituted a comprehensive revision of the 1920 Act as it pertained to federal coal leases. Of particular significance to this Article, section 6 of FCLAA made important changes in the structure of a federal coal lease by:

(i) requiring a lease term "of 20 years and so long thereafter as coal is produced annually in commercial quantities from that lease," rather than the "indeterminate" lease term under the prior 1920 Act;

(ii) providing that any "lease which is not producing in commercial quantities at the end of ten years shall be terminated";

(iii) subjecting the lease provisions to readjustment at the end of the twenty year primary term and at the end of each succeeding ten year period; and

(iv) imposing a minimum royalty of 12½% of value on coal recovered by surface mining methods. Furthermore, in section 3 of FCLAA Congress prohibited the Secretary from issuing any new leases to any entity which holds a federal coal lease and, with certain exceptions, has held that lease for ten years after August 4, 1976 without producing coal in commercial quantities from the lease deposit.

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21 41 Fed. Reg. 21,779 (1976) (codified at scattered sections of 43 C.F.R. pts. 3500 & 3520). The regulations allowed extensions of the ten year diligent development period for delays attributable to (1) strikes, the elements or casualties of which were not attributable to the lessee, (2) administrative delay in DOI not caused by the lessee, and (3) extraordinary circumstances not attributable to the lessee and not foreseeable by a reasonably prudent operator. In addition, a five year extension could be granted if the lessee could show additional time was needed (1) for development of advanced technology, such as in situ gasification, (2) due to the magnitude of the project, or (3) because the lessee held a firm contract to sell 2½% of the reserves commencing after the initial ten year period. Id.

22 See COAL LAW AND REGULATION, supra note 2, at § 82.03[4]; Ebzery & Kunz, supra note 20, at 323-28.

23 30 U.S.C. § 207(a) (1982). Section 6 of FCLAA allows the Secretary to fix a lesser royalty rate for coal recovered by underground mining methods, and in exercise of that authority the Secretary has set the minimum royalty for underground mines at 8% of gross value. 43 C.F.R. § 3473.3-2(a)(3) (1983).

24 30 U.S.C. § 201(a)(2)(A) (1982). The exceptions are interruptions caused by strikes, the elements or casualties of which are not attributable to the lessee. See 30 U.S.C. § 207(b) (1982).
On December 29, 1976 the Secretary promulgated regulations which, with respect to existing leases, carried forward the ten year diligent development requirement of the May 28, 1976 regulations. On April 25, 1979 Mobil Oil Company filed a suit challenging the applicability of that diligent development requirement to a federal coal lease issued to Mobil in 1971. The suit was eventually settled, with the government agreeing to give Mobil a five year extension of the diligent development period. In June 1979, in recognition of the questionable enforceability of the 1976 diligence regulations, the Secretary directed BLM to request existing leaseholders to execute lease revisions which would specifically incorporate the 1976 diligence requirements as part of the lease terms. This approach, predictably, did not receive enthusiastic support from such leaseholders and was eventually abandoned by DOI.

When the Department of Energy was created in 1977, the responsibility for determining policy regarding the diligent development of federal coal leases was transferred to the new department. In December 1981, the Department of Energy proposed new regulations on diligent development that allowed the holders of leases issued prior to FCLAA to elect to remain under the lease terms until the date of the first lease readjustment after August 4, 1976. In practical effect, the proposed regulations allowed holders of existing leases to postpone commencement of the ten year diligent development period until the lease readjustment date. As explained in the preamble to these proposed regulations, the change was intended to "allow more freedom for the marketplace mechanism to govern the development of coal." Shortly thereafter, the responsibility for diligent development regulations was transferred back to DOI. On July 30, 1982 DOI promulgated new federal coal regulations which made numerous changes in the prior program, including adoption of the diligent development regulations proposed earlier by the Department of Energy. In doing so, DOI noted the marketplace reasons stated previously by the Department of Energy, but further added that DOI had determined: "[T]he congressional intent [in section 6 of FCLAA] in mandating this 10-year period was

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27 The Secretary relied upon his authority under the 1976 regulations to grant five year extensions for large mines with coal supply contracts. See supra note 21; Solicitor's Letter, supra note 12, at 2.
32 Id. at 62,228.
prospective. The statutory period cannot be applied retroactively to Federal leases issued prior to August 4, 1976.\textsuperscript{35} Several environmental groups subsequently filed a suit, styled National Resource Defense Council v. Burford, broadly challenging the DOI's July 1982 regulatory changes.\textsuperscript{36} Included in the plaintiffs' complaint was a charge that the diligence regulations contained in the 1982 regulatory changes contravene section 6 of FCLAA in that Congress intended holders of existing leases to have ten years from the date of enactment of FCLAA (August 4, 1976) in which to achieve diligent development, not ten years from the date of the first lease readjustment after FCLAA.\textsuperscript{37}

During the 1970s, when DOI was engaged in a series of massive coal lease studies and planning efforts, many of the pre-FCLAA leases began to come due for readjustment.\textsuperscript{38} In the past, DOI's practice had been to evaluate each lease individually upon readjustment and to notify the lessee of any readjusted terms before the readjustment date or shortly thereafter.\textsuperscript{39} However, being "otherwise occupied with matters of basic policy on coal leasing,"\textsuperscript{40} DOI was not readjusting these leases on their readjustment dates. Following the enactment of FCLAA, DOI began sending notices to the holders of leases for which the readjustment dates had passed informing them that such leases would be readjusted to conform to the requirements of FCLAA. In many cases, these notices were sent between five and seven years after the readjustment date and in one case more than thirteen years after the readjustment date.\textsuperscript{41}

In the readjustment process, of course, the new royalty rate was a principal item of concern. As a policy matter, DOI considered whether the new readjusted royalty should be based on specific economic evaluations of each lease upon readjustment, which had been DOI's practice in the past, or whether to adopt a blanket policy of simply imposing the minimum royalty rate upon readjustment without a specific economic evaluation.\textsuperscript{42} The Secretary opted for the latter approach, essentially because DOI considered the minimum royalty rates to be substantially higher than the prevailing market rates and, therefore, the rate which would be indicated by an economic evaluation.\textsuperscript{43} DOI took the position that under FCLAA it had no choice but to impose upon lease readjustment a royalty rate at least equal to the minimum royalty stated in section 6 of FCLAA. Since the economic evaluations would virtually always indicate a royalty below the minimum rate, such

\textsuperscript{36} Natural Resources Defense Council v. Burford, No. 82-2763 (D.D.C. filed Sept. 28, 1982).
\textsuperscript{37} Id.
\textsuperscript{38} See 1 Secretarial Document, supra note 28, Issue Papers at 141-57.
\textsuperscript{39} Rosebud Coal Sales Co. v. Andrus, 667 F.2d 949, 952 (10th Cir. 1982).
\textsuperscript{40} Id.
\textsuperscript{41} See Kaiser Steel Corp., Interior Bd. of Land App. No. 79-519, 63 IBLA 363, 368, GOWER FEDERAL SERV. (MINING) 160 (1982).
\textsuperscript{42} 1 Secretarial Document, supra note 28, Issue Papers at 141-57.
\textsuperscript{43} Id. at 104, Issue Papers at 141-57.
economic evaluations would be a waste of time in DOI's view. DOI's decision also was driven by more pragmatic concerns. Because of the growing backlog of leases which were due for readjustment but on which DOI had not yet acted, and the increasing number of leases which would be due for readjustment in the 1980s, individual review of each lease would have required a massive administrative effort.

