INTERIOR BOARD OF INDIAN APPEALS

Shirley Delgado v. Acting Anadarko Area Director, Bureau of Indian Affairs

27 IBIA 65 (12/12/1994)

Earlier judicial case:

Stayed for decision by Department, *Delgado v. United States*, No. 91-1650L (Ct. Cl.)

Judicial review of this case:

Affirmed, *Delgado v. United States*, No. CIV-95-262-A (W.D. Okla. Feb. 5, 1997)
Affirmed, 153 F.3d 726 (Table), 1998 WL 439661 (10th Cir. 1998)

United States Department of the Interior

OFFICE OF HEARINGS AND APPEALS
INTERIOR BOARD OF INDIAN APPEALS
4015 WILSON BOULEVARD
ARLINGTON, VA 22203

SHIRLEY DELGADO
v.
ACTING ANADARKO AREA DIRECTOR, BUREAU OF INDIAN AFFAIRS

IBIA 94-80-A Decided December 12, 1994

Appeal from the denial of a request to cancel an oil and gas lease.

Affirmed.

1. Indians: Trust Responsibility

The Federal trust responsibility applies to each bureau or office within the Department of the Interior that has authority to take actions relating to or affecting Indian trust resources.

2. Indians: Leases and Permits: Cancellation or Revocation--Indians: Leases and Permits: Violation/Breach: Generally--Indians: Mineral Resources: Oil and Gas: Generally

25 CFR 212.23(a) does not mandate cancellation of an Indian oil and gas lease whenever there is a violation of the lease terms or the regulations. Instead, when there is such a violation, the Bureau of Indian Affairs has discretion to review the circumstances surrounding the violation and determine whether cancellation is warranted, taking into consideration, inter alia, the trust responsibility to act in the best interest of the Indian landowner(s).

3. Indians: Leases and Permits: Cancellation or Revocation--Indians: Leases and Permits: Violation/Breach: Generally--Indians: Mineral Resources: Oil and Gas: Generally

Absent contrary provisions in the lease, the lessee under a lease of Indian oil and/or gas has the right to cure lease violations, and, once cure has been effected, the lessee is considered to be in good standing.

APPEARANCES: R. Robyn Assaf, Esq., and Marina S. Valley, Esq., Oklahoma City, Oklahoma, for appellant; Beverly Ohline, Esq., Office of the Regional Solicitor, U.S. Department of the Interior, Albuquerque, New Mexico, for the Area Director; Donald L. Kahl, Esq., and Fred M. Buxton, Esq., Tulsa, Oklahoma, for Vintage Petroleum, Inc.; Paul McKinney, Esq., Shawnee, Oklahoma, for William R. Austin, NiJean Petroleum, Inc., Velta Pipeline, Inc., and Sundance Pipeline, Inc.

OPINION BY CHIEF ADMINISTRATIVE JUDGE LYNN

Appellant Shirley Delgado 1/ seeks review of a February 7, 1994, decision of the Acting Anadarko Area Director, Bureau of Indian Affairs (Area Director. BIA), denying her request to cancel Oil and Gas Lease Contract No. 14-20-0208-3947 (lease). For the reasons discussed below, the Board of Indian Appeals (Board) affirms that decision.

Delgado v. United States

On December 2, 1991, appellant filed suit in the United States Claims Court (now the United States Court of Federal Claims). Delgado v. United States, No. 91-1650L. Although the information concerning this case in the administrative record is incomplete, it appears that appellant seeks money damages for the Department's alleged breach of its trust responsibilities by failing promptly and fully to collect royalties due and to cancel the lease. The suit may also seek cancellation of the lease.

The filing of suit in Federal court might deprive the Board of jurisdiction. Here, however, judicial proceedings have been stayed pending consideration of three matters by the Department. This appeal addresses one of those three matters. 2/ Therefore, the Board proceeds with consideration of this appeal.

1/ As discussed infra, the present lessors are Jerry Shawn Trevino; Josephine Kay Trevino; Jesse Smith Trevino, Jr.; Jase Lee Trevino; Brenna Ketcheshawno; Erik Jason Elizondo; Juan Pablo Delgado, Jr.; and Anthony Darren Delgado. Shirley Delgado is the mother of Brenna, Erik, Juan, and Anthony; and the aunt of Jerry, Josephine, Jase, and Jesse. By a Feb. 2, 1993, order, the Kickapoo Tribal District Court appointed Shirley guardian ad litem for Erik, Juan, Anthony, Jase, and Jesse in order to pursue Delgado v. United States, No. 91-1650L (Cl. Ct.), discussed infra. Jerry, Josephine, and Brenna have submitted affidavits authorizing Shirley to represent them in this proceeding. Accordingly, although Shirley is not a lessor, the Board recognizes her as being authorized to pursue this appeal on behalf of the lessors, and addresses her as the appellant.

2/ According to information in the administrative record, the three matters to be addressed by the Department were: (1) the recovery of overdue or underpaid royalties in proceedings before the Minerals Management Service (MMS); (2) probate of the trust or restricted estate of Luther Namaso; and (3) determination of whether the lease should be cancelled.

Background

In order to simplify understanding of various chronologically overlapping events, the Board has divided the factual background discussion into topics. The following recitation of facts omits certain disputed matters, which are more fully developed in the Discussion and Conclusions section, infra.

The Lease. Luther Namaso, successor in interest to Chuck e skin ah a, Mexican Kickapoo Allottee No. MK-254, entered into the lease at issue here with D.B. Jones on September 18, 1980. The lease, which was approved by the Superintendent, Shawnee Agency, BIA (Superintendent), on October 31, 1980, covers the S½ NW¼, sec. 13, T. 10 N., R. 3 E., Indian Meridian, Pottawatomie County, Oklahoma, containing 80 acres more or less. The initial term, of the lease was 5 years; the extended term was "as much longer thereafter as oil and/or gas is produced in paying quantities."

