<u>Editor's note</u>: 97 I.D. 1

SUN EXPLORATION AND PRODUCTION CO.

IBLA 88-11 Decided January 19, 1990

Appeal from an August 13, 1987, decision of the Acting Director, Minerals Management Service, that the total production from the lease should be used when calculating the average daily production rate, which is used to determine the applicable royalty rate. MMS-86-0202-O&G and MMS-86-0307-O&G.

Affirmed as modified.

1. Oil and Gas Leases: Royalties: Generally--Regulations: Interpretation--Statutory Construction: Administrative Construction

> It is within the authority of the Department to inter- pret its own regulations, and its interpretation should be given great deference. Normally an interpretive ruling stating the accounting procedures to be used
> for royalty calculation may be given retroactive effect. However, when it appears from the record that: (1) for several years the lessee had applied an accounting pro- cedure which conformed with a reasonable interpreta- tion of the applicable regulations when calculating
> the royalty due for oil produced and removed from the lease; (2) the Department had accepted lessee's royalty accounting procedure for several years before issuing an interpretive ruling that required a different accounting

procedure; (3) the new procedure was an abrupt departure from a well-established practice, and not an attempt to fill a void in an unsettled area of the law; and (4) the prejudice to the lessee affected by retroactive appli- cation of the new interpretation substantially out-weighs the statutory interest and purposes sought to be protected, then the new MMS accounting procedure should be applied prospectively.

APPEARANCES: Jerry E. Rothrock, Esq., Jeffrey G. DiSciullo, Esq., Washington, D.C., for appellant; Peter J. Schaumberg, Esq., Geoffrey Heath, Esq., Howard W. Chalker, Esq., Office of the Solicitor, U.S. Department of the Interior, Washington, D.C., for the Minerals Management Service.

OPINION BY ADMINISTRATIVE JUDGE MULLEN

Sun Exploration and Production Company (Sun) has appealed from an August 13, 1987, decision of the Acting Director, Minerals Management Service (MMS), that Sun had failed to properly apply the sliding-scale royalty provisions of its lease when determining the royalty rate appli- cable to oil production during the period from January 1977 through January 1983 (MMS-86-0202-O&G and MMS-86-0307-O&G).

The record does not contain a copy of the lease 80-020997, and we do not know when it was initially issued. The lease was renewed with an effective date of February 1, 1978, and a copy of that renewal is in the case file. For the purposes of this decision, the term "lease" shall mean the February 1, 1978, lease renewal. 1/ Section 2, paragraph (d)(1) of the lease requires the lessee to "pay rentals and royalties in amount or value of production removed or sold from the leased lands as set forth in the rental and royalty schedule attached to and made a part hereof" (Lease at 2).

The attachment referred to in paragraph (d)(1) is Schedule D. This Schedule calls for a "sliding scale" royalty rate which is based upon the average daily production volume per well in the month the royalty accrues. The portion of Schedule D applicable to this case provides:

> (2) For all oil produced of less than 30° Baume:
>
> On that portion of the average production per well not exceeding 20 barrels per day for the calendar month 12 1/2%
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> On that portion of the average production per well of more than 20 barrels and not more than 50 barrels per day for the calendar month 14 2/7%
>
> On that portion of the average production per well of more than 50 barrels and not more than 100 barrels per day for the calendar month 16 2/3%
>
> On that portion of the average production per well of more than 100 barrels and not more than 200 barrels per day for the calendar month 20%
>
> On that portion of the average production per well of more than 200 barrels per day for the calendar month 25%

1/ We note that the period under review commenced prior to the renewal of the lease. If the previous lease terms differ materially from those contained in the Feb. 1, 1978, renewal, this decision may not be applicable to the royalties under the previous lease document. Neither party to this appeal raised this issue and we are presuming that the terms are unchanged.