Holders of such existing leases, not surprisingly, challenged DOI's efforts to belatedly readjust those leases. In *Rosebud Coal Sales Company v. Andrus*, the United States Court of Appeals for the Tenth Circuit ruled, in a case involving a two and one-half year delay between the readjustment date and BLM's first notice to the lessee of its intent to readjust the lease, that by its delay DOI had foregone its opportunity to readjust the lease, and its "attempt by retroactive regulation and by a belated notice to readjust . . . was outside of the statutory authority of the Department and contrary to the terms of the lease." The effect of the *Rosebud* decision was that where DOI had failed to timely readjust a lease, the lease continued with its existing terms, including the existing royalty rate, for another twenty years until the next readjustment date.

DOI's regulations now state that BLM is to provide the lessee with notice of BLM's intent to readjust the lease prior to the readjustment date and that its failure to do so constitutes a waiver of DOI's right to readjust the lease for that particular readjustment period. The rules also allow BLM two years from the date of the notice to transmit to the lessee the readjusted lease terms. The rules require that upon readjustment the royalty must be set at a level equal to or greater than the minimum rate set by FCLAA.

As sequels to the *Rosebud* decision, cases now coming before the courts raise the question whether DOI, in order to timely readjust a lease, must issue a final decision on readjustment on or before the readjustment date, and not merely send to the lessee, prior to that date, a notice of intent to readjust the lease terms. These cases also raise the related issue whether FCLAA mandates imposition of the minimum royalty rate on pre-FCLAA leases upon their readjustment. On June 29, 1984 the United States District Court for the District of Wyoming ruled in *FMC Wyoming Corporation v. Watt* that under the *Rosebud* decision a notice to the lessee prior to the readjustment date was adequate. The court, however, re-
jected DOI’s argument that FCLAA mandated imposition of the minimum royalty rate of section 6 of FCLAA on pre-FCLAA leases upon the readjustment. Rather, the court concluded that the lessee was entitled under the terms of its lease to a "reasonable" royalty rate upon readjustment, and ruled that:

Before readjustment can be completed, the BLM must make careful consideration of the facts and circumstances involved in, and especially those specific to plaintiff's leases. The royalty rate readjustment must be reasonable in light of those facts and circumstances. The 12½% royalty rate, though now a statutory minimum, cannot be flatly and mandatorily imposed on pre-existing leases at the time of readjustment.¹³

Questions concerning the readjustment of pre-FCLAA federal coal leases and the application of FCLAA to such leases, particularly the diligent development and minimum royalty provisions, are now before the courts. Also, while section 3 of FCLAA was enacted in 1976, the impact of its penalty will be felt in 1986, and consequently its merit is now being reconsidered in light of present conditions.

III. APPLICATION OF SECTION 6 TO PRE-FCLAA LEASES

FCLAA raises a number of legal issues with respect to pre-FCLAA leases, but the central question is one of statutory construction: to what extent do the provisions of section 6 of FCLAA mandatorily apply to pre-FCLAA leases? In addition to this legal issue, whether section 6 must apply to pre-FCLAA leases, there is a broader question, whether it should apply. It is not clear that mandatory application of section 6 to pre-FCLAA leases furthers any worthwhile public purpose or secures any social benefits.

A. Scope of Section 6 of FCLAA

DOI interprets section 6 of FCLAA as mandating conformance of pre-FCLAA leases to the provisions of that section upon readjustment.¹⁴ The point of beginning for any effort to divine the meaning of a statute (and perhaps the ending point as well) is the statutory language itself. Section 6 of FCLAA, in pertinent part, provides:

Section 6. Section 7 of the Mineral Lands Leasing Act (30 USC 207) is amended to read as follows:

Section 7(a) A coal lease shall be for a term of twenty years and for so long thereafter as coal is produced annually in commercial quantities from that lease. Any lease which is not producing in commercial quantities at the end of ten years shall be terminated. The Secretary shall by regulation prescribe annual rentals on leases. A lease shall require payment of a royalty in such amount as the Secretary shall determine of not less than 12½ per centum of the value of coal as defined

¹³ Id. at 1549.
by regulation, except the Secretary may determine a lesser amount in the case of
coal recovered by underground mining operations. The lease shall include such other
terms and conditions as the Secretary shall determine. Such rentals and royalties
and other terms and conditions of the lease will be subject to readjustment at the
end of its primary term of twenty years and at the end of each ten year period
thereafter if the lease is extended.\textsuperscript{55}

The problem with section 6 is determining whether the class to which the word
"lease" in the amended section 7(a) refers includes existing and future leases, or
only future leases. Common sense suggests that the term "lease" is used consistently
in the quoted provision such that the words "coal lease" in the first sentence of
the amended section 7(a), which concerns the term of the lease, refer to the same
class of leases as the word "lease" in the second sentence, which concerns diligent
development, and in the fourth sentence, which concerns the minimum royalty.
These sentences read together harmoniously if understood as applying only to future
leases, but awkwardly and inconsistently if understood as applying to both existing
and future leases.\textsuperscript{56} This suggests that in section 6 Congress was setting forth the
minimum terms which must be included in all future coal leases, but was not also
mandating terms applicable to the then-existing coal leases.

This conclusion also finds support in other provisions of the Act. Section 5(b)
of FCLAA provides for the inclusion of "leases issued before the date of the enact-
ment of this [Act]" in logical mining units,\textsuperscript{57} and section 13 authorizes DOI to
modify an "existing coal lease" by adding additional acreage.\textsuperscript{58} Moreover, section
3 of FCLAA, which imposes a penalty on holders of existing leases which are not
producing coal in commercial quantities ten years after enactment of FCLAA,
becomes superfluous if the ten year diligent development requirement of section
6 is read as applying to leases existing upon enactment of FCLAA.\textsuperscript{59} These provi-
sions, when considered with the general orientation of FCLAA toward future

\textsuperscript{55} Pub. L. No. 94-377, § 6, 90 Stat. 1083 (codified at 30 U.S.C. § 207(a) (1982)).
\textsuperscript{56} For example, if the first sentence of the amended section 7(a) applies to both existing and
future leases, the result with respect to existing leases is either: (i) upon enactment of FCLAA, the
term of an existing lease must be retrospectively rewritten to change the "indeterminate" term to a
primary term of twenty years with a "so long thereafter" secondary term, or (ii) upon enactment of
FCLAA such existing leases automatically must be given a new twenty year primary term followed
by the "so long thereafter" secondary term. Interpretation (i), as respects a pre-FCLAA nonproducing
lease, would be inconsistent with the second sentence of section 7(a). This interpretation would require
termination of the non-producing lease upon the twenty year anniversary date for lack of commercial
production, while the second sentence, if applied to existing leases, clearly allows such lessees, at a
minimum, ten years in which to achieve commercial production. Interpretation (ii) is at odds with DOI's
and the Burford plaintiffs' application of the second sentence. This interpretation could allow a pre-
FCLAA lease twenty years in which to produce commercial quantities, rather than ten years from the
date of FCLAA as argued by the plaintiffs in Burford, or ten years from the date of readjustment
as DOI interprets the second sentence.
administration of the coal program, indicate that in using the term "lease" Congress generally had future leases in mind, and when Congress desired to address existing leases it specifically so provided.

The congressional reports and debates indicate that Congress did not intend for section 6, particularly the diligent development provision, to apply immediately upon the enactment of FCLAA to existing leases. There is no real support in the legislative history for the Burford plaintiffs' claim that the diligent development provision of FCLAA was intended to apply as of the date of enactment. The legislative history is not so clear, however, on what Congress expected to occur upon readjustment of the pre-FCLAA leases. For example, the House Committee Report stated with particular reference to the diligent development provision of section 6: "Old leases (those existing on the date of enactment of the 1975 Act) would be exempt from this provision, except to the extent it might be made applicable upon readjustment of lease terms. . . ."