Provisions of the lease relevant to this decision are set forth in the Discussion and Conclusions section, infra.

Lessors. Namaso, the original lessor, died on November 19, 1990. His trust or restricted estate was probated by Administrative Law Judge Sam E. Taylor, who approved a will Namaso executed on December 14, 1989. Appellant was named in the will as Namaso's executrix, was the devisee of the surface interest in 5 acres of land covered by the lease, and was the residuary devisee. Namaso devised the rest of the allotment, including the entire mineral interest, in equal and undivided shares, to his grandnieces and grandnephews Jerry, Josephine, Jesse, Jase, Brenna, Erik, Juan, and Anthony. These eight individuals are the present lessors.

Lessee. The Area Director states that BIA approved an assignment of the lease from Jones to Andover Oil Co. on December 23, 1980. The record shows IBIA approved further assignments on December 9, 1983, to Bill Austin, a.k.a. William R. Austin (Austin); and on April 28, 1988, to Vintage Petroleum, Inc. (Vintage). Vintage is the current lessee.

Production. The parties agree that the Ricki #1 well was put into production on the leasehold during the primary term of the lease, and the Fern #1 well was put into production in June 1986. Both wells produce oil and/or gas, and the lease is currently in its extended term and is held through production.

Communitization. Possibly on or around June 1, 1985, Austin executed a proposed communitization agreement (CA) that would have pooled the 80 acres in this lease with 80 acres of adjoining privately owned lands in the north half of the same quarter section. The CA was apparently submitted to the Oklahoma Corporation Commission (OCC), which issued an order on October 17, 1985, unitizing the ownership interests in the quarter section into a single 160-acre spacing unit in accordance with Oklahoma State law. On November 5, 1985, a Division Order Title Opinion was prepared for NiJean Petroleum, Inc.

(NiJean), the then-designated operator for the lease, by its attorney. This title opinion advised that both the Ricki #1 and the Fern #1 wells were part of the 160-acre unit and that royalty payments should be made to the Indian owners based on one-half of the production from the unit.

There is no evidence that the proposed CA was submitted to BIA for approval until 1988. On March 2, 1988, the Bureau of Land Management (BLM) recommended that the Superintendent not approve the CA because it did not provide adequate protection for the Indian owners. Based on BLM's recommendation, on March 24, 1988, the Superintendent declined to approve the CA.

After being assigned the lease, Vintage resubmitted the CA with some modifications. On May 11, 1988, BLM notified the Superintendent that it was negotiating with Vintage for the inclusion of additional term and conditions that would protect the Indian interests. Vintage agreed to the additional terms, and BLM initially recommended approval of the revised CA. However, based upon concerns raised by the Superintendent in a June 9, 1988, memorandum, BLM reconsidered its recommendation and advised that the CA not be approved. By letter dated September 2, 1988, the Superintendent notified Vintage that the CA was not approved. This CA was not resubmitted after the second disapproval.

In 1992, Vintage proposed another CA, in order to allow the use of a waterflood secondary recovery plan. Appellant was represented by a private attorney in negotiating changes to the proposed CA which increased the royalty percentages payable to the Indian interests. The basis for the increase was apparently that the Ricki #1 and Fern #1 wells were more productive than the other wells which would be included in the communitized area. Appellant signed the amended CA, which was then approved by the Superintendent on February 2, 1993. Under this CA, which is presently in effect, Vintage is the designated unit operator.

<u>Meter Bypass</u>. On September 15, 1989, BLM inspected the Ricki #1 and Fern #1 wells, and discovered that piping had been installed bypassing the meters. Citing 43 CFR 3162.7-5(b)(3) and stating that the violation was "major," BLM issued Vintage a verbal "incident of noncompliance" (INC) and instructed it to remove the piping immediately. A written INC was issued on September 18, 1989. A second BLM inspection on September 18, 1989, showed that the piping was removed before issuance of the written INC.

<u>Lease royalty payments</u>. When its CA was disapproved, Vintage notified BIA that, based on Austin's practice, it had paid royalties as if the proposed CA were in effect. Vintage began paying all royalties to the Indian lessors and making payments against the royalties they had not previously received. It also informed BIA that Austin had underpaid royalties by one-half.

Based on the information provided by Vintage, on April 19, 1989, the Superintendent requested that the Area Director audit this lease. The Area Office referred the matter to MMS for investigation.

By letter dated August 7, 1990, Namaso notified the Superintendent that his own investigations indicated he had been underpaid in excess of $575,000. Based upon this alleged underpayment and the bypass piping, Namaso requested that the lease be cancelled; that efforts be undertaken to recover the amount of royalty owed him plus 12 percent interest; that the value of the gas produced, but not metered, be determined and that amount collected with interest; and that Ramsey Property Management, Inc., be approved as the new operator. The Superintendent transmitted Namaso's letter to the Area Office for submission to MMS for use in its on-going audit.

The MMS audit ultimately found royalty violations in three areas. In all, the audit resulted in the recovery of more than $1,023,000 in underpaid royalties and interest penalties.

1. Volume Allocation. The MMS audit confirmed that royalties had been paid on only one-half of the production from the date of first production until the CA was disapproved on September 2, 1988. By separate letters of November 26, 1991, MMS notified Austin and Vintage that they owed additional royalties. After receiving payment in accordance with the demand letters, MMS assessed interest penalties against both Austin and Vintage. The interest assessed has also been paid.

2. "Dual Accounting." MMS regulations require that when hydrocarbons are sold to certain affiliated companies, the operator must perform "dual accounting." Under the regulations, the operator is required to pay royalties on whichever accounting method yields the greater royalty amount.

