INTERIOR BOARD OF INDIAN APPEALS

Joe Bob and Lara Kelley, Flagship Oil, Inc., and William M. Park v.
Eastern Oklahoma Regional Director, Bureau of Indian Affairs

54 IBIA 26 (08/19/2011)

United States Department of the Interior

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

JOE BOB and LARA KELLEY, FLAGSHIP OIL, INC., AND WILLIAM M. PARK, Appellants,	)	Order Affirming Decisions
v.	)	Docket No. IBIA 09-119
EASTERN OKLAHOMA REGIONAL DIRECTOR, BUREAU OF INDIAN AFFAIRS, Appellee.	)	August 19, 2011

We affirm the May 26, 2009, decisions (as to oil lessees and Appellants Flagship Oil, Inc., and William M. Park) and the May 29, 2009, decision (as to oil lessees and Appellants Joe Bob and Lara Kelley) of the Eastern Oklahoma Regional Director (Regional Director), Bureau of Indian Affairs (BIA), in which she in turn affirmed the decisions of the Superintendent of BIA's Osage Agency (Osage Superintendent) to assess unpaid royalties and late charges against Appellants. Appellants argued that their oil purchaser, SemCrude, L.P. (SemCrude), was liable for paying the royalties pursuant to BIA-approved division orders. We disagree. The division orders do not purport to relieve Appellants of liability, and applicable regulations repose responsibility for the payment of royalties in the lessees at all times, which includes late charges.

Undisputed Facts

Appellants each hold oil mining leases on the Osage Reservation, together with division orders, as follows:

Joe Bob and Lara Kelley

Oil Mining Lease No. 14-20-G06-2206, covering the SW¼ of Sec. 5, T. 25 N., R. 12 E., containing 160 acres more or less, Osage County, Oklahoma
Division Order No. 6000024203, approved by BIA on April 13, 2007

Oil Mining Lease No. 14-20-G06-2265, covering the SE¼ of Sec. 6, T. 25 N., R. 12 E., containing 160 acres more or less, Osage County, Oklahoma
Division Order No. 6000024203, approved by BIA on April 13, 2007[1]

William M. Park

Oil Mining Lease No. 14-20-201-5533-1, covering the SE¼NE¼SW¼ of Sec. 27, T. 20 N., R. 12 E., containing 10 acres more or less, Osage County, Oklahoma
Division Order No. 6000030697, approved by BIA on March 15, 2006

Oil Mining Lease No. 14-20-201-5532, covering the SE¼ of Sec. 27, T. 20 N., R. 12 E., containing 160 acres more or less, Osage County, Oklahoma
Division Order No. 6000030705, approved by BIA on March 15, 2006

Oil Mining Lease No. Ind-2572, covering the SE¼ of Sec. 22, T. 20 N., R. 12 E., containing 160 acres more or less, Osage County, Oklahoma
Division Order No. 6000030698, approved by BIA on March 15, 2006

Blanket Oil Mining Lease No. 14-20-0406-839, covering Lots 3 and 4 of fractional SW¼ of Sec. 14; the SE¼ of Sec. 15; the NE¼ of Sec. 22; and Lots 1 and 2 of fractional NW¼ of Sec. 23, all in T. 20 N., R. 12 E., containing 339.14 acres more or less, Osage County, Oklahoma
Division Order No. 6000030698, approved by BIA on March 15, 2006[2]

Flagship Oil, Inc.

Blanket Oil Mining Lease No. 14-20-G06-1278, covering the SE¼ of Sec. 24, T. 22 N., R. 10 E.; Sec. 25, T. 22 N., R. 10 E.; and the NW¼ of Sec. 19, T. 22 N. R. 11 E., containing 960 acres more or less, Osage County, Oklahoma
Division Order No. 6000027903, approved by BIA on December 14, 2006

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[1] Division Order No. 6000024203 covered both of the Kelleys' leases.

[2] Although not entirely clear, it appears from a handwritten notation on Division Order No. 6000030698 that it covers both Appellant Park's blanket oil lease and lease no. Ind-2572.

