TESTIMONY OF BOBBY L. MAXWELL
BEFORE THE SUBCOMMITTEE ON ENERGY AND MINERAL RESOURCES
UNITED STATES HOUSE OF REPRESENTATIVES
MARCH 28, 2007

Mr. Chairman and subcommittee members, thank you for the privilege and opportunity to be here today. This is an opportunity for me to participate in a hearing that will hopefully make the Mineral Management Service (MMS) a better servant of the U.S. taxpayer. MMS is responsible for collecting royalty payments for the U.S. Government and brings in revenue only second to the Internal Revenue Service.

I served the American taxpayer with over thirty years of service, including three years in the U.S. Army. I believe one of the greatest joys in life was the opportunity to work for the government as a citizen of this great country. My only regret is that my career was cut short due to exposing the Federal government's current cozy relationship with the oil and gas industry and its unwillingness to consistently enforce laws and regulations requiring the industry to pay royalties due on Federal oil and gas leases.

I audited the oil & gas industry for over 25 years. I became an expert in reviewing industry contracts, revenue accounting and production systems. I understand professional auditing, industry contracts and how to determine what monies are owed the Federal government under oil and gas leases.

I have a Bachelor of Business Administration degree in accounting from Chaminade University of Honolulu, a Master's in Business Administration from Texas A & M University, and I am a certified public accountant in the states of Oklahoma and Hawaii. I received many awards from MMS for being highly effective as a manager and for audit results. In June 2003, I received the Department of the Interior Meritorious Service Award from the Secretary of Interior, Gail A. Norton.

Around the year 2000, MMS began to change. The auditing function began to be de-emphasized and the enforcement of the lease terms and regulations seemed to become less important. To replace professional audits, top management advocated a new system. This system was called a "compliance review" and often resulted in professional auditors being replaced with other staff. The new staff often did not have an educational background containing college level accounting or auditing courses. All senior managers were "directed" that they would support the new process as part of their jobs. It was clearly stated that no dissent would be tolerated. I do believe that there is an appropriate need and use for compliance reviews, but they should never be used as a replacement for professional audits.

With the new compliance system we were told not to bother the oil companies. We were told not to be requesting documents as we formerly had with audits. Audit staff was reduced. Many auditors stopped traveling to companies for audits, stopped interviewing oil company staff, stopped visiting marketing departments and field personnel. Audits were marginalized, and accounting and auditing degrees were no longer required. For

four years, MMS received a qualified audit report reflecting substandard audit work. In 1992 audits covered 90% of all royalty payments, currently audits and compliance reviews are only covering 72% of royalty payments. Remember that the compliance review is not an audit and does not provide the same level of assurance that royalties were correctly paid. Further, royalty underpayment collections have decreased by over $100 million per year.

By the year 2002, we were no longer allowed to audit certain areas. For example, we were not allowed to review or audit many Royalty-in-Kind contracts. In an attempt to review the contracts and transportation agreements, I was ordered not to get any information from the Royalty-in-Kind division of MMS, or review their contracts for sales of the oil and gas. In an attempt to overcome this major scope limitation on our audits, a meeting was schedule with the Office of the Inspector General and Royalty-in-Kind personnel in Lakewood, Colorado. Audit staff traveled from Oklahoma City, Oklahoma, for the meeting. Neither the Office of Inspector General nor the Royalty-in-Kind personnel showed up for the meeting. I was told not to pursue the issue any further.

This was reminiscent of being directed to not pursue an issue many years earlier. In the early 1990's, I was directed not pursue the issue of oil companies exchanging crude oil by contracts using artificially low exchange values. This resulted in MMS receiving royalties based on a value far below the fair market value of the crude oil. A former employee of ARCO Oil & Gas Corporation filed a False Claims Act lawsuit against the oil companies based on this issue and collected over $400 million for MMS. This was over $400 million that MMS would never have collected on its own initiative.

In 2003, I was chastised for attempting to bill a corporation for interest due on millions of dollars it paid as a result of an audit. However, the audit staff convinced the company to voluntarily remit the interest payment without a bill from MMS. I was told that a system was in place for billing interest and the audit staff should never issue bills for interest relating to royalty underpayments we collected. However, everyone in MMS knew that the system wasn't working and the government was behind many years in the billings and apparently millions of dollars in interest would never be collected. The fact that many millions of dollars in interest would be years late being collected – if ever collected at all – was of no concern to senior management. The Jicarilla Apache Nation complained directly to the Director of MMS and I was allowed to bill all companies for interest due the Jicarilla Apache Tribe.

Every year we were pressured to do less auditing and state that royalties were accurately reported and paid by the oil companies using the compliance review process. In some cases the compliance reviews were adequate and useful in determining if royalties were correctly reported and paid. In other situations, it was only used as a method of smoke and mirrors to state that royalties were in compliance. I was told that finding and collecting royalty underpayments wasn't important, but meeting our Government Performance Results Act standards was what mattered, our operating budget depended upon it. Further, we were directed that MMS would not issue any subpoenas to oil and gas companies for records.

Pressure continued to mount in 2002 & 2003 to not pursue royalty underpayments to the U.S. government by the oil and gas industry. The most well known case is the Kerr-McGee Corporation (Kerr-McGee) royalty underpayments. I developed an order requiring Kerr-McGee to pay MMS an additional $10 million. I was pressured not to issue the order even though it was fully supported by the lease terms and regulations. The pressure came down from the Director of MMS not to pursue these underpayments against Kerr-McGee. I was never told that the order was not supported by the MMS regulations or justified – just not to issue the order. No criteria was ever provided to me stating why the additional royalty should not be collected from Kerr-McGee.