When he operated the lease, Austin owned NiJean, which was the operator of the lease, and Sundance Pipeline, Inc. (Sundance) and Velta Pipeline, Inc. (Velta), both of which purchased hydrocarbons from NiJean. NiJean also sold to other companies not affiliated with Austin. When Vintage became lessee in 1988, it apparently purchased Austin's interest in Sundance and Velta, operating them under the name Vintage Marketing, Inc. Vintage continued sales to these companies, as well as to other, non-affiliated, companies.

Based on the failure of either Austin or Vintage to perform dual accounting, MMS determined that they each underpaid royalties. The amounts MMS determined to be owed have been paid, with interest.

3. Condensate Sales. MMS performed a spot audit of 4 months for condensate sales. The audit indicated there was a systemic problem in Austin's payment of royalties on these sales. MMS found that, although there were initial problems with Vintage's reporting of these sales, Vintage changed the way an which condensate was separated and marketed, and had begun adjusting its system before MMS conducted its audit.

MMS informed Austin and Vintage of the amounts determined to be owed for the 4 months that were audited and ordered both of them to review their books and pay actual amounts due for other months. MMS reported that Austin elected to pay the amount MMS extrapolated was due, and Vintage reviewed its records and paid additional royalties based on actual sales.

Major Portion Analysis. MMS concluded a "major portion analysis" of this lease in March 1993. This analysis is discussed infra.

Administrative History. No action to cancel the lease was taken during the MMS audit. By memoranda dated March 11, 1992, the Southwest Regional Solicitor, Department of the Interior (Regional Solicitor), sought input from BLM and MMS as to whether lease cancellation was warranted. Both MMS and BLM recommended that the lease not be cancelled. These recommendations are discussed infra.

The parties were allowed a full opportunity to brief the case before the Area Director. The Area Director's decision not to cancel the lease was issued on February 7, 1994.

Appellant appealed this decision to the Board. Briefs have been filed by appellant, the Area Director, and Vintage. Austin, NiJean, Velta, and Sundance adopted the brief filed by Vintage.

Discussion and Conclusions

In each of her filings, appellant repeats arguments in different contexts. Addressing each argument as it is raised would result in a repetitious and confusing decision. Therefore, the Board does not follow the organization of appellant's opening brief in this discussion. 3/ It first addresses several generalized arguments.

Appellant devotes a large part of her discussion to the relationships between BIA, BLM, and MMS in regard to Indian oil and gas leases. The Board agrees with most of her discussion and her contention that, in general, BLM monitors lease compliance, MMS monitors royalty calculations and payments, and BIA has overall responsibility for leases of Indian lands. BLM and MMS are involved in Indian oil and gas matters because of the specialized expertise they have developed in dealing with similar issues relating to public lands administered by the Department.

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3/ Appellant's opening brief is divided into three sections. In outline, it argues that the Area Director's decision is in error because it 1) is arbitrary, capricious, lacks substantial evidence, and is an abuse of discretion because the Area Director omitted and distorted facts, considered extraneous issues and irrelevant facts, failed to consider all relevant evidence, and drew unreasonable inferences, and because the decision is contrary to the weight of the evidence and lacks substantial evidence; 2) lacks principled reasons; and 3) is contrary to Federal law and regulations, and to the terms of the lease.

Appellant argues that BIA erred in seeking and relying on input and recommendations from BLM and MMS concerning whether the lease should be cancelled, and that BIA's regulations supersede those of BLM and MMS. She contends that, because of its reliance on recommendations from BLM and MMS, the Area Director's decision "provided no principled reasons for the denial of * * * cancellation" (Opening Brief at 33), and his "conclusions amount to conclusory and subjective opinions without legal or factual authority relevant to the BIA and its trust responsibility to the Restricted Indian." Id. at 35.

[1] These arguments appear to be based at least in part on a belief that BLM and MMS are not bound by the Federal trust responsibility. This is not correct. The Federal Oil and Gas Royalty Management Act, 30 U.S.C. § 1701(a)(4) (1988), specifically imposes a duty on the entire Department to "aggressively carry out [the] trust responsibility in the administration of Indian oil and gas." Furthermore, the Department has explicitly acknowledged that each office and bureau within it that deals with Indian lands and/or resources is bound by the trust responsibility, and has created the Office of American Indian Trust, in the Office of the Secretary, to ensure that all offices and bureaus understand and carry out their trust responsibilities. See, e.g., Secretarial Order No. 3175 (Nov. 8, 1993), Departmental Responsibilities for Indian Trust Resources. To the extent appellant argues BIA should not have considered recommendations made by BLM and MMS because those offices are not bound by the trust responsibility, the Board rejects her argument.

Appellant objects that the Area Director's decision contained only 2 pages of background facts, and asserts that the facts presented "are chronologically incomplete and contain irrelevant and superficial information that [has] nothing to do with the issue" (Opening Brief at 20). Obviously, appellant's 17-page factual recitation in her opening brief is more thorough than the one in the Area Director's decision. Just as obviously, appellant places different emphasis on some facts than the Area Director did.

Appellant's clear suggestion is that the Area Director did not consider any facts other than those he set out in the background section. However, the Area Director's discussion evidences thorough awareness of the facts that appellant cites as having been omitted. The failure to state each and every "fact" related to this case in the background section of the Area Director's decision does not constitute error.

Appellant notes that the Area Director stated that cancellation of the lease would impact Vintage rather than Austin. She argues that this statement shows the Area Director was considering the best interests of the lessee, rather than the best interests of the Indian owners, and therefore violated his fiduciary responsibility to the trust beneficiaries.