The MMS decision followed a review of Sun's royalty payments for production from lease 80-020997 during the period from January 1, 1977, through January 31, 1983. This review was conducted by the State of California pursuant to section 205 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), 30 U.S.C. § 1735 (1982). The State con- cluded that Sun's failure to apply the correct royalty rates resulted in underpayment and delivery of less than the required amount of royalty-in-kind oil. The basis for the State's contention was that Sun had improp- erly excluded oil used on the lease when calculating the average daily production for the purpose of determining the royalty rate.

By letter dated March 21, 1986, the Royalty Compliance Division, MMS, ordered Sun to pay $222,331 in underpaid royalties. This amount was stated to be the additional amount due as a result of applying the royalty at a higher rate to the sales volume. 2/ Sun appealed from this determination (MMS-86-0202-O&G). By letter dated April 21, 1986, MMS ordered Sun to pay an additional $76,410, after determining that Sun had also applied the incorrect royalty rate when calculating the royalty-in-kind payment. Sun also filed a timely appeal of this determination (MMS-86-0307-O&G).

In his August 13, 1987, decision, the Acting Director, MMS, found the basis for the State's calculations to be incorrect, noting Sun's argument

2/ The State had applied a royalty at the higher rate and had calculated the royalty based on gross production without deducting the fuel Sun had used on the lease.

that the State's method imposed a royalty on the oil used on the lease by including oil not subject to a royalty to produce a higher royalty rate. After noting Sun's arguments that the phrase "average production per well" has always been interpreted as referring solely to "production subject to royalty," and that in its 1970 and 1979 correspondence the Department implicitly agreed to Sun's method of calculating royalties, the Director found that the United States is not estopped from asserting prerogatives granted by regulatory authority and that its rights may not be waived by past administrative practice. He then stated his opinion that neither the method advanced by the State nor the method advanced by Sun fairly implements the sliding-scale royalty provisions of the lease. Based on his finding that "the object of the sliding scale rate provisions to spread royalties over the total produced volumes is best served by allocating the lease use volumes proportionately to each production category calculated for a month," he found that, for the period in question, Sun had improperly calculated the average daily production by not including the oil consumed in lease operations. He then found that this failure resulted in Sun's misapplication of the sliding-scale royalty rates to the oil sold and its failure to deliver the total volumes of royalty-in-kind oil due. He then directed MMS to assign lease use volumes to each royalty rate category pro- portionately and recalculate the royalties due based on the reassignment of the total volume of oil used on the lease to each category. Sun appealed from this decision.

In its statement of reasons (SOR) on appeal, Sun contends that, under the Mineral Leasing Act, royalties are to be based on sales volumes rather than total production, and MMS failed to establish statutory authority for its method of calculating sliding scale royalties. Sun correctly notes that the issue of assessing royalties on that portion of the oil sold, rather than the total production, is well settled and cites Federal court and Board cases in support of this limitation. Sun contends that the Acting Director erred when finding the manner of determining the royalty rate set out in his decision does not impose a royalty on exempt lease fuel and conflicts with MMS regulations.

According to Sun, the courts, this Board, and MMS regulations and forms construe the word "production" to include only royalty bearing production, and the Director has misconstrued the plain meaning of the MMS regulations. Sun contends that the MMS decision "conveniently fails to discuss a single regulation that supports [its] newly devised methodology. The Director instead purports to find authority for his action in certain terms of the [lease] itself * * *" (SOR at 14). Sun cites the Board's holding in Amoco Production Co., 45 IBLA 16 (1980), in support of its contention that a pro- vision of the lease which purports to negate the express language of the Mineral Leasing Act, as amended, and the oil and gas operating regulations is a nullity. Sun further contends that the following portion of the Amoco decision directly supports its contention:

> Section 17 of the Mineral Leasing Act, as amended, 30 U.S.C. § 226(b) (1976), provides that royalty due the United States shall be computed at the rate fixed in the lease on the amount or value of production removed or sold from the lease. The words "removed or sold from the lease" were added after the word "production" in the 1946 amendment to the Act, August 8, 1946, 60 Stat. 951, giv- ing thereby persuasive evidence that the Congress intended to ensure that royalty would be due only on oil and gas removed

> from the leasehold, not on the total oil and gas produced from the well. The operating regulations in 30 CFR 221.44 specifi- cally state this exception.