What is equivocal is whether this congressional report merely reflected the possibility that the Secretary, in his discretion, could try to incorporate such provisions into existing leases upon readjustment, or whether the report reflected a statutory mandate in FCLAA compelling the imposition of some, but perhaps not all, of such terms upon readjustment. Further confusion is created by a 1978 amendment to FCLAA. As noted above, section 13 of FCLAA permitted acreage additions to existing leases, called lease modifications, but required that the entire lease acreage become subject to the FCLAA lease provisions. As a result, lessees were reluctant to apply for lease modifications. Congress therefore amended section 13 in 1978 to provide that certain provisions of FCLAA, including the minimum royalty provision, would not apply to the original lease acreage until readjustment of the lease. As far as providing guidance on the intent of Congress in 1976, the 1978 amendment is also equivocal. The amendment could reflect an understanding that (1) the provisions of FCLAA, such as a minimum royalty rate provision, must

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60 See supra note 3.
61 For example, Representative Mink, Chairwoman of the House Subcommittee on Mines and Mining, advised the House that the diligent development provisions were not made retroactive, and were confined to "any future leasing," because "we [did] not wish to trigger constitutional questions." 122 CONG. REC. 486 (1976). Similarly, Congressman Drinan said that existing leases were exempt from the development period. 122 CONG. REC. 497 (1976).
62 H.R. REP. No. 681, 94th Cong., 2d Sess. 15, reprinted in 1976 U.S. CODE CONG. & AD. NEWS 1943, 1951. Likewise, Chairwoman Mink summarized the effect of FCLAA on pre-FCLAA leases as follows: "The 533 existing Federal leases would be unaffected by the bill except to the extent its provisions are made applicable upon the periodic ten [sic] year readjustment of the lease terms or upon the inclusion of an existing lease in a logical mining unit. The only other sanction imposed on existing leases would be a prohibition on leasing any additional Federal tracts to an entity which holds a non-productive lease [ten] years after the date of enactment of this bill." 122 CONG. REC. 489 (1976) (emphasis added).
63 See supra text accompanying note 58.
be incorporated into all pre-FCLAA leases upon their readjustment, or (2) a lease modification represents a bargain wherein the lessee agrees to subject the lease (which may not otherwise be subject to FCLAA) to the provisions of FCLAA upon readjustment in exchange for the additional acreage. The latter conclusion seems logical in the context of lease modification, since Congress was obviously reluctant to place additional acreage under lease at terms less strict than those required by FCLAA. Moreover, unless at some time the existing lease and the modified acreage became subject to the same lease terms, the resulting arrangement could hardly be called a single lease. To some extent, the legislative history of that 1978 amendment tends to support the first interpretation.

There are, of course, certain inherent limitations in using legislative history as a guide in interpreting specific statutory provisions. One difficulty is that the critical terms are frequently and quite understandably not used in the congressional reports and debates with great precision. Another is uncertainty over the weight which should be given congressional committee reports and statements made during debates. What is sought is the collective intent of Congress; it is not entirely clear that in voting for a specific item of legislation a congressman is necessarily endorsing the whole legislative history.

Section 6 of FCLAA has received some judicial scrutiny. In Rosebud, the court held that DOI essentially had an option to readjust the lease terms upon the twenty year anniversary, and that by delay DOI had declined to exercise that option. DOI’s regulations concerning lease readjustment contemplate that DOI can waive the right to readjust the lease terms. It is difficult to square DOI’s and the court’s conclusion that DOI has the discretion not to readjust the lease terms at all with a statutory mandate under FCLAA to impose specific new lease terms upon readjustment.

Common rules of statutory construction, of course, must also be considered. Of particular concern here is the well established rule that “a retrospective operation will not be given to a statute which interferes with antecedent rights unless such be the unequivocal and inflexible import of the terms and the manifest intention of the legislature.” The term “retrospective” application is used here in the sense of applying new rules to a preexisting relationship, rather than merely applying new rules to past conduct. There certainly is no “unequivocal and inflexible” expression of a “manifest intention” by Congress that the provisions in section 6 of FCLAA mandatorily apply to pre-FCLAA leases upon readjustment. Indeed,

66 See Solicitor’s Opinion, supra note 54, at 1011-12.
67 Rosebud, 667 F.2d at 953.
the court in *Rosebud* considered the retroactivity question and, in the context of that case, concluded that there "is no suggestion whatever that the amendment was to be retroactive and the contrary is indicated."70

This rule against retrospective application would require that section 6 of FCLAA not be imposed on pre-FCLAA leases in a way which affects the antecedent and existing rights of such lessees. Application of this rule of construction dovetails with another judicial tendency to avoid constructions which raise a possible constitutional question. The blanket application of section 6 to pre-FCLAA leases, depending on the particular lease circumstances, could raise the possibility of an unconstitutional taking of property.71 Interpreting section 6 so as to avoid altering the existing rights held by lessees avoids this constitutional issue.

In an opinion regarding the applicability of the minimum royalty provision of FCLAA upon lease readjustment, DOI's Solicitor recognized that section 6 of FCLAA applies only prospectively, but concluded "that readjustment of a pre-FCLAA lease after August 4, 1976 is, like issuance of a new lease, an event which FCLAA governs."72 The Solicitor therefore opined that DOI is statutorily required to conform pre-FCLAA leases to the provisions of FCLAA upon readjustment.73 In reaching that conclusion, the Solicitor equated the readjustment provision with a lease renewal provision and cited a line of cases stating that a renewal of a contract produces "a new contract" rather than a continuation of an existing contract.74 From those premises, the Solicitor concluded that section 6 mandatorily applies upon readjustment, since readjustment is the equivalent of a new lease and therefore governed by FCLAA.75

A problem with the Solicitor's syllogism is his first premise—that lease readjustment is the legal equivalent of a lease renewal. The difference between an indeterminate lease subject to periodic readjustment and a fixed term lease with a preferential renewal right was carefully reviewed by the Solicitor elsewhere in that same opinion.76 But that discussion points to a different conclusion regarding lease readjustment. Pertinent portions of the Solicitor's analysis are set forth below:

> [In addition to coal, the] 1920 Act also provided that phosphate and oil shale would be leased for an indeterminate term subject to periodic readjustment. Oil and gas and sodium were leased for twenty years, with the lessee having a preferential right to renew for successive periods of ten years.

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70 *Rosebud*, 667 F.2d at 952; accord *FMC Wyoming Corp.*, 587 F. Supp. at 1548.


72 Solicitor's Opinion, *supra* note 54, at 1008.

73 *Id.* at 1012.

74 *Id.* at 1008. The principal case relied upon by the Solicitor is Wyodak Chemical Co. v. Board of Land Comm'rs, 51 Wyo. 265, 65 P.2d 1103 (1937), which involved a state lease with a preferential right to renew for successive ten-year periods.

75 Solicitor's Opinion, *supra* note 54, at 1009.

76 *Id.* at 1004-06.
Why did Congress choose to lease coal for an indeterminate term subject to readjustment of all terms and conditions at twenty-year intervals instead of for a twenty-year term with a preferential right to renew? . . .