The part of the Area Director's decision to which this argument refers can also be read as a statement of fact. It simply acknowledges the fact that, as present lessee, Vintage will be directly affected by a cancellation of the lease, whereas Austin, who no longer has an interest in the lease, will not be affected. To the extent the statement can be read as appellant contends, the Board agrees that the Area Director's trust responsibility was to the Indian owners. However, if the Area Director's decision is otherwise proper, the Board would not reverse the decision, or find that the Area Director had failed to perform his trust duties properly, solely on the basis of this ambiguous statement.

Appellant alleges that the Area Director relied upon unreasonable inferences. She first contends he has inferred that the lessees were guiltless, and has failed to consider the relevant evidence that both lessees admitted violating the lease and the regulations. The Board cannot find evidence of the alleged inference anywhere in the decision, nor can it conclude that the Area Director failed to consider the admitted violations. In fact, quite the opposite is true. The Area Director's decision evidences not only his awareness of the fact that Vintage and Austin admitted the violations, but also of the conclusions reached by MMS and BLM that there were violations.

Appellant also argues that the Area Director relied upon an unreasonable inference in stating that the wells would have to be plugged and abandoned if the lease were cancelled because plugging producing wells is not in the owners' best interest, but "is inimical to well grounded legal principles of property law and conservation law in the prevention of waste" (Opening Brief at 29). Appellant does not otherwise identify these "well grounded legal principles." The statement to which appellant objects was based on a comment made by MMS in a March 2, 1993, memorandum to the Regional Solicitor, and was attributed to MMS in the decision letter. 4/

The Board can only assume appellant contends that but for the allegedly incorrect conclusion that the wells would have to be plugged, the Area Director would have determined that it was in the owners' best interest to cancel the lease and allow either a new lessee or appellant immediately to assume the lease. However, the sentence in the Area Director's decision which contains the statement about plugging the wells begins with a reference to MMS' conclusion that the owners are receiving compensation equal to or exceeding current market prices. Even if the Area Director was incorrect in stating that the wells would need to be plugged, this was only one factor in his determination of whether lease cancellation was in the owners, financial interest. Again, if the decision is otherwise correct, the Board would not reverse the Area Director on the basis of this one statement.

4/ A footnote in the Area Director's decision states that the present CA, which was negotiated with the assistance of private counsel, "contain[s] a clause which states how properties will be managed if they become unleased" (Decision Letter at 3, note 1). No citation is given for this clause, and the Board was not able to determine which provision of the CA was being referenced. Article 24.3 of the CA deals with sales of interests held by current lessees, and Article 25 deals with the withdrawal of a lessee. The Board did not find a provision specifically dealing with "unleased" areas, or cancellation of a lease.

Several of appellant's arguments appear to include challenges to royalty decisions made by MMS. This Board does not have jurisdiction to review MMS royalty decisions. Administrative review of those decisions lies with the Interior Board of Land Appeals. See 43 CFR 4.330(b)(3). Although the Board finds it must discuss these matters in order to respond to appellant's arguments, it does so only to the extent necessary for an understanding of its decision. 5/

Having addressed appellant's more general arguments, the Board proceeds to her specific allegations of error.

Although appellant approaches her major argument from several different directions, the essence of the argument is that cancellation of the lease is mandated by both the lease and the regulations, and therefore failure to cancel the lease violates both Federal law and regulations and the lease. Appellant bases this argument on 25 CFR 212.23(a) and Paragraph 6 of the lease. 25 CFR 212.23(a) provides in pertinent part:

> A lease will be cancelled by the Secretary of the Interior for good cause upon application of the lessor or lessee, or if at any time the Secretary is satisfied that the provisions of the lease or of any regulations heretofore or hereafter prescribed have been violated.

Paragraph 6 of the lease, Cancellation and Forfeiture, provides:

> When, in the opinion of the [Secretary], there has been a violation of any of the term and conditions of this lease before restrictions are removed, the [Secretary] shall have the right at any time after 30 days, notice to the lessee, specifying the terms and conditions violated, and after a hearing, if the lessee shall so request within 30 days of receipt of notice, to declare this lease null and void, and the lessor shall then be entitled and authorized to take immediate possession of the land * * *.

Although appellant states that section 212.23(a) and Paragraph 6 are not inconsistent, she does not specifically address the obvious differences between them. Devoting most of her argument to section 212.23(a), appellant contends that both section 212.23(a) and Paragraph 6 establish "strict liability" for lessees of Indian oil and gas properties, and require the cancellation of a lease whenever there is a violation of the lease terms or regulations:

5/ One of the three issues for which the Claims Court stayed its decision was a determination by MMS of overdue or underpaid royalties. If appellant objected to MMS decisions, she should have pursued the matter through the administrative review channels established for review of those decisions.

> The mandatory language of 25 C.F.R. sec. 212.23 is stiff and severe in that it demands automatic results. It is stiff and severe because it is a tool to be used by the B.I.A. in exercising its fiduciary duty as trustee over restricted Indian land and in protecting the best interest of the Indian. Because of the higher standard imposed on the B.I.A. [than on BLM or MMS], it has been given this devise to carry out its fiduciary functions.

(Opening Brief to Area Director at 27).

Appellant reads section 212.23(a) as establishing two circumstances under which the Secretary can cancel a lease: (1) for "good cause" upon application, and (2) whenever there has been a violation of the lease or regulations. She argues that the use of the disjunctive "or" in the regulation means that "good cause" need not be present when a lease is cancelled for a violation of the lease or regulations. Appellant's reading of the regulation would apparently require BIA to cancel a lease for any violation, regardless of how trivial the violation might be, whether cancellation was in the best interest of the Indian lessor, or even whether the lessor and lessee wanted to continue in the relationship.