* * * * * * *

> The Oil and Gas Operating Regulations in 30 CFR Part 221 were issued pursuant to the authority granted the Secretary by the Mineral Leasing Act, 30 U.S.C. § 189 (1976). The Secretary, therefore, must abide by and follow these regulations in adminis- tering oil and gas leases issued under the Act. As above quoted, section 221.44 provides that gas used for production purposes is excepted from royalty due the United States. We think it is error by the Geological Survey in this instance to seek payment of roy- alty for such gas, contrary to the statute and regulations, not- withstanding the language in section 5 of the Unit Agreement.

45 IBLA at 20. Finally, Sun contends that the method of determining the royalty rate is arbitrary and capricious. Sun advances three lines of reasoning in support of this argument. The first is that, contrary to the intent of the regulations, the method imposed penalizes operators who must use lease fuel for production, because this non-income generating oil must be included in the calculation of the royalty rate. According to Sun, this results in the lessee paying more royalty on less profit than would be the case for an operator not having a lease-fuel-consuming operation. The second is that MMS' interpretation is discriminatory because, under this interpretation, a lessee using lease fuel is always subject to a higher royalty rate than one who does not. The third is that when lease fuel volumes equal or exceed lease-sales volumes a higher royalty rate would always be imposed, none of the royalty bearing production would be sub- ject to the lower rate, and the objective of giving preferential treat- ment to marginally productive leases would be vitiated.

The Department filed an answer to Sun's SOR. MMS contends that its method of royalty calculation complies with both the lease and the regulations. MMS states that:

> Schedule D of the lease states that royalty will be calculated based on the "average production per well." 30 C.F.R. § 206.104 (formerly set forth in similar form at 30 C.F.R. § 221.49) also states that sliding scale royalties "are based on the average daily production per well * * *. The average daily production per well for a lease is computed on the basis of * * * the gross production from the leasehold." [Emphasis added.] Addition- ally, 30 C.F.R. § 206.104(i)(2) states: "The average production per well per day is determined by dividing the total production of the leasehold by * * * the number of wells * * *." See also 30 C.F.R. § 206.104(i)(1).

(Answer at 3). According to MMS, use of qualifiers such as "gross" and "total" in the regulations cited above would be superfluous unless it was possible to confuse gross or total production with "net" production; i.e., production that has been reduced (netted) by some amount. It is MMS' position that the use of the qualifiers in the regulatory language clearly refers to an amount that would include oil consumed on lease.

The answer also addresses Sun's contention that Amoco Production Co., supra, is applicable by noting that the Amoco case did not interpret the sliding-scale royalty provision of a Federal oil and gas lease. It further contends that its interpretation of the lease is consistent with the Amoco decision, noting that, although total production is used when determining the average daily production, the royalty amount is determined by applying the applicable royalty to the oil removed or sold from the lease.

Citing Marathon Oil Co. v. Andrus, 452 F. Supp. 548 (D. Wyo. 1978) (which had also been used as authority for Sun's arguments), MMS noted a statement made on page 551 of that opinion that:

> Prior to the issuance of the NTL-4 Notice, the practice of the United States Department of the Interior had been that, in determining the amount of production to which royalty rates will be applied, no royalty is payable on oil or gas unavoidably lost, used in lease or producing operations on the leasehold premises, or beneficially used for purposes of production on the leasehold.

MMS argues that this quote makes it clear that "production" includes all of the oil produced and the royalty is collected only on that portion of the production removed or sold from the lease.

In its final response to Sun's arguments MMS states that its appli- cation of the formula does not automatically impose a second tier royalty rate on any production legally subject to a royalty obligation, and submits two examples of how the royalty would be calculated using the formula each advances as being correct.