The legislative history of the 1920 Act suggests that Congress chose indeterminate coal and phosphate leases and twenty-year oil and gas leases primarily to satisfy what Congress perceived to be a greater need for reliability of investment in coal mines and phosphate plants. . . . The critical difference in the reliability of investment provided by an indeterminate and a determinate lease is in the termination procedures. With an indeterminate lease, if a lessee fails to comply with a condition the lessor must go to court in order to end the lease. . . . But if a lessee fails to comply with the terms and conditions of a twenty-year lease, the lessor can end the lease simply by notifying the lessee at the end of the lease term. 77

As the Solicitor’s analysis illustrates, the essential distinguishing characteristic of the indeterminate lease is that it is an indefinite and continuing legal relationship which does not come to an end and then begin anew upon readjustment. This characteristic explains why the indeterminate lease can be terminated only by judicial action rather than by an administrative decision not to renew a lease as in the case of a determinate lease. In a subsequent opinion, the Solicitor considered renewal of federal sodium leases, which were issued under the 1920 Act for twenty year terms with a preferential right to renew for successive ten year periods. 78 There the Solicitor also concluded that “Congress knew of, and intended that there be a difference between indeterminate leases subject to readjustment and twenty year leases with a preference right of renewal.” 79 Unlike a coal lessee, the Solicitor concluded that a sodium lessee has no right to a renewal term. Rather, if the Secretary, in his discretion, decides to renew the sodium lease, the lessee has the preference over other parties who may also want the lease. 80 This comparison of these two types of leases reveals quite vividly the significantly different and greater rights held by a lessee under an indeterminate coal lease upon readjustment than those held by a lessee under a determinate lease upon lease renewal.

Readjustment of a pre-FCLAA coal lease does not create a new legal relationship but is the continuation of an existing legal relationship. The Solicitor’s conclusion that the readjustment of pre-FCLAA leases creates a “new contract” governed by FCLAA or is the equivalent of a lease renewal, ignores the most distinguishing characteristic of the indeterminate lease.

The results of these several, and somewhat divergent, lines of inquiry regarding section 6 and its application to pre-FCLAA leases are best reconciled by the conclusion that Congress did not intend by FCLAA to abrogate the terms of existing 77 Id.
78 Memorandum from the Solicitor to Director, Bureau of Land Management, and Acting Director, Minerals Management Service (March 18, 1982), reprinted in GOWER FEDERAL SERV. (MINING) S0-4 (1982).
79 Id. at 6.
80 Id. at 6-16.
leases and gave DOI no such statutory mandate, preferring to deal with the problems of existing leases separately through section 3. However, members of Congress did assume that DOI would seek to incorporate some of the provisions of section 6 into pre-FCLAA leases upon readjustment, but only to the extent that such readjustments could be accomplished consistently with the provisions of such leases. In other words, DOI has no statutory mandate to abrogate the terms of pre-FCLAA leases in order to impose the section 6 lease terms, but DOI may, as a discretionary action, incorporate such lease terms or similar lease terms upon readjustment to the extent the provisions of pre-FCLAA leases allow.

B. Limitations in Pre-FCLAA Leases on Readjustment

As argued above, the limitations on DOI’s ability to adjust pre-FCLAA leases to conform to FCLAA are the provisions in such existing leases. In this regard, the lease readjustment process raises a procedural issue concerning the time when such readjustment must take place and substantive issues regarding the specific lease terms which may be added or modified upon readjustment.

1. Timely Readjustment

The 1920 Act provided that leases were to be subject to readjustment “at the end” of each twenty year period. This provision was included as a specific term in pre-FCLAA leases. DOI’s present regulations require it to notify the lessee prior to the readjustment date of DOI’s intent to readjust the lease terms, but allow DOI two years from that notice in which to transmit to the lessee the new, readjusted terms. As a result of Rosebud, DOI now typically provides the lessees with a notice of intent to readjust the lease terms prior to the readjustment date. Commonly, this is a notice only and does not state any proposed terms (and for that reason is generally known as the “naked notice”). Following the naked notice, DOI submits to the lessee proposed readjusted lease terms and allows the lessee sixty days in which to submit objections. The lessee may or may not receive the proposed lease terms prior to the readjustment date, and rarely is a final decision made by DOI regarding the readjusted terms on or before the readjustment date.

The FMC litigation has raised the issue whether the 1920 Act and the pre-FCLAA lease provisions require a final decision before the readjustment date. In that case, the lessee had received the naked notice and proposed readjustment terms, but a final decision had not been made by DOI on the lease readjustment prior to the twenty year anniversary date. The district court ruled “that notice prior to the anniversary date made readjustment in the present case timely.”

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82 See supra notes 10 & 13 and accompanying text.
84 FMC Wyoming Corp., 587 F. Supp. at 1546.
85 Id.
86 Id. at 1547.
The 1920 Act and the lease provisions unambiguously refer to readjustment “at the end of” the twenty year period, and there seems to be no reason why DOI should not be able to complete the readjustment process on or before that time or why DOI should be entitled to additional time in which to make a readjustment decision. However, a procedure by which the readjustment process is commenced by a notice prior to the readjustment date and completed shortly thereafter is not necessarily inconsistent with the 1920 Act and the lease provisions, although the two year period DOI allows itself in which to submit the readjusted lease terms seems unnecessarily long.

There are certain consequences, and perhaps inequities, which result from a strict interpretation of the twenty year deadline. If the lease is not timely readjusted, the readjustment opportunity is lost for that period and the lease continues under its existing terms (including its existing royalty rate) for another twenty year period, at which time it would again be subject to readjustment. Such a result could represent a substantial windfall for the lessee and a corresponding loss for the government.\textsuperscript{87} The result may also have certain incidental effects on competition. For example, the mine involved in the \textit{FMC} case was in the vicinity of and in competition with another federal lessee whose federal lease, because of DOI’s delay in seeking to readjust its terms and the holding of the court in \textit{Rosebud}, continued with a royalty rate of seventeen and one-half cents per ton for another twenty year period.\textsuperscript{88} Clearly, DOI’s failure to timely readjust that lease provided the competitor with an important advantage over the FMC mine, particularly if the royalty on FMC’s lease were readjusted as high as twelve and one-half percent of gross value. Such problems were the inevitable result of the \textit{Rosebud} decision, but would be exacerbated by a judicial ruling that all readjustments are untimely if not fully completed on or before the twenty year anniversary date.

2. Substantive Lease Terms

With respect to the substantive provisions which DOI may incorporate into a lease upon its readjustment, two basic issues are raised: whether specific provisions of the pre-FCLAA leases automatically subject such leases to present statutes and regulations, regardless of reasonableness, and whether the readjusted provi-

\textsuperscript{87} California Portland Cement Co. v. Watt, 667 F.2d 953 (10th Cir. 1982), was a companion case to \textit{Rosebud} on appeal and involved somewhat similar facts. In its brief in \textit{California Portland Cement}, the government observed that, assuming the production rates on the lease involved remained the same, the loss of potential royalties on that lease alone by reason of an untimely readjustment would be in the neighborhood of \$15 million before the end of the current 20 year lease period. The government further noted that at that time there were 69 coal leases which similarly were readjusted after their anniversary dates. Brief for Appellants at 25 (filed June 11, 1981). This provides a general idea of the magnitude of the royalties lost by DOI by reason of its failure in those cases to timely readjust the leases, a loss which is largely due to DOI’s preoccupation at the time with endless studies on federal coal planning and management, and its failure to properly tend to the more routine responsibilities of lease management.

\textsuperscript{88} See \textit{FMC Wyoming Corp}, 587 F. Supp. at 1548.
sions are subject to a standard of reasonableness based on the circumstances of each particular lease.