In contrast, the Area Director held that "good cause" must be shown in all cases, and that "good cause" does not exist when the lessee has timely cured a violation.

The Board would have agreed with the Area Director's reading of section 212.23(a) based merely on the language used in the regulation and the canon of construction that an interpretation should be avoided if it leads to an absurd or incongruous result. This interpretation, however, has additional support. In Poafpybitty v. Skelly Oil Co., 390 U.S. 365, 374 (1968), the Supreme Court examined 25 CFR 172.23 (1967), the predecessor regulation to 25 CFR 212.23, and stated:

> The regulations do empower the Secretary to cancel a lease "for good cause upon application of the lessor or lessee, or if at any time the Secretary is satisfied that the provisions of the lease or of any regulations heretofore or hereafter prescribed have been violated." * * * However, there is no justification for concluding that the severe sanction of cancellation of the lease is the only relief for all breaches of the lease term or for any failure to pay royalties. [Citation to regulation omitted.]

[2] The Board is bound by Supreme Court decisions. See Bitz v. Acting Billings Area Director, 23 IBIA 286 (1993). Under the Supreme Court's ruling considering language identical to the present 25 CFR 212.23(a), BIA is not required to cancel a lease whenever the lease terms or regulations are violated. Instead, it retains discretion to review the circumstances surrounding a violation(s) and determine whether cancellation is warranted,

taking into consideration, inter alia, the trust responsibility to act in the best interest of the Indian landowner(s). 6/

Paragraph 6 of the lease is not written in language stronger than that in section 212.23(a) or its predecessor regulations. If the regulations do not mandate cancellation for any violation, the Board cannot conclude that Paragraph 6 does. Accordingly, the Board rejects appellant's argument that 25 CFR 212.23(a) and Paragraph 6 of the lease mandate cancellation of a lease whenever there is a violation of the lease or regulations.

The Board next considers appellant's arguments that there was "good cause" to cancel the lease because the violations were so egregious, and that because the violations were so egregious, the Area Director's decision not to cancel the lease was against the weight of the evidence. Appellant states that the lease violations included:

> a) decreasing the royalties by one half from December 1985, the date of initial production, through September 1988; b) installing an unnecessary by-pass pipe around the gas meter; c) failure to pay royalties on condensate sales; d) failure to perform dual accounting; e) questionable pricing of hydrocarbons; f) lack of arm's-length transactions; g) providing false information to the restricted Indian lessor in an attempt to force his consent to a [CA]; h) officially reporting one amount of production to the Oklahoma Tax Commission [OTC] and the B.L.M. while reporting one-half of that amount to the M.M.S.; i) sporadic and improper payments of advance rentals and j) violation of other regulations.

(Opening Brief at 30). She also lists the regulations she asserts were violated: 25 CFR 212.16; 25 CFR 212.20; 30 CFR 202.100; 30 CFR 202.150; 30 CFR 206.102; 30 CFR 206.105; 30 CFR 206.152; 30 CFR 206.153; 30 CFR 206.155; 30 CFR 206.157; 30 CFR 206.159; and 43 CFR 3162.7-5(b)(3). 7/

For purposes of this discussion, the Board groups appellant's discussion of lease violations with the appropriate regulation(s).

Appellant's section a) deals with the payment of royalties on only one-half of the production. In response to the Regional Solicitor's request for input, MMS acknowledged that both Austin and Vintage had improperly paid

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6/ In Poafpybitty, the Court cited as a reason for not cancelling a lease the possibility that both the lessor and the lessee might wish to resolve their disagreement through the payment of damages. There is no indication that the Court viewed this as the only situation under which BIA could decide not to cancel a lease.

7/ BIA is responsible for promulgating and enforcing the regulations cited in 25 CFR, MMS is responsible for those in 30 CFR, and BLM is responsible for 43 CFR 3162.7-5(b)(3).

royalties based on the unapproved CA, but recommended that the lease not be cancelled for this reason. MMS stated that "[f]or the period in question, it was not an uncommon practice for payors to calculate and pay royalties based on a proposed [CA], pending approval by [BIA] and [BLM]. In most instances, proposed [CAs] were approved and royalty payments based on the proposed agreement would represent the most accurate royalty basis" (Apr. 2, 1992, Memorandum from MMS Dallas Area Manager at 2). MMS also noted that the erroneous payments were based on the October 17, 1985, OCC pooling order and the November 5, 1985, Division Order Title Opinion. Although these documents were ultimately determined to be incorrect, at the time they provided an arguable legal basis for concluding that the Indian interest had been communitized.

Appellant asserts that the Area Director distorted MMS' position by stating that the proposed CA was "neither approved, nor disapproved," and by ignoring both the fact that it was improper to pay royalty based on a proposed CA and that, according to affidavits submitted by appellant, it was not industry practice to pay royalties based on an unapproved CA.

Although MMS did not state that it was proper to pay royalties based on an unapproved CA, it did state that this "was not an uncommon practice." The Board cannot conclude that the Area Director's wording distorted MMS' position.

Furthermore, the Area Director nowhere stated or implied that it was proper to pay royalties based on an unapproved CA. Rather, he held that, despite the improper payments, the violation was cured. The Board also concludes, based on MMS' determination, that the improper payment method was cured and that royalties not previously paid have been paid, with interest.

Section h) is closely related to section a) and concerns the fact that different production amounts were reported to MMS, BLM, and OTC. Austin and Vintage contend that they properly reported production to each organization, stating that they reported the full production to BLM and OTC, in accordance with the requirements of those organizations; and reported one-half of the production to MMS, in accordance with its requirement to report only the amount of production on which royalties were paid to Indian lessors.