[1] The issue before us can be more readily understood when viewed in the light of an example of the royalty calculations which would be made using the method advanced by Sun and that advanced by MMS. As a starting point we will set out the relevant text of 30 CFR 206.104 (1987), 3/ which was applicable at the time of the production:

3/ The regulations have been substantially amended. See 53 FR 1218 (Jan. 15, 1988).

Royalty rates on oil; sliding- and step-scale leases (public land only).

Sliding- and step-scale royalties are based on the average daily production per well. The Supervisor shall specify which wells on a leasehold are commercially productive, including in that category all wells, whether produced or not, for which the annual value of permissible production would be greater than the estimated reasonable annual lifting cost, but only wells which yield a commercial volume of production during at least part of the month shall be considered in ascertaining the average daily production per well. The average daily production per well for a lease is computed on the basis of a 28-, 29-, 30-, or 31-day month (as the case may be), the number of wells on the leasehold counted as producing, and the gross production from the leasehold.

The following assumptions will be made in this example: (1) the month for which the royalty is to be calculated contains 30 days; (2) the lease contains 10 wells; (3) the total production from the wells was 15,000 barrels (bbl) of oil; (4) 4,500 bbls of oil were used on the lease; and 5) the oil was sold at $20/bbl.

We will now apply the regulation to the assumptions, first using the method urged by Sun, and then using the method urged by MMS:

<u>Sun's calculation:</u>

1. <u>Average daily production per well</u>:

$$\frac{(15{,}000 \text{ bbl} - 4{,}500 \text{ bbl})}{(30 \text{ days} * 10 \text{ wells})} = 35 \text{ bbl/well/day}$$

2. <u>Royalty at the various rates:</u>

A. At the 12 1/2% royalty rate:

20 bbl/day/well * 10 wells * 30 days = 6,000 bbl.

6,000 bbl * $20/bbl * 12 1/2% = $15,000.00

B. At the 14 2/7% royalty rate:

15 bbl/day/well * 10 wells * 30 days = 4,500 bbl.

4,500 bbl * $20/bbl * 14 2/7% = $12,857.14

3. <u>Total royalty due</u>:

$15,000.00 + $12,857.14 = $27,857.14

<u>MMS's calculation:</u>

1. <u>Average daily production per well</u>:

$$\frac{15{,}000 \text{ bbl}}{(30 \text{ days} * 10 \text{ wells})} = 50 \text{ bbl/well/day}$$

2. <u>Portion of oil consumed in production</u>:

$$\frac{4{,}500 \text{ bbl}}{15{,}000 \text{ bbl}} = 30\%$$

3. <u>Royalty at the various rates</u>:

A. At the 12 1/2% royalty rate:

i) total production:

20 bbl/day/well * 10 wells * 30 days = 6,000 bbl.

ii) production upon which royalty is assessed:

6,000 bbl - (6,000 * 30%) = 4,200 bbl

iii) royalty due:

4,200 bbl * $20/bbl * 12 1/2% = $10,500

B. At the 14 2/7% royalty rate:

i) Total production:

30 bbl/day/well * 10 wells * 30 days = 9,000 bbl.

ii) production upon which royalty is assessed:

9,000 bbl - (9,000 * 30%) = 6,300 bbl

iii) royalty due:

6,300 bbl * $20/bbl * 14 2/7% = $18,000

4. Total royalty due:

$10,500.00 + 18,000.00 = $28,500.

As can be seen from the examples, the divergence of accounting pro- cedures comes from Sun's deduction of the oil consumed on the lease prior to calculating the average daily production from the lease and MMS' calcu- lation of the average daily production based on total production and subse- quent pro-rata deduction of that portion consumed to each barrel of oil subsequently sold or removed. Sun argues that its method recognizes that there should be no royalty imposed on oil used on the lease and, therefore, the royalty calculation should be made as if the oil used on the lease had never been produced. On the other hand, MMS argues the same amount of oil is used to produce each barrel of oil subject to the 12-1/2 percent royalty as is used to produce the oil subject to the 14-2/7 percent royalty, and the pro-rata application of consumed oil recognizes this fact.