Section 7 of the 1920 Act provided that at the end of each twenty year period such readjustment of the lease terms could be made as the Secretary might determine, "unless otherwise provided by law at the time of the expiration of such periods." Prior to 1964, the preamble of the standard federal coal lease form included a provision subjecting the lease to "all reasonable regulations of the Secretary of the Interior now in force," but the standard form was subsequently changed to subject the lease to "all reasonable regulations of the Secretary of the Interior now or hereafter in force." These two provisions, the "unless otherwise provided" provision in section 7 of the 1920 Act and the "or hereafter in force" provision in the post-1964 leases, may render a pre-FCLAA lease automatically subject to FCLAA's mandatory provisions by virtue of the terms in the lease itself. The "or hereafter in force" clause would apply only to post-1964 leases, while the section 7 clause would apply to all pre-FCLAA coal leases.

The "unless otherwise provided" clause of section 7 was eliminated by section 6 of FCLAA and thus is no longer a statutory provision. However, pre-FCLAA coal leases included the clause as a lease term by reserving to the lessor the "right reasonably to readjust . . . terms and conditions at the end of 20 years from the date hereof and thereafter at the end of each succeeding 20-year period during the continuance of this lease unless otherwise provided by law at the time of the expiration of any such period." The meaning and effect of that lease proviso is not entirely clear. The proviso may modify the immediately preceding provisions regarding the time between readjustments, simply recognize that the Secretary's right to readjust may be later withdrawn by an act of Congress, or broadly reserve to Congress an unlimited right to alter all of the material terms of the lease upon readjustment. Even if broadly construed, however, reliance upon this provision as a basis for requiring adjustments to pre-FCLAA leases to conform with section 6 of FCLAA creates a circular argument. The Secretary is, of course, required to comply with the statutory directives existing upon lease readjustment. But, as discussed above, the provisions of section 6 of FCLAA apply prospectively and there is no clear mandate in FCLAA to the Secretary to impose those terms upon readjustment of pre-FCLAA leases.

The "or hereafter in force" clause of the post-1964 standard form lease, as a basis for incorporating FCLAA lease provisions into pre-FCLAA leases upon readjustment, raises similar problems. If the regulations to which the lease is sought to be subjected were promulgated under the authority of FCLAA to implement

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90 Compare COAL LEASE, FORM 4-696 (December 1958) with COAL LEASE, FORM 4-696 (January 1964), *supra* note 13.
92 COAL LEASE, FORM 4-696 (December 1958) sec. 3(d), *supra* note 13 (emphasis added).
section 6 of that Act, then they could hardly be mandatorily applicable upon read-
justment of pre-FCLAA leases if section 6 itself was not intended to apply to such
leases. However, these regulations may also be based on the Secretary's general
authority to prescribe regulations to carry out the purposes of the statute, which
could make them broadly applicable to pre-FCLAA leases.

If broadly interpreted, the clause would allow the Secretary the unlimited right
at any time to unilaterally alter the terms of the lease, even those lease provisions
set forth in great detail in the lease document, by promulgating regulations. But
that provision may not be entitled to such a broad construction. As the court in
Rosebud ruled, the leases should be considered in a commercial context, applying
typical contract law doctrines. With such contract doctrines in mind, the clause
should be construed narrowly to avoid an illusory contract with the lessee unalterably
bound to its terms but the government free to change them at will. Also, the
"hereafter in force" clause, which is a more general provision in the lease pre-
amble, may be in conflict with specific terms of the lease (for example, term,
royalties, lease readjustment, and so forth) to the extent that clause allows the
Secretary unlimited powers to abrogate those specific provisions. Ordinarily, in con-
tract law the specific provisions of an agreement control over the more general ones.

Furthermore, DOI's practice indicates a more narrow use of such clauses in
mineral leases. Form leases for other minerals, such as oil and gas and geothermal
leases, subject the lease to regulations now or hereafter in force, "when not inconsis-
tent with" the express terms of the lease. This concept has been used in federal
oil and gas leases since the 1930s. In 1984, DOI solicited comments on a pro-
aposed new coal lease form, which form included the "hereafter in force" clause. Commentators responded by stating that the terms and conditions of the leases
cannot be altered until the leases are subject to readjustment. In light of those
comments, DOI decided to include in the form coal lease the "when not inconsis-
tent" clause, as in other federal mineral leases.

The use of the "hereafter in force" clause as a means of incorporating into
the lease future regulations is also inconsistent with the cancellation provision of
the 1920 Act. Under section 31(a) of the 1920 Act, a lease is subject to cancellation
"whenever the lessee fails to comply with any of the provisions of this [Act], of
the lease, or of the general regulations promulgated under this chapter and in force
An implication of that provision in the 1920 Act is that leases were not to be subject to cancellation for failure to comply with regulations promulgated after the date of the lease.

The foregoing indicates that neither the "unless otherwise provided" clause of section 7 of the 1920 Act nor the "hereafter in force" clause in the preamble of post-1964 leases, provides much of a foundation on which to build an argument that the pre-FCLAA leases are, by their own terms, subject to the requirements of section 6 of FCLAA. It is also noteworthy that in concluding that FCLAA mandatorily applies upon readjustment of pre-FCLAA leases, the Solicitor does not rely upon the "unless otherwise provided" clause or the "hereafter in force" lease provision.

With the exception of some early lease forms, pre-FCLAA leases reserved to the United States "the right reasonably to readjust and fix royalties . . . and other terms and conditions at the end of 20 years [and] at the end of each succeeding 20-year period. . . ." Even absent the specific reference to "reasonably," DOI's powers upon readjustment would probably be subject to standards of reasonableness, good faith, or their equivalent. While the lease terms limit readjustment to a reasonableness standard, the lease does not particularly limit the terms subject to readjustment. The royalty and diligent development provisions would clearly be subject to "reasonable" readjustment. However, because the leases specifically provide for readjustment at twenty year intervals, it is arguable that DOI may not upon readjustment shorten the interval between readjustments to less than twenty years, even though a shorter interval may be "reasonable."

As a standard, reasonableness shares the same problem of perspective as beauty and the beholder’s eyes. What may appear entirely reasonable to DOI, from its policy-making perspective, may well seem simply outrageous to the lessee, from its more narrow, profit-oriented perspective. Some guidance on through whose eyes the reasonableness of the readjusted terms is to be viewed is provided by the Rosebud decision. In setting forth the context in which the pre-FCLAA lease was to be examined, the court stated:

The lease and the transactions in connection therewith created a commercial relationship. The Secretary, before the trial court, asserted that he was seeking in this transaction to "deal realistically in a business context." We should, as did the trial court, consider the entire contract in the context suggested by the Secretary. . . .

103 See Union Oil Co. v. Morton, 512 F.2d 743 (9th Cir. 1975) (holding that a similar clause in a federal oil and gas lease did not refer to future regulation because otherwise it would be invalid as inconsistent with the similar cancellation provisions of 43 U.S.C. § 1334(a)(2)); but see Alaska v. Andrus, 580 F.2d 465 (D.C. Cir.), vacated, 439 U.S. 922 (1978).
104 See Solicitor's Opinion, supra note 54.
105 See supra note 13 (emphasis added).
ing Act, we used the typical contract law doctrines applicable to commercial transactions.\textsuperscript{106}

In addition to this "business context," lease readjustment should also be considered as a true readjustment process and not the creation of a new lease or bargain. Federal coal lessees frequently have made considerable investments in the coal mines and entered into long-term contractual commitments to produce and sell coal in reliance upon such federal leases. Reliability of such long-term investments may well have been a principal reason why Congress provided in the 1920 Act for coal leases with indeterminate terms, rather than with a fixed term and a preferential renewal right.\textsuperscript{107} To the extent the readjustment process allows DOI the unrestricted right to propose a new economic bargain, which the lessee must accept or relinquish the lease, the process more closely resembles a preferential renewal right, which was not originally intended. Rather, the objective in the readjustment process should be to adjust the existing lease terms so that the original economic relationship is preserved in light of changing market and economic conditions. The reasonableness of the adjustments should be measured against the extent to which they successfully achieve that objective. Since the royalty rates for pre-FCLAA leases were ordinarily stated on a cents-per-ton basis, the lease readjustment process was likely the intended method for adjusting for the effects of inflation and changes in price levels.