The lessor in each of these leases is the Osage Tribe of Indians of Oklahoma (Tribe). As noted above, the record provided to the Board of Indian Appeals (Board) contains division orders for all of the above leases. The division orders for oil sold from Appellant Flagship Oil's leasehold and from Appellant Kelleys' leaseholds do not provide for any payments to the Tribe or to BIA, only to the lessees; the division orders for Appellant Park's leases state that BIA is entitled to receive a royalty of 16⅔ percent.[3]

BIA's approval of each of the division orders in the record is expressly "subject to the terms of the lease and 25 CFR [§§] 226.11 and 226.14." In pertinent part, § 226.11(a) as well as the terms of each of the lessees' leases provide that "Lessee shall pay or *cause to be paid* to the [Osage] Superintendent, [a] royalty" and these terms provide the amount of the royalty to be paid. *See* Oil Mining Leases Nos. 14-20-G06-2206, 14-20-G06-2265, 14-20-201-5533-1, 14-20-201-5532, IND-2572, 14-20-0406-839, and 14-20-G06-1278, at ¶ 2 (emphasis added). Section 226.14(a) provides in relevant part "[t]hat such division orders . . . *shall not relieve Lessee from responsibility for the payment of the royalty should the purchaser fail to pay*." Emphasis added. In addition, Appellants' leases each contain a provision subjecting the leases "to the regulations now or hereafter prescribed by the Secretary of the Interior, relative to such leases, all of which are made a part of this lease [excepting those regulations that affect the term of the lease, rate of royalty, rental or acreage unless otherwise agreed to]." *See id*. at ¶ 16 (emphasis added).

Apparently, royalties were paid by SemCrude to BIA until June 2008. On July 22, 2008, SemCrude filed for bankruptcy under Chapter 11 of the bankruptcy code. *See In re SemCrude L.P.*, No. 08-11525 (BLS) (Bankr. Del. Jul 22, 2008). When BIA did not receive the royalty payments due for June and part of July 2008, the Osage Superintendent sent letters on November 14, 2008, and November 18, 2008, to Appellants demanding

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[3] As we explained in *Plains Marketing and Transportation, Inc. v. Acting Muskogee Area Director*, 37 IBIA 73, 74 (2001):

> Under section 4 of the Act of June 28, 1906, 34 Stat. 539, 544, the royalties received from leases of the [Osage] mineral estate are required to be paid into the Treasury of the United States and distributed per capita to the persons on the 1906 tribal roll or their heirs. [Footnote omitted.] The regulations in 25 C.F.R. Part 226 require that royalty payments be made to the [Osage Superintendent] (25 C.F.R. § 226.11(a)(1)), by either the lessee or the purchaser (25 C.F.R. § 226.13(a)).

See also Estate of Vivian M. Rogers v. Acting Muskogee Area Director, 14 IBIA 217, 218 (1986).

payment for the unpaid royalties for June and July 2008, respectively. The Superintendent also advised in her letters that late payments would be assessed a late charge of 1.5 percent per month pursuant to 25 C.F.R. § 226.13.[4]

Appellants each appealed to the Regional Director and submitted a joint statement of reasons in support of their respective appeals. They argued that SemCrude was an oil purchaser "approved" by BIA and that each division order "clearly states . . . that royalties were to be paid by the Purchaser." Appeal to the Regional Director at 1. Appellants rely on language in § 226.13 to argue that SemCrude is liable for any late charge. Appellants also claim without explanation that "the lessee has never been allowed to disburse the royalties and as such the only entity that is required to remit the royalties is SemCrude." *Id*. Appellants also suggested that they are not liable because BIA should have filed a claim in SemCrude's bankruptcy action and claim that BIA did so when another purchaser filed for bankruptcy.

On May 26, 2009, the Regional Director affirmed the Superintendent's decision to collect the June and July 2008 royalties and late charges from the lessees. The Regional Director pointed out that the regulations permit either the lessee or the purchaser to pay to BIA the royalty payments due to the Tribe. The Regional Director also pointed out that while § 226.13(a) permits either the lessee or the purchaser to remit the royalty due the Tribe, the regulation that authorizes division orders explicitly warns that "such division order or contracts shall not relieve Lessee from responsibility for the payment of the royalty should the purchaser fail to pay." 25 C.F.R. § 226.14(a). Finally, the Regional Director observed that, pursuant to § 226.13(a), the failure to remit royalty payments "shall" result in late charges.

This appeal followed.