Both sides have cited a number of cases in support of their respective positions. However, we find none of these cases to be directly in point regarding the accounting procedure to be used when applying a sliding-scale or a step-scale royalty, when a portion of the oil produced had been used on the lease. To this extent this appears to be a case of first impression.

As noted above, in Amoco, supra, the Board stated that section 17 of the Mineral Leasing Act, as amended, 30 U.S.C. § 226(b) (1982), provides that royalty due the United States shall be computed at the rate fixed in the lease on the amount or value of production removed or sold from the lease. Both accounting procedures satisfy this requirement. The royalty is computed at the rate fixed in the lease, and is assessed against the amount or value of the production removed or sold from the lease. As can be seen from the examples, the amount of oil subject to a royalty is the same in each case (Sun: 6,000 bbl + 4,500 bbl = 10,500 bbl, and MMS: 4,200 bbl + 6,300 bbl = 10,500 bbl). Neither accounting method assesses a roy- alty on the oil consumed during the process of production.

The initial question before us is whether a reasonable interpre- tation of the applicable regulations would allow the imposition of the MMS accounting procedure when determining the royalty for the oil sold or removed. Therefore, we will first examine the appropriate regulations to determine if they contain language which would permit the use of the MMS accounting method.

The regulation at 30 CFR 206.104 states that sliding-scale royalties "are based on the average daily production per well * * *. The average daily production per well for a lease is computed on the basis of * * * the gross production from the leasehold." MMS focuses on the term "gross" with the conclusion that the average daily production calculation should include oil used on the lease. The MMS interpretation also complies with 30 CFR 206.104(i)(2), which states: "The average production per well per day is determined by dividing the total production of the leasehold by * * * the number of wells * * *." <u>See also</u> 30 CFR 206.104(i)(1). The term "total production," as used in the regulations, can reasonably be interpreted to mean the total production from the wells before deducting the oil used on the lease. Thus, the regulations are subject to the interpretation advanced by MMS.

The August 13, 1987, decision is a statement of the Department's accounting policy applicable to calculating royalties due under the regu- lation, and is within the language and purpose of the Act. It is, of course, within the authority of the Department to interpret its own regu- lations, and its interpretation should be given great deference. Udall v. Tallman, 380 U.S. 1, 16 (1965). This being the case, the policy of pro- rating oil used on the lease among the various applicable royalty rates, as stated in the August 13, 1987, decision, is neither arbitrary nor capri- cious, if applied to all lessees falling within this category. 4/

Throughout the briefs filed with this Board, Sun has couched the August 13, 1987, MMS royalty-rate determination as "new methodology." At no place in the case file, the MMS decisions, or pleadings MMS has filed with this Board is there any indication that the methodology set out in the August 13, 1987, decision is an application of a longstanding account- ing procedure. Rather, MMS addresses the issue in terms of its authority to enforce a public right or protect a public interest, which "is not 'lost by acquiescence of its officers or by their laches, neglect of duty, failure

4/ A parallel is suggested. The step-scale royalty is similar to the graduated-scale income tax, and the IRS approach to the deduction of business expenses is similar to the Sun royalty approach. If the IRS adopted the MMS approach, taxpayers now deducting business expense would be subject to increased tax liability.

to act, or delays in performance of their duties.' Otay Mining Co., 62 IBLA 166, 168 (1982)" (Answer at 6).

We have no quarrel with the notion that MMS is not forever bound by its prior interpretation of a statute or regulation, even though that interpretation has been applied for a long time. If MMS determines that a different construction should be given, it is within MMS' prerogative to apply the new construction, so long as it is "adequately explicated." See, e.g., NLRB v. Weingarten, Inc., 420 U.S. 251, 265-67 (1975); Brennan v. Gilles & Cotting, Inc., 504 F.2d 1255, 1264-66 (4th Cir. 1974). Our inquiry does not end here, however.