As the district court in \textit{FMC} held, application of this reasonableness standard in most cases requires a specific evaluation by DOI of each particular lease upon readjustment, as was DOI's practice in the past. Moreover, rules governing administrative decision-making may also require a factual study or evaluation of the lease to support DOI's readjustment decision.\textsuperscript{108} Such a case by case readjustment process, of course, is more burdensome on DOI than its present practice, and administrative convenience may have had an important role in DOI's formulation of its present policies.\textsuperscript{109} However, a specific review of a lease every twenty years does not seem to be an unreasonable requirement of DOI as a party to the lease.\textsuperscript{110}

The lease terms required by FCLAA, or perhaps even more stringent terms, may satisfy this standard of reasonableness in some circumstances. However, problems in incorporating some of the FCLAA-mandated provisions, the minimum

\textsuperscript{106} \textit{Rosebud}, 667 F.2d at 951.
\textsuperscript{107} See supra text accompanying note 78.
\textsuperscript{109} See supra note 42 and accompanying text.
\textsuperscript{110} DOI may be able to ease the burden of individual lease evaluations and lessen the risk of an untimely readjustment (and consequently a complete waiver of its right to readjust the lease terms), by offering to lessees, in advance of readjustment, a standard proposal with terms somewhat more attractive to the lessee than section 6 of FCLAA (e.g., a royalty rate somewhat below 12 1/2\% in exchange for the lessee's acceptance of the proposal and agreement to waive a specific lease evaluation. If a lessee rejects the proposal, DOI could then perform a specific lease evaluation and on that basis impose readjusted terms which may or may not be as attractive as the original proposal.
royalty rates in particular, are evident. Congress adopted the minimum royalty rate of twelve and one-half percent of value for surface mined coal without extensive consideration.\textsuperscript{111} It is widely believed that the rate was simply borrowed from the one-eighth royalty common in the oil and gas industry without careful consideration of the significant differences between the two industries.\textsuperscript{112} The twelve and one-half percent rate was higher than the royalty rates normally prevailing in the industry prior to FCLAA, and DOI itself had stated that the twelve and one-half percent rate would be excessive.\textsuperscript{113} More recently, the Commission on Fair Market Value Policy for Federal Coal Leasing (commonly known as the Linowes Commission after its Chairman, David F. Linowes) concluded that the twelve and one-half percent minimum rate may be excessive in many areas and considered recommending a lower rate of eight percent.\textsuperscript{114} The foregoing, together with the present slowness in Western coal markets, support DOI’s earlier conclusion that economic evaluations for individual leases would generally indicate royalty rates less than twelve and one-half percent.\textsuperscript{115} Accordingly, it may be difficult for DOI to demonstrate the reasonableness of the twelve and one-half percent rate on many pre-FCLAA leases.

With respect to the time period for diligent development, however, the situation may be different. Upon readjustment, DOI now adjusts the lease terms to provide that diligent development (mining of coal in commercial quantities) must be achieved within ten years of the readjustment date. This, of course, may not be a problem for producing coal leases. Absent unique and extenuating circumstances, however, it may be difficult for a holder of a nonproducing lease to persuade DOI or a court that such a requirement is unreasonable, since that holder has already had twenty years in which to develop the lease and to commence commercial production.

C. \textit{Public Benefits}

Apart from the legal issues regarding the applicability of the minimum royalty and diligent development requirements of section 6 to pre-FCLAA leases, consideration should also be given to whether such an application provides any significant public benefits. The minimum royalty rate of section 6 is not based on the particular economic value of the reserves or other market related consideration, but


\textsuperscript{112} Id.


\textsuperscript{114} Linowes Report, supra note 111, at 317.

\textsuperscript{115} 1 Secretarial Document, supra note 28, Issue Papers at 141-57.
is a minimum economic burden Congress rather arbitrarily placed on future federal coal leases. Because of the extensive federal coal reserves in the West, the federal government is able to maintain an otherwise economically excessive royalty on federal leases. The Linowes Commission determined that: "Federal market power in most of the West is sufficient to dictate royalties throughout the market. Indeed, without such market power, a Federal royalty of 12.5 percent could not have been sustained." In assessing the social desirability of also arbitrarily imposing that minimum royalty cost on pre-FCLAA leases, careful consideration of how the benefits and burdens of that royalty are shared is necessary.

Federal revenues from mineral leasing (royalties, rent, and bonus payments) are distributed as follows:

(i) thirty-seven and one-half percent to the state in which the leased minerals are located for use "by such State or subdivisions thereof for the construction and maintenance of public roads or for the support of public schools or other public educational institutions, as the legislature of that State may direct. . . ."[118]

(ii) twelve and one-half percent to the state for use "by such State and its subdivisions as the legislature of the State may direct giving priority to those subdivisions of the State socially or economically impacted by development of minerals leased under this Act for (1) planning, (2) construction and maintenance of public facilities, and (3) provision of public services. . . ."[119]

(iii) forty percent to the Reclamation Fund, a special federal account for western water projects supervised by the Bureau of Reclamation of DOI.[120]

(iv) ten percent to the federal treasury.[121]

States in which federal coal reserves are located, primarily western coal producing states, receive a total of fifty percent of the revenues from federal coal leases and are the major beneficiaries of higher federal coal royalty rates. While a portion of these payments to the states is intended for specific areas impacted by mineral

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116 Linowes Report, supra note 111, at 313-19. The burden of the royalty is made even more onerous by the manner in which DOI requires the royalty to be calculated. Ordinarily, the contract sales price is used as the gross value for royalty purposes. 43 C.F.R. § 3485.2(g) (1983). No deductions or adjustments are allowed for production taxes, such as state severance taxes, see infra note 126, the federal reclamation fee, 30 U.S.C. § 1231 (1982), the black lung excise tax, 26 U.S.C. § 4121(e) (1982), or for the royalty itself, even if it is directly passed through to the customer (creating a royalty on a royalty). See Knife River Coal Mining Co., 86 INTERIOR DEC. 472 (1979); 47 Fed. Reg. 33,158 (1982). These taxes and the royalty increase mining costs and correspondingly increase the price of coal. Such increases in price, however, also increase the federal royalty, since it is calculated as a percentage of the total price.

117 Linowes Report, supra note 111, at 315.


119 Id.

120 Id.

121 Id.
development, in practice states tend to use the funds for the benefit of the state generally. Furthermore, the western coal producing states benefit indirectly from the forty percent of the revenues paid to the Reclamation Fund, since many of these states would likely benefit from water projects supported by that fund. However, expenditures from the fund are not tied to amounts received from coal production in individual states.

Development of federal coal reserves may cause rapid growth or "boom-bust" economic cycles which strain the ability of a state and its subdivisions to provide adequate public and governmental services. The states' share of federal lease revenues is intended to help alleviate that burden. Many coal producing states, however, have also imposed substantial severance taxes on coal production. The thirty percent coal severance tax imposed by the state of Montana is the most notorious, and was upheld by the Supreme Court in Commonwealth Edison v. Montana. Also, through state industrial siting laws and local land use planning and zoning authority, Western states and their subdivisions have been able to further mitigate adverse impacts from energy development. In short, using their own governmental authority, the western coal producing states have adapted quite well to the impact of the development of federal coal leases, and the revenues generated for the states by such development may well exceed any related economic burden.