As you know, I filed a False Claims Act lawsuit against Kerr-McGee on behalf on the U.S. government to collect the royalty underpayments by Kerr-McGee. Within days of the lawsuit becoming public, I was notified that I was being terminated from employment with MMS. MMS was determined not to require Kerr-McGee to pay the royalty underpayments. The Department of Justice did not intervene in the lawsuit, but allowed me to take the lawsuit forward on behalf of the American public. This has become a political issue within the Department of Justice.

I personally continued the lawsuit against Kerr-McGee Worldwide Corporation on my own time and at my own expense. It has been a long and difficult road, with absolutely no assistance from the Federal government. On January 23, 2007, a jury in the United States District Court for the District of Colorado found Kerr-McGee guilty of underpaying the Federal government $7,555,886.28, and that Kerr-McGee had failed to disclose to the United States Government all relevant information to determine the value of royalties due. Kerr-McGee's guilt of underpaying royalties and withholding vital information from MMS was quickly determined when the evidence was presented before an impartial judge and jury.

It is important to note that these twelve courageous citizens had no hesitation in finding Kerr-McGee guilty. The overall deliberations were less than four hours, and all indications are that the jurors determined Kerr-McGee was liable in less than two hours into their deliberations. Kerr-McGee's trial evidence did not seriously question the royalty underpayments I had calculated, did not dispute the fact that it had not engaged in reasonable and prudent marketing of this Federal oil, and did not dispute that the buyer, Texon Corporation, L.P. (Texon), had provided other significant consideration, including the assumption of essentially, all of Kerr-McGee's transportation responsibilities. No, Kerr-McGee's primary defense was that MMS had decided not to issue an order to pay.

Kerr-McGee clearly lost in district court, but now is trying for a technical win as a way of not paying its royalties due the American taxpayer.

Not withstanding the fact that the American public has spoken on this issue, even today MMS still states that Kerr-McGee owes no additional royalty. However, MMS never attended the trial; MMS never reviewed the almost 60,000 documents I received under the trial discovery process; MMS never read the thousands of pages of depositions; MMS

never listened to the trial testimony or reviewed the trial transcripts. In essence, MMS is the proverbial ostrich with its head in the sand. It sees nothing and hears nothing, but is sure no additional royalty is due. With this type of behavior, it is scary to know that MMS is responsible for protecting the American public's assets and collecting royalties due.

Kerr-McGee's testimony at trial clearly stated that its personnel knew additional royalty was due, but elected not to pay the U.S. Government. Kerr-McGee's accounting and marketing personnel stated that they knew Kerr-McGee received additional value for the oil in the form of services provided by Texon. Further, they testified that they knew royalty was due on this additional value. However, no attempt was ever made to pay MMS the full royalty value. The manager of revenue accounting at Kerr-McGee, Mr. Terry Kyle, even directed an employee to not provide answers to MMS for questions about additional incentives or consideration that Kerr-McGee received in exchange for its sale of the Federal oil to Texon.

Kerr McGee's attorney, Mr. Gorenson, provided an affidavit with respect to one of Kerr-McGee's district court motions indicating that he had full knowledge of the Texon contract terms many years ago. As a Kerr-McGee attorney he made no attempt to have Kerr-McGee pay the proper value of royalties. Rather, he worked to increase Kerr-McGee's profitability at the expense of the American taxpayer.

I personally believe that the knowledge of the contracts and royalty underpayments by Mr. Gorenson and Mr. Kyle are sufficient to show that they knowingly and willfully filed false Federal royalty reports and underpaid the royalties due the American taxpayers. Further, the Director of MMS by stopping a valid order for royalty underpayments makes one wonder if collusion between MMS and Kerr-McGee took place. It is a matter that I personally believe should be closely evaluated. In this instance, a career senior manager, myself, was instructed not to issue a valid order for payment of the additional royalty. Kerr-McGee knew the royalty was underpaid and the Director of MMS personally stopped the order from being issued.

Kerr-McGee has taken a stand that it owes no royalty on the deep-water leases that were issued without threshold values for royalty payments. These leases were issued by MMS in error by not including a threshold value for determining royalties due the Federal government. Some companies have renegotiated similar leases in an attempt to correct the error and bring an element of fairness to the American taxpayer. However, Kerr-McGee is aggressively pursuing the issue indicating that it will not pay any royalties to the American taxpayers on its deep-water leases with the missing threshold dollar value. However, Kerr-McGee will receive billions of dollars in revenue from the sales of oil and gas from these assets that belong to the American public.

I sincerely hope that this Congress will hold Kerr-McGee responsible for paying all royalties that it owes. I believe, and a jury of 12 American citizens agreed, that Kerr-McGee filed false royalty reports with MMS and did not pay its full royalty obligation. Further, I believe that behind closed doors in Washington D.C. the decision was made

that Kerr-McGee would be let off the hook and not required to pay the royalties it owed. It was totally inappropriate for the Director of MMS, as a political appointee, to intervene and revoke my authority to issue a legal order to Kerr-McGee to pay the additional $10 million. Also, I hope Congress will review MMS' compliance program and encourage them to have a highly professional workforce and a truly professional audit program independent of political pressure.

This concludes my formal testimony. Thank you for the opportunity to appear here before this Subcommittee. I will be happy to answer any question you may have.