Issues relating to the different reporting requirements of MMS and BLM have previously arisen in cases before the Board, although a discussion of these issues has not been necessary to disposition of the cases. Based upon its knowledge that the reporting requirements have been different, and the facts presented in this case, the Board finds that Austin and Vintage followed the reporting requirements of MMS and BLM.

This finding does not, however, mean that Austin and Vintage properly reported to MMS the amount of production on which royalties should have been paid. The improper reporting resulted from the improper calculation of royalties as if the CA were in effect. However, the Board does find that there was a regulatory basis for the different amounts of production reported to

MMS and BLM. Because MMS states that the correct amounts of production are now being reported to it, the Board concludes that this violation has been cured.

Section b) concerns the bypass piping. 43 CFR 3162.7-5(b)(3) prohibits bypass piping around gas meters on Federal and Indian leases. In an April 7, 1992, memorandum to the Regional Solicitor, BLM stated that this violation was quickly cured, and recommended that it not be used as a basis for lease cancellation, giving seven reasons why the lease should not be cancelled.

Appellant argues that the Area Director should not have relied on BLM's recommendation because another case which BLM cited in support of its recommendation involved hydrogen sulfide, a "life threatening poisonous sulfur gas" (Opening Brief at 35), and this case does not. The Board finds nothing in BLM's memorandum indicating that the potentially poisonous nature of the gas in the case referenced had any bearing on BLM's decision. The Area Director did not err in relying on BLM's recommendation merely because hydrogen sulfide was involved in the case BLM cited.

It appears that for the first time on appeal appellant may be arguing that the bypass piping was in place since the wells were initially put into production. Although the Board is not required to consider arguments and evidence presented for the first time on appeal, see, e.g., All Materials of Montana, Inc. v. Billings Area Director, 21 IBIA 202, 212 (1992), and cases cited therein, it does so here to ensure that there is administrative finality to this decision. There is no evidence in the record, and appellant has presented none, on which to base a finding that the bypass piping was in place for more than a short period of time. To the contrary, BLM has stated that the evidence indicates the piping was in place for only a short period of time. See Apr. 7, 1992, memorandum. Appellant has failed to carry its burden of showing that the bypass piping was in place for an extended period of time.

The Board concludes that the violation of the regulations resulting from the installation of bypass piping has been cured.

Section c) concerns failure to pay royalties on condensate. 25 CFR 212.16, 30 CFR 202.100, and 30 CFR 202.150 each require payment of royalties on all production, including condensate. Appellant argues that MMS conducted only a spot audit of condensate sales, and required both Austin and Vintage to review their records and make further royalty payments. She asserts that neither Austin nor Vintage did any further analysis to determine whether additional royalties were due on condensate sales. 8/

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8/ It appears that appellant's allegation of a violation of 25 CFR 212.20, which requires that royalties be paid monthly, also relates to the nonpayment of royalties on condensate. If appellant is alleging some other violation of 25 CFR 212.20, it is not apparent from her filings. The Board is not required to make an appellant's argument for her, especially when she is represented by counsel. See, e.g., Estate of Eugene Patrick Dupuis, 11 IBIA 11, 13 n. 1 (1982).

The information presented by MMS contradicts appellant's allegations. MMS states that Austin elected to pay the additional royalties which MMS extrapolated were due, while Vintage reviewed its records and paid an additional $119 in royalties on condensate sales. MMS verified that Vintage's calculations were correct (Declaration of Tommy R. Holamon, Attachment to Area Director's Answer Brief, at 4).

Based on the information presented by MMS to the effect that Vintage is now properly reporting condensate sales, the Board concludes that any violations in regard to this issue have been cured.

Sections d), e), and f) all relate to the fact that Austin and Vintage sold production from the lease to affiliated companies. Appellant's arguments in this area appear to evidence a belief that sales not at arm's- length are <u>per</u> <u>se</u> collusive, and that there is no way in which the lessor will receive fair compensation.

30 CFR 206.102(b) and 30 CFR 206.155 concern royalty valuation, and contain provisions relating to sales to affiliated companies. Neither section prohibits sales to affiliates, but section 206.155 requires dual accounting when sales are not at arm's-length, in order to ensure that the maximum royalty is paid. At page 2 of its April 2, 1992, response to the Regional Solicitor's request for recommendations concerning lease cancellation, MMS stated that "it is not uncommon for MMS and royalty payors to have different interpretations on 'dual accounting' valuation requirements. The MMS audits often result in additional royalty payments when 'dual accounting' analyses are performed."

Appellant asserts that the Area Director distorted MMS' position by saying that the lessees had "misinterpreted" the dual accounting regulations, when MMS actually stated that the lessees admitted not performing dual accounting. Appellant contends that the lessees were presumed to have knowledge of the regulations, including the requirement to perform dual accounting.

The Area Director's decision refers to "the lessee's misinterpretation of and <u>failure to perform</u> 'dual accounting'" (Decision Letter at 3; emphasis added). Although appellant quotes the entire phrase at page 22 of her opening brief, she does not address the fact that the Area Director specifically stated that the lessees had "fail[ed] to perform" dual accounting, and instead bases her argument exclusively on the use of the word "misinterpretation." The Board finds no distortion of MMS' position.

Furthermore, the MMS audit resulted in a determination of the amounts owed under dual accounting, and the lessees have paid those amounts, with interest. MMS indicates that Vintage is now properly performing dual accounting. The Board finds that the violation resulting from the failure to perform dual accounting has been cured.

Section g) refers to a February 5, 1988, letter from NiJean to Namaso, which stated:

> NiJean Petroleum, Inc. is Communitizing the NW/4 of Section 13, T10N, 3E, Pottawatomie County, Oklahoma.
>
> This will not affect the amount of money you are receiving now. This is a requirement of the B.I.A. and B.L.M. to match the spacing unit set by the [OCC].
>
> I want to emphasize that this will not change anything from the way it has been done in the past.
>
> Thank you for your consideration in this matter.