Nonfederal owners of coal reserves in the West also benefit from the high federal royalty. Major private owners of coal in the West are three large western railroads,

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123 Linowes Report, supra note 111, at 327.
125 Linowes Report, supra note 111, at 321-26; Israel, supra note 122, at 27-33. In 1980, Western states collected about $50 million in severance taxes on federal coal production, which exceeded the total coal royalties collected by the federal government—half of which are paid directly to the states. Linowes Report, supra note 111, at 322.
126 MONT. Code Ann., §§ 15-35-101 to -122 (1983) (due to certain deductions the effective severance tax is somewhat less than 30%). Wyoming imposes a severance tax on coal production of 10.5%, WYO. STAT. §§ 39-6-301 to -307 (Cum. Supp. 1984). When combined with local taxes, the Wyoming severance tax is approximately 17%. Linowes Report, supra note 122, at 322. Colorado, New Mexico, and North Dakota set a uniform rate per ton for coal severance taxes, but index the tax to follow changes in the producer or wholesale price index. The effective coal severance tax rate on surface mines for 1982 was 79.2c per ton in Colorado, 91c per ton in New Mexico and $1.01 per ton in North Dakota. Israel, supra note 122, at 29. Utah does not have a coal severance tax.
128 See Barnhill, The Role of Local Government in Mineral Development, 28 ROCKY Mtn. Min. L. Inst. 221 (1982). For example, Western Fuels-Utah, Inc. was required to commit to various local governmental entities in northwestern Colorado a total of $15 million in prepayment moneys for capital facilities, and to make annual operation and maintenance payments to "mitigate" the socioeconomic impact of the Deserado Mine, Bonanza Station, and associated facilities. Id. at 260.
129 Linowes Report, supra note 111, at 326, 329.
Burlington Northern, Union Pacific, and Santa Fe, which are successors to the original western railroad land grants. Because these railroad holdings generally form a “checkerboard” pattern of ownership with federal reserves, the railroads are directly affected by federal leasing practices. Western states also own significant coal reserves, which are commonly adjacent to or in the vicinity of larger federal coal reserve areas. These nonfederal reserves have historically been leased at rates roughly comparable to the going federal rate. Since the federal rate rose to twelve and one-half percent, these nonfederal reserve owners have similarly been able to raise the rates on their reserves. Thus, FCLAA is something of a windfall for these nonfederal coal owners since it allows them to earn royalties in excess of what would otherwise likely be the actual value of their reserves.

The federal treasury, directly receiving only ten percent of coal royalties, is not a significant beneficiary of coal royalties, particularly since the federal government bears the entire cost of administering the federal coal program. That administrative cost, which is paid by the federal treasury, probably exceeds the treasury’s ten percent share of the revenues.

The cost of the federal coal royalties, along with the corresponding higher “tag along” royalties on nonfederal Western coal, is borne by the mining companies, their customers (primarily electric utilities) and ultimately the electricity users in coal consuming states. High federal coal royalties under the present conditions do not seem to provide significant benefits to the federal treasury, federal taxpayers in general, or the national economy. Rather, working in concert with Western coal severance taxes, these royalties may have the general effect of transferring wealth from electrical power users in coal consuming states to the governments of coal

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110 Linowes Report, supra note 111, at 337-38. These three railroads hold approximately 16 billion tons of coal reserves, comprising about 25% of the nonfederal reserves in the West. Burlington Northern, Inc., whose coal is held by its subsidiary, Meridian Land & Mineral Co., is second only to the federal government in the extent of its coal ownership. Id. See generally P. GATES, HISTORY OF PUBLIC LAND LAW DEVELOPMENT 341-86 (1968).

111 Linowes Report, supra note 111, at 337-38.

112 The cost of administering the coal program probably exceeds the revenues to the federal treasury from that program. In fiscal year 1983, the federal coal program generated $84.2 million in revenues, of which the federal treasury received directly 10%, or $8.42 million. The costs of the coal program for BLM alone were $24.9 million, which does not include royalty collection costs. Hence, in fiscal year 1983, for every dollar the federal treasury received from the coal program it spent nearly three dollars to administer that program. The effect on the federal treasury is even worse, however, if it is taken into account that the royalties paid by a mining company are expenses which reduce the mining company’s income taxable by the federal government. Linowes Report, supra note 111, at 328-29. This situation not only raises questions about the present royalty distribution formula, but also indicates that the effort required to administer the federal coal program, with its seemingly never-ending and expensive planning efforts and litigation, far exceeds the national significance of that program.

113 Even if the royalty expense is borne by the mining company, such that a reduction in the royalty would increase the company’s profits rather than benefit the customer, the federal treasury would benefit by a lower royalty since the corresponding increase in profit presumably would be subject to federal income tax, perhaps at the marginal corporate tax rate of 46%. See Linowes Report, supra note 111, at 328.
producing western states. In any event, the high federal royalty increases the contribution by those who ultimately pay the royalty for the general expense of government in western coal producing states.

Section 6 of FCLAA unambiguously mandates a high minimum royalty for new leases, a mandate the Secretary of course must follow. However, there is no such unambiguous congressional declaration that such high royalties should be arbitrarily imposed on pre-FCLAA leases. Perhaps, before committing to a course of automatically applying that minimum royalty to pre-FCLAA leases or seeking the highest royalty sustainable upon readjustment, the Secretary should consider whether such high royalties on pre-FCLAA leases are truly in the national, public interest.

Neither is it clear that the diligent development requirement of section 6 is in the general public interest. The Department of Justice reviewed the economic and market effects of the diligent development provision and concluded that such a requirement lessens competition, results in inefficient markets, and in general creates no potential social benefits. The fundamental problem with FCLAA's diligent development approach (lease termination if production in commercial quantities is not achieved in ten years), is that it forces the lessee to develop a lease in response to that governmentally established time frame rather than in response to the market. An obvious lesson of the last decade is that normal market forces allocate energy resources more effectively than does the federal government.

IV. SECTION 3 OF FCLAA

Section 3 of FCLAA prohibits DOI from issuing a lease to any entity which "holds a lease or leases issued by the Untied States to coal deposits and has held such lease or leases for a period of ten years [not counting periods before August 4, 1976] when such entity is not [with certain exceptions] producing coal from the lease deposits in commercial quantities." The prohibition in section 3 may apply not just to coal but also to oil and gas, oil shale, phosphate, and other minerals leased under the 1920 Act. The true effect of section 3 is on undeveloped, pre-FCLAA leases, since post-FCLAA leases would already be subject to the ten year diligent development requirement of section 6 of FCLAA. The bulk of these

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134 U.S. DEP'T OF JUSTICE, COMPETITION IN THE COAL INDUSTRY, 9-14 (December 1982) [hereinafter cited as Justice Dep't Report].
135 30 U.S.C. § 201(a)(2)(A) (1982). The exceptions from the production requirement are interruptions caused by strikes, the elements or casualties of which are not attributable to the lessee. Id. § 207(b).
136 The prohibition in section 3 extends to "a lease or leases under the terms of this [Act]. . . ." 30 U.S.C. § 201(a)(2)(A) (1982). There is some ambiguity whether the words "this [Act]" refer to FCLAA, which would limit the scope of the prohibition to federal coal leases, or to the 1920 Act, which would expand the scope of the prohibition to all federal mineral leases. DOI has interpreted the prohibition in section 3 to refer to all leases issued under the 1920 Act, not just coal leases. Letter from Lawrence G. McBride, Asst. Solicitor, to Charles Cook, Vice President, American Mining Congress (April 8, 1980).
pre-FCLAA leases were issued in the 1960s and therefore will be subject to readjustment in the 1980s. Upon such readjustment, DOI would have the opportunity to readjust the diligent development provisions. While section 3 appears to be only an interim measure, its impact is substantial and it is an issue of immediate concern to mining and energy companies.118