Discussion

The regulations as well as the parties' leases make crystal clear that the responsibility of remitting the royalties due the Tribe rests with the lessees regardless of any arrangements that the lessees may make with their purchasers. And even if that were not so, there is no

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[4] Section 226.13(a) states in pertinent part, "[r]oyalty payments due may be paid by either purchaser or Lessee. . . . . Failure to make such payments shall subject Lessee or purchaser, *whoever is responsible for royalty payment*, to a late charge. . . ." Emphasis added. In addition, § 226.13(c) warns that "[f]ailure to remit payments . . . shall subject *Lessee* to further penalties . . . ." Emphasis added.

contract between BIA and SemCrude that requires SemCrude to pay the Tribe's royalty to BIA, nor do the division orders on which Appellants attempt to rely, which are contracts between Appellants and SemCrude, contain any language that relieves Appellants of their obligation to ensure that the Tribe's royalties are remitted to BIA. Therefore, we affirm the Regional Director's decision.

1. Standard of Review

The burden falls on appellants to show error in the Regional Director's decision. *McCann Resources, Inc. v. Eastern Oklahoma Regional Director*, 46 IBIA 266, 269 (2008). This burden is not met by mere disagreement with the decision but must be supported by identifying specific error(s) of law or of material facts. *Id*. Thus, appellants are charged with directing the Board's attention to evidence in the record in support of their factual contentions (or, as appropriate, to the absence of evidence supporting the Regional Director's findings) or with citations to the law in support of their legal contentions. The Board will review errors of law as well as the sufficiency of the evidence *de novo*. *Chuchua v. Pacific Regional Director*, 42 IBIA 1, 5 (2005).

2. Merits

The terms of Appellants' leases as well as the applicable regulations control the outcome of this appeal. And they are each consistent and unequivocal in holding the lessees responsible at all times for the payment of the Tribe's royalties. And, because there is no showing that SemCrude or any other party is responsible for the payment of the Tribe's royalty other than Appellants, late fees are assessable against Appellants.

At their discretion and subject to BIA's approval, lessees are authorized to enter into division orders with oil purchasers pursuant to which the purchasers will remit the royalty due under the terms of the lessee's lease, "*[p]rovided* [t]hat such division orders or contracts *shall not relieve Lessee from responsibility for the payment of the royalty should the purchaser fail to pay*." 25 C.F.R. § 226.14(a) (emphasis added). The terms of Appellants' leases as well as § 226.11(a) also require the lessee to pay or *cause* to be paid the royalty due under the lease. The leases each contain a clause (¶ 16) that subjects the leases to applicable regulations, which include 25 C.F.R. pt. 226.

To the extent that any Appellant has division orders pursuant to which the lessee arranged to have SemCrude remit the Tribe's royalties directly to BIA, e.g., Appellant Park, the argument may be that Appellants have thereby "caused" the royalty to be paid within the meaning of § 226.11(a), and that they are therefore absolved of responsibility for any

unpaid royalties. We disagree. This provision in § 226.11(a) simply authorizes the lessee to arrange for the Tribe's royalties to be remitted by a third party. When construed in harmony with § 226.14(a), which makes clear that the lessee remains responsible for the payment of the Tribe's royalty notwithstanding a division order with a purchaser under which the purchaser remits the royalty, *cause*, as used in § 226.11(a), means that the lessees must ensure that the royalty is actually paid. It does not mean that lessees may transfer *their liability* for paying the Tribe's royalties to a third party. Consistent with § 226.14(a) and contrary to Appellants' claim, nothing in the terms of Appellants' division orders absolves Appellants from their responsibility — under the terms of their respective leases with the Tribe — to ensure that the Tribe receives all royalties due.

We turn now to a discussion of Appellants' arguments. Appellants claim that their division orders "clearly state[] . . . that royalties were to be paid by the Purchaser." Notice of Appeal at 1. What the division orders "clearly state" is that royalties are to be paid to the lessees. In fact, there is no mention of BIA or the Tribe in the division orders between Appellants Flagship Oil, Inc., and the Kelleys, and nothing in Appellant Park's division orders that obligates SemCrude to pay royalties to BIA. Even if the division orders did require SemCrude to remit the Tribe's royalty payments to BIA, which we do not find to be the case, BIA is not a party to the division orders. BIA's only role, with respect to the division orders, is that of an *approving* authority as required by 25 C.F.R. § 226.14(a), not a contracting party. And, division orders are only permitted *if* the lessees remain liable for the payment of royalties to the Tribe in the event the purchaser fails to pay. *See* 25 C.F.R. § 226.14(a). Nothing in the language of any of Appellants' division orders relieves Appellants of this responsibility.