Vintage and Austin contend that the letter was not seeking to force Namaso to agree to communitization because he had already agreed to abide by any CA approved by the Superintendent under Paragraph 11 of the lease, Unit Operation, which provides:

> The parties hereto agree to subscribe to and abide by any agreement for the cooperative or unit development of the field or area, affecting the leased lands, or any pool thereof, if and when collectively adopted by a majority operating interest therein and approved by the [Secretary], during the period of supervision.

The Board agrees that Paragraph 11 constituted Namaso's agreement to abide by any CA approved by BIA. See, e.g., Cheyenne and Arapaho Tribes of Western Oklahoma v. Deputy Assistant Secretary--Indian Affairs (Operations), 11 IBIA 54, 90 I.D. 61 (1983).

It is not clear what NiJean intended to accomplish with this letter. The last sentence suggests that NiJean believed additional agreement was required. However, nothing in the letter actually requests action from Namaso. It is possible the letter was intended to be purely informational, even though some of the information, i.e., that communitization was required by BIA and BLM, was incorrect.

In any case, Namaso obviously was not pressured into giving additional approval of a CA by the letter. Even assuming that appellant is correct and that NiJean was attempting to coerce Namaso into agreeing to the CA by providing him with false information, the attempt did not succeed.

The Board finds no continuing violation of the lease or regulations in relation to this letter.

In summary, the Board concludes that the violations listed in appellant's sections a), b), c), d), e), f), g), and h), as well as the violations of 25 CFR 212.16, 25 CFR 212.20, 30 CFR 202.100, 30 CFR 202.150, 30 CFR 206.102, 30 CFR 206.155, and 43 CFR 3162.7-5(b)(3), have been cured.

Appellant cites prior Board cases for the propositions that a lessee's curing of violations does not create a right to continue to breach the lease with impunity, and that when a lessee has been given an opportunity to cure a breach and has failed to do so, the lessee need not be given additional chances to cure. French v. Aberdeen Area Director, 22 IBIA 211 (1992); Mast v. Aberdeen Area Director, 19 IBIA 96 (1990). The Board assumes from these references and the context of appellant's brief that she is arguing that violations which have been cured can still be the basis for lease cancellation. This argument is consistent with appellant's earlier argument that cancellation is mandated for any violation of the lease or regulations.

The general rule regarding business leases of trust property which are governed by 25 CFR Part 162, is that the regulations "require[] that a lessee be given an opportunity to take corrective action," Chissoe v. Acting Muskogee Area Director, 25 IBIA 146, 151 (1994), and "contemplate that leases of Indian lands will not be cancelled for breaches that may readily be cured," Plumage v. Billings Area Director, 19 IBIA 134, 142 (1991). This interpretation follows general contract law. Federal contract law, including contracts involving trust or restricted lands, is governed by the same principles as general contract law. Priebe & Sons, Inc. v. United States, 332 U.S. 407 (1947); United States v. Humboldt Fir, Inc., 426 F. Supp. 292 (N.D. Calif. 1977), aff'd mem., 625 F.2d 330 (9th Cir. 1980); Naegele Outdoor Advertising Co. v. Acting Sacramento Area Director, 24 IBIA 169, 177 (1993), and cases cited therein.

[3] This case is not governed by 25 CFR Part 162. However, given the Supreme Court's statement in Poafpybitty concerning the same regulatory language as is now found in 25 CFR 212.23(a), the Board concludes that lessees of Indian oil and gas leases should, and do, have the same right to cure lease violations that other business lessees have, unless the particular lease provides otherwise. The necessary concomitant to this conclusion is that once lease violations have been cured, the lessee must be considered to be in good standing. This is true even though it may be possible to characterize the violations as "major" or "egregious."

French and Mast do not require a contrary conclusion. In both of those cases, the lessees had established a course of conduct under which they were notified that a particular action constituted a breach; either cured the breach (French), or represented that they would cure it, but failed to do so (Mast); and continued to breach the same obligation. The leases in those cases were cancelled based on the continuing or repetitive breach of the same provision(s) of the lease or regulations. The violations here have been cured, and no evidence has been presented to suggest there is, or may be, a repetition of the same breaches. Should such repetition occur, BIA would have discretion to consider lease cancellation in accordance with the holdings in French and Mast.

The Board concludes that if a violation of the lease or regulations has been cured and not repeated, it cannot form the basis for lease cancellation. In the context of this case, the Board holds that the violations discussed supra, all of which have been cured, cannot serve as bases for cancellation of the lease.

Appellant's section i) concerns payment of advance rentals. The lease provides in Paragraph 3:

> In consideration of the foregoing, the lessee hereby agrees: * * *
> (c) **Rental and royalty.**--To pay, beginning with the date of approval of the lease by the Secretary of the Interior, a rental of $1.25 per acre per annum in advance during the continuance hereof, the rental so paid for any one year to be credited on the royalty for the year, together with a royalty of 20 percent of the value or amount of all oil, gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and saved from the land leased herein * * *. [Emphasis in original.]

Based on a review of its records, BIA stated that advance rentals were paid approximately 1 month late in 1983, and that it could not locate records showing whether or not the advance rental was paid in 1981.

As presented in her opening brief, appellant's argument concerning advance rentals is by no mean clear. She contends there: "[S]ome years lessees failed to pay advance rentals totally. The few advance rentals that were paid, were paid untimely, sporadically and in varying amounts" (Opening Brief at 28). However, in her reply brief she argues: "25 C.F.R. sec. 212.16 requires that advance rentals be paid throughout the life of the lease regardless of production" (Reply Brief at 7). 9/ It thus appears appellant believes advance rentals are due in addition to royalty payments. However, both the lease and the regulation specifically provide that, once production has begun, i.e., once royalties are due, advance rentals are "credited on the royalty for that year."