Section 3 was enacted to address what Congress perceived as rampant speculation with existing federal coal leases.119 This congressional concern was only natural in light of the economic climate of the mid-1970s. The nation was then rebounding from the effects of the Arab oil embargo of 1974 and the resulting "energy crisis." The country's vast coal reserves, much of which were owned by the federal government, were expected to play a significant role in the country's drive for energy independence. When Congress examined the federal coal program, however, it saw reports showing that while federal coal acreage under lease had increased dramatically, there was not a corresponding increase in coal actually produced from federal lands.120 Congress, concerned that companies may have been hoarding the leases to earn speculative profits in the rising coal markets rather than putting those leases into production to solve the nation's energy problems, enacted section 3 to discourage speculation and to encourage coal production.

Subsequent analyses have questioned whether such speculation was all that harmful or rampant, and have argued that in any event speculation is socially beneficial and makes for more efficient markets.121 Regardless of whether section 3 was justified in 1976 when enacted, its full effect will be felt in 1986 and the wisdom of section 3 should be considered in light of current conditions.

As respects the western coal industry, history did not unfold in the 1980s the way governmental planners had envisioned in the 1970s.122 Coal production in the West did not increase at the rate forecasted in the 1970s, and some western coal producing areas, where federal leases predominate, are currently plagued by substantial production capacity in excess of demand.123 If section 3 is enforced and holders of affected leases decided to meet the commercial production requirement, the result would be an even greater surplus of coal producing capacity and attendant distortions and inefficiencies in the coal market.124 However, if such leaseholders elect to relinquish such leases, the result could be a shortage of western coal at competitive prices in the late 1980s and early 1990s.125 Such results are not surprising

120 Id.
121 Id.
122 Id. at 25.
123 Id. at 303.
124 Id.
125 Id.
when it is remembered that under section 3 federal coal lessees are putting leases into production in response to government edicts, not market conditions. The Department of Justice has considered at some length the impact of diligent development requirements, including section 3, and has recommended that Congress repeal all diligent development and continued operation requirements because these “diligence requirements apparently create no potential social benefits but do create substantial, potential costs. . . .” 146

Apart from concerns about lease speculation, several other justifications are commonly offered in support of section 3. Supporters claim that enforcement of section 3 “will offer an unparalleled opportunity for the Government to recoup millions of dollars in lost revenue through the resale of non-diligent leases. . . .” 147 This argument attributes to federal leaseholders a more generous attitude toward the federal government than would be warranted by their historically avaricious actions. The section 3 penalty applies only if the lessee “holds and has held” the nonproducing lease for ten years. 148 Consequently, the impact of section 3 could be avoided by the leaseholder assigning the nonproducing lease to another company. The assignor would no longer “hold” the nonproducing lease and would therefore be free from the section 3 penalty. The assignee, not having held that particular lease for ten years, would also be free of the section 3 penalty, at least for ten years. Accordingly, lessees affected by section 3 could avoid its impact by simply swapping leases. More likely, enforcement of section 3 would cause speculators, particularly those for which the section 3 penalty is not significant (they have no need to acquire future federal mineral leases), to acquire such leases from affected companies at highly discounted prices, expecting to subsequently resell them at a profit, perhaps even to the original lessee, at a time when the buyer is prepared to commence mining. Thus, ironically, enforcement of section 3, which was intended to discourage speculation, will likely cause speculators who may have been leaving the federal coal lease market to reenter that market. In any event, it is unlikely that any federal lease of value (which could be subsequently reissued by the government for a substantial bonus) would simply be surrendered by the leaseholder.

Section 3 is also defended as a mechanism to counter the perceived problem of the concentration of federal coal leases in the control of a few large companies. 149 With respect to federal lessees, “bigness” is not necessarily the equivalent of “badness.” The development of large federal coal leases frequently requires large operations with sizable capital investments. The participation of such large companies in the western coal industry is helpful since they often are best able to actually put large federal coal leases into production. However, there may be a genuine

146 Justice Dep't Report, supra note 134, at 14.
149 SIERRA CLUB, supra note 147, at 6.
concern about the anticompetitive behavior which could result if a few companies were able to dominate the western coal market by controlling extensive federal coal lease acreage. All evidence now suggests that the western coal markets are highly competitive and, in any event, section 3 is not an effective prevention against such anti-competitive consequences. Indeed, section 3 may cause a greater concentration of federal leaseholdings. Some lessees, electing to relinquish federal coal leaseholdings in order to assure their right to participate in the leasing of other federal minerals, may transfer their leases to other companies, which may elect to hold their federal leaseholdings and forego for the present any future mineral leasing. More importantly, section 11 of FCLAA places restrictions on the total federal acreage a lessee may control and section 15 prohibits DOI from issuing, renewing, or readjusting any coal lease until the Attorney General has had an opportunity to advise whether such action would create or maintain a situation inconsistent with the antitrust laws. These two provisions are more effective and appropriate methods than section 3 to address any problem arising from a concentration of ownership of federal coal leases.

Moreover, for leaseholders which are diversified energy or mining companies and which also participate in the leasing of other federal minerals, section 3 may impose a particularly harsh penalty, since the penalty may extend to all federal mineral leases, not just coal leases. In contrast, for leaseholders who may not have an immediate need for future federal mineral leases the penalty of section 3 is of little or no significance. There is no rational basis for this apparent discriminatory impact of the section 3 penalty on diversified companies. On the contrary, lack of competition at federal lease sales has been a problem, not only for coal leases but for other mineral leases. At a time when DOI is trying to enhance competitive bidding at such sales, section 3, which by design will exclude some companies which have historically been the most active in federal mineral lease sales, seems strangely out of place. Additionally, section 3 may also preclude a company from acquiring "bypass leases," small lease tracts which cannot be mined economically apart from present adjoining mining operations and which would be bypassed and probably never mined if not leased to that adjoining mine. Thus, a federal lessee impacted by section 3 may be prevented from acquiring such a bypass lease, even though its issuance would benefit the federal government and further conservation policies.

In sum, section 3 will not likely provide any public benefit but, on the whole, may be detrimental. The intended objective of section 3 can be accomplished with more desirable consequences by other means. Largely for that reason legislation to repeal section 3 was introduced, though not enacted, in the 98th Congress.

152 See supra note 136 and accompanying text.
Also, the Linowes Commission recommended entirely repealing section 3 and substituting escalating advance royalties on existing leases upon their readjustment. These actions suggest an increasing awareness of the need to introduce some flexibility into the application of section 3 in order to mitigate its arbitrary and harsh consequences.

V. CONCLUSION

Mandatory application of the minimum royalty and diligent development requirements of section 6 to pre-FCLAA leases upon readjustment may not be legally required and may not be socially desirable. Neither does it appear that section 3, which was intended to force development of pre-FCLAA leases, will produce any beneficial results. History may reveal those provisions of FCLAA as sensible only in the context of the unique “energy crisis” attitude prevailing in the late 1970s. But there is no need to risk compounding those possible errors of policy, made at the height of such perceived crisis, by unnecessarily and thoughtlessly imposing those policies on pre-FCLAA leases.

155 Linowes Report, supra note 111, at 303-04.