Appellants further claim that they "ha[ve] never been allowed to disburse the royalties [to BIA]," and therefore cannot be held liable. Notice of Appeal at 1. This statement is unsupported and, moreover flies in the face of Appellants' lease terms, applicable regulations, and the demand — now the subject of this appeal before the Board — from BIA for the unpaid royalties. Nothing in the regulations or the leases require Appellants, as lessees, to utilize division orders nor do the regulations prohibit lessees from tendering the royalty payments on oil that they have sold. Rather, 25 C.F.R. § 226.13(a) specifically authorizes royalty payments to "be paid by *either* purchaser or Lessee." Emphasis added.

Appellants also rely on 25 C.F.R. § 226.13(a) to support their argument that they are not liable for the unpaid royalties or late fees. Again, Appellants' argument is misplaced. Section 226.13(a) states in relevant part that "[f]ailure to make such [royalty] payments shall subject Lessee or purchaser, whoever is responsible for royalty payment, to a late

charge. . . ." Emphasis added. This provision addresses only the payment of late charges; it does not address the payment of the royalties themselves. And, with respect to late fees, Appellants bear the burden of showing that SemCrude is directly responsible for the payment of the Tribe's royalty. Appellants have not met their burden of directing us to any language in their division orders or otherwise that creates a legal liability on the part of SemCrude to pay the Tribe's royalty to BIA. The division orders for the leases of Appellants Kelley and Flagship Oil do not even reference any entitlement by BIA to any royalty payments. As for the division orders for Appellant Park's leases, there is only a notation that BIA is "Owner #656370" and is "entitled to receive payment." *See* Division Orders No. 6000030697, 6000030698, and 6000030705. The text of Appellant Park's division orders state that "[p]roceeds shall be paid to the undersigned. . . ." *Id*. There is only one "undersigned" on each of Appellant Park's division orders: William M. Park. Therefore, despite the acknowledgment in the division order that BIA is entitled to receive payment, we do not find any language in the division orders that imposes any responsibility on SemCrude to remit any royalty payments to BIA.

Appellants further claim that BIA should be estopped from seeking the unpaid royalties from them because SemCrude was on a list of purchasers "approved" by BIA. Appellants appear to suggest that they relied on BIA's approval in selecting SemCrude as their purchaser. Estoppel does not lie under such circumstances, especially where the regulations and Appellants' leases set forth in unmistakable terms that the lessee remains liable at all times for the payment of royalties to the Tribe, not third parties.[5]

Additionally, Appellants argue that BIA should have filed a claim in SemCrude's bankruptcy action. Appellants cite no basis for any claim to be filed by BIA. The Regional Director responds by asserting that nothing in the record shows that BIA has "a contractual relationship with SemCrude and presumably [BIA] could not have filed a claim." Answer Brief at 7. Even assuming that BIA could have filed a claim in SemCrude's bankruptcy, neither the regulations nor the leases require BIA to do so or even to do so in lieu of or prior to seeking payment of the royalties from the lessees.

Finally, Appellants contend that BIA handled the collection of royalties differently when another purchaser declared bankruptcy. Appellants do not state how BIA handled the matter differently nor do Appellants provide any documentation in support of their factual

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[5] And even assuming that estoppel could lie under these facts, there is simply no evidence suggesting, let alone proving, that BIA knew in March 2006 and October 2007 (when BIA approved Appellants' division orders) that SemCrude would be filing for bankruptcy in July 2008.

contentions. Appellants suggest that BIA demanded payment of the royalties from the bankrupt purchaser. Assuming that to be the case, it does not follow that BIA was obligated to demand payment of the unpaid royalties from SemCrude instead of demanding payment from Appellants.

When a company goes bankrupt or through a reorganization, it is because the company is unable to meet its financial obligations, including payments to creditors. It is unfortunate that Appellants are among those who may be left holding the bag in the wake of SemCrude's Chapter 11 filing. But Appellants cannot pass along their misfortune to BIA or the Tribe. At all times, Appellants have held exclusive responsibility — under the terms of their leases as well as the applicable regulations — for remitting the royalties due the Tribe to BIA. Thus, any risk that payments might be missed falls squarely on Appellants and not on BIA or the Tribe. BIA properly demanded payment from Appellants for the unpaid royalties, and it is up to Appellants to seek whatever reimbursement they may be able to obtain from SemCrude.

Therefore pursuant to the authority delegated to the Board of Indian Appeals by the Secretary of the Interior, pursuant to 43 C.F.R. §4.1 the Regional Director's decisions of May 26, 2009, and May 29, 2009, are affirmed.

I concur:

// original signed
Debora G. Luther
Administrative Judge

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Steven K. Linscheid
Chief Administrative Judge