When MMS finds that a prior interpretation of its regulations was based upon a mistake of law it is entitled to retroactively correct that interpretation. However, it must clearly set forth and identify the mistake of law in sufficient detail to show that the departure from the prior administrative position is not arbitrary or capricious. See, e.g., Squaw Transit Co. v. United States, 574 F.2d 492 (10th Cir. 1978);
FTC v. Crowther, 430 F.2d 510, 514 (D.C. Cir. 1970); Issac & Katherine Bonaparte v. Commissioner of Indian Affairs, 9 IBIA 115, 122 (1981). When MMS departs from a prior administrative position and seeks to apply its new position rectoactively, it is not enough to state that it has the right to do so. A mere showing that the new interpretation is within the meaning of the law is not sufficient to meet that burden of clearly setting forth and

identifying the mistake of law. If the prior interpretation is also within the meaning of the law, no mistake is established. 5/

We will examine the appropriate regulations to determine if the regu- latory language would also permit the use of the accounting method applied by Sun. As previously noted, 30 CFR 206.104 states that sliding-scale royalties "are based on the average daily production per well * * *. The average daily production per well for a lease is computed on the basis of * * * the gross production from the leasehold." Sun's interpretation focuses on the phrase "from the leasehold," which Sun interprets to mean removed or sold. Under this interpretation, the term "gross" would be syn- onymous with the term "sum of" and refer to all producing wells. Like- wise, the term "total production" in the phrase "average production per well per day is determined by dividing the total production of the leasehold by * * * the number of wells * * *" in 30 CFR 206.104(i)(2) can be interpreted to mean the total production subject to a royalty. Thus, these regulations are also subject to the interpretation advanced by Sun.

Sun's interpretation conforms with the Geological Survey Conservation Division Manual (GS Manual). Part 647 of the GS Manual addresses issues of accounting. Chapter 13 of that part is entitled "Variable Royalty Rate

5/ When the decision fails to clearly set forth and identify the mistake of law in sufficient detail, it is proper for this Board to assume that the prior practice was also within the ambit of the statutes and regulations. All else appearing regular, administrative officials are presumed to have properly discharged their duties. H.S. Rademacher, 58 IBLA 152, 88 I.D. 873 (1981), and cases cited therein.

and Well Count." Part 647, Chapter 13.3 provides: "In calculating a roy- alty rate, production and sales are generally considered to be the same thing, with the sales figures being used to calculate all royalty rates even though the word "production" may be used in this chapter." 6/ GS Manual, Part 647.13.3A (Release No. 26, July 5, 1974). When Part 647.13.3A is applied, the oil used on the lease is not sold, it need not be reported, and the accounting method advanced by Sun is clearly applicable.

After examining the provisions of Part 647.13 of the GS Manual, which was specifically written to provide "guidance and procedures for reviewing variable royalty rate * * * leases to ensure that royalties are properly computed," 7/ it is our opinion that the GS Manual clearly "specified that a particular method of valuation adopted by a lessee [i.e., Sun] is ade- quate." Supron Energy Corp., 46 IBLA 181, 191 (1980), appeal filed sub nom. Supron Energy Corp. v. Hodel, Civ No. 80-0463 JB (D.N.M., June 18, 1980). There is also no question that Survey was applying this interpre- tation before, during, and after the period in question. When the lease was renewed, Schedule D (quoted above) became applicable as provided by Exhibit 3, Part 647.13.2G, of the GS Manual.

We now will consider whether Sun had relied upon MMS' acceptance of the accounting procedure used by Sun when calculating the royalty due on

6/ The use of the term "production" in Chapter 13 parallels the language found in 43 CFR 221.49 (7 FR 4132 (June 2, 1942)). This statement is thus an interpretation of that regulation.
7/ GS Manual, section 647.13.1.

the oil production removed or sold from the lease. Sun calculated the royalty due on the basis set forth in the example above during the entire period in question, and states that it did so in reliance upon its belief that the Department had accepted Sun's method of calculating royalties in the 1970 and 1979 correspondence.