The Board finds no basis for appellant's apparent contention that advance rentals are due in addition to royalties. It therefore concludes that appellant has not shown a continuing violation in regard to payment of advance rentals.

Appellant's section j) refers to violations of "other regulations." The Board considers that these "other regulations" are the regulations appellant listed, but which have not already been addressed in the discussions relating to one of the other sections of appellant's brief.

Appellant contends that the royalties which were paid were calculated improperly under 30 CFR 206.102, 30 CFR 206.152, and 30 CFR 206.153. 30 CFR 206.102(a)(2)(i) requires that

> [f]or any Indian leases which provide that the Secretary may consider the highest price paid or offered for a major portion of production (major portion) in determining value for royalty

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9/ Section 212.16 provides in pertinent part: "The lessee shall pay * * * a rental of $1.25 per acre per annum, in advance during the continuance [of the lease], the rental so paid for any one year to be credited on the royalty for that year."

> purposes, if data are available to compute a major portion, MMS will, where practicable, compare the value determined in accordance with this section with the major portion. The value to be used in determining the value of production, for royalty purposes, shall be the higher of those two values.

30 CFR 206.152(a)(3)(i) and 30 CFR 206.153(a)(3)(i) differ only incidentally from this provision. Paragraph 3(c) of the lease provides in relevant part:

> During the period of supervision, "value" for the purposes [of determining royalty] may, in the discretion of the Secretary, be calculated on the basis of the highest price paid or offered (whether calculated on the basis of short or actual volume) at the time of production for the major portion of the oil of the same gravity, and gas, and/or natural gasoline, and/or all other hydrocarbon substances produced and sold from the field where the leased lands are situated, and the actual volume of the marketable product less the content of foreign substances as determined by the oil and gas supervisor. The actual amount realized by the lessee from the sale of said products way, in the discretion of the Secretary, be deemed mere evidence of or conclusive evidence of such value.

The Area Director states that as part of a settlement agreement in Kauley v. United States, Case No. CIV-84-3306-T (W.D. Okla. Dec. 6, 1991), a class action suit in which the present lessors were members of the class, the Department agreed to conduct a "major portion analysis" on Indian leases in western Oklahoma when adequate data was available. In response to a February 27, 1992, request from the Washington, D.C., Office of the Solicitor, MMS conducted a major portion analysis for this lease, and concluded that appellant was "receiving compensation for gas production that equals or exceeds the fair market value of other gas production in the same area. Our analyses identify no pricing discrepancies that would warrant lease cancellation" (Mar. 2, 1993, Memorandum from Chief, Valuation and Standards Division, MMS, to Regional Solicitor, at 4).

The responsibility for performing a major portion analysis rests with the Department, not with the lessee. The lessee's responsibility is merely to pay royalties based on the results of the major portion analysis. Even if there were a violation of these regulations, a finding the Board does not make, such a violation would not support lease cancellation. Because of this conclusion, the Board does not further address appellant's arguments concerning the major portion analysis.

Appellant also contends that 30 CFR 206.105, 30 CFR 206.157, and 30 CFR 206.159 were violated when MMS allowed a transportation allowance. This argument apparently applies only to Austin, because MMS states that Vintage did not claim a transportation allowance. Appellant argues that "[a] transportation allowance way have been available pursuant to 30 C.F.R. secs. 206.157(b) and 206.159; however, according to 30 C.F.R. sec. 206.157(b) transportation allowances would be permitted for only 90 days retroactively unless good cause is shown" (Opening Brief to Area Director at 38).

The Area Director states that 30 CFR 206.157 was amended, effective March 1988, and that the Board of Land Appeals has held that revised royalty valuation regulations are not to be applied retroactively. Walter Van Norman, Jr., 126 IBLA 375, 376 n.2 (1993). MMS concluded that because all of Austin's transactions occurred before the 3-month limitation was imposed, they were governed by the prior regulation, which did not have a time limitation for the allowance. MMS states that it worked with Austin to determine the appropriate transportation allowance.

This argument is addressed to MMS' interpretation and application of its regulations, and its resulting determination of the amount of royalties due from Austin. As in the previous discussion, the Board concludes that even if MMS improperly interpreted its own regulations in granting a transportation allowance, appellant's remedy is not lease cancellation. 10/

In summary, the Board concludes that (1) 25 CFR 212.23(a) does not mandate that a lease of Indian oil and/or gas be cancelled whenever there is a violation of the lease or regulations; (2) when a violation of a lease of Indian oil and/or gas properties has been cured and not repeated, the violation may not serve as the basis for lease cancellation; (3) BIA may request and consider recommendations from BLM and MMS concerning whether lease violations in areas under their respective jurisdictions support lease cancellation; and (4) a violation of a regulation that requires or authorizes action by the Department, or a misapplication of a regulation by the Department, cannot support lease cancellation. Based on these conclusions and the preceding discussion, the Board finds that the Area Director did not err in declining to cancel this lease.

Therefore, pursuant to the authority delegated to the Board of Indian Appeals by the Secretary of the Interior, 43 CFR 4.1, the Acting Anadarko Area Director's February 7, 1994, decision is affirmed. 11/

//original signed
Kathryn A. Lynn
Chief Administrative Judge

I concur:

//original signed
Anita Vogt
Administrative Judge

10/ Because Vintage did not claim a transportation allowance, it would be especially inappropriate to cancel its lease based on MMS' interpretation of whether Austin was entitled to a transportation allowance.

11/ Other arguments that appellant may have raised, but which are not specifically addressed, were considered and rejected.