On February 4, 1970, the Regional Oil and Gas Supervisor for the Pacific Region of the Geological Survey (Survey) wrote the Accounting Supervisor of Sun in Tulsa concerning Sun's January 1969 Report of Sales and Royalty for this lease. At the time Survey's figures for the amount subject to royalty were lower than Sun's:

> We began making inquiries into the matter, and through a phone call to your Mr. J. T. Gibson we learned that this oil (Code 50) was used on the lease. We contacted Mr. J. R. Hinkle, District Engineer in your Newhall, California, office, and by letter of September 26 he informed us that the oil was "consumed in firing the lease heater treater facilities only."
>
> Early in October our District Engineer visited the Maxwell lease and confirmed that the oil was used on the lease for "royalty free" purposes. After obtaining all the facts, we realized that Sun-DX had paid royalty on lease oil for which royalty was not required.
>
> *　*　*　*　*　*　*
>
> Although your oil purchase statements continue to show Code 50 entries, <u>we have not included them in our royalty calculations since we began to take our royalty in kind. In this regard, we suggest that you discontinue showing these items on your oil purchase statements. Since the oil is used on the lease and is not subject to royalty, you do not need to report the oil</u>. If convenient, please make the change effective with your January 1970 statement. [Emphasis added.]

This letter confirms the Department's acceptance of the interpreta- tion advanced by Sun, as it would be necessary to report the quantity of oil used on the lease under the interpretation set out in the August 13, 1987, decision. We believe that this correspondence and Sun's subsequent royalty reports, which conformed with the described procedure, are ample evidence that Sun relied upon the assurances that the oil should be accounted for in the manner outlined in the GS Manual. Indeed, there is nothing in the record reflecting any reservation about the aspect of Sun's royalty accounting now in question until the California audit.

MMS argues that the United States is not estopped from asserting pre- rogatives granted by regulatory authority. However, this is not a matter of estoppel. Rather, MMS has stated a new policy, which amended the Depart- ment's previous policy regarding the accounting procedure to be used for calculating a sliding-scale or step-scale royalty when a portion of the production is used on the lease. Having determined that both accounting procedures are within the scope of the regulation, we must now determine whether the accounting procedure set out in the August 13, 1987, decision can be retroactively applied to the oil produced during the audit period.

This case, like all cases of first impression, has a retroactive effect. See S.E.C. v. Chenery Corp., 332 U.S. 194, 203 (1947).

In Runnells v. Andrus, 484 F. Supp. 1234 (D.C. Utah 1980), the court addressed whether an interpretive ruling by the Department would be given retroactive effect, and applied the balancing test set out in Retail, Wholesale & Department Store Union v. NLRB, 466 F.2d 380, 390 (D.C. Cir. 1972). We believe that the application of this test weighs in favor of Sun. There is no question that when MMS adopted the new accounting procedure in its decision, that decision was an abrupt depar- ture from a well-established practice, and not an attempt to fill a void in an unsettled area of the law. The facts clearly demonstrate that Sun relied upon the prior interpretation during the entire audit period. The newly adopted accounting procedure clearly imposes an additional royalty burden on Sun. In Runnells, the court found that the prejudice to the plaintiffs substantially outweighed the statutory interest and purposes sought to be protected, and held that the rule announced below should be applied prospectively. Runnells v. Andrus, supra at 1240. The same rationale applies in this case. We therefore find that MMS has the author- ity to impose the accounting procedure for calculating royalties set out in the August 13, 1987, decision, but that this accounting procedure should be applied prospectively. 8/

In light of our findings, appellant's request for a hearing is denied.

8/ In reaching this conclusion we need not address whether the provi- sions of 28 U.S.C. § 2415 (1982) are applicable to a portion of the royalties MMS had found to be due and owing.

Accordingly, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision of the Acting Director, Minerals Management Service, is affirmed as modified.

R. W. Mullen
Administrative Judge

I concur:

Will A. Irwin
Administrative Judge