

AMOCO PRODUCTION CO.

IBLA 88-551

Decided April 3, 1990

Appeal from a decision of the Director, Minerals Management Service, affirming an order requiring the payment of additional royalties on natural gas produced from Outer Continental Shelf oil and gas lease OCS-G 0297. MMS-87-0066-OCS.

Affirmed.

1. Oil and Gas Leases: Royalties: Generally--Outer Continental Shelf Lands Act: Oil and Gas Leases

A royalty valuation letter issued by Geological Survey specifically addressing royalty computation for gas delivered under a particular contract from a specific Outer Continental Shelf oil and gas lease committed to a unit does not establish the royalty base for gas production from a well subsequently completed on the lease in a non-unitized formation.

2. Oil and Gas Leases: Royalties: Generally--Outer Continental Shelf Lands Act: Oil and Gas Leases

Where Geological Survey issues a royalty valuation letter determining the proper method of computing royalties owed to the United States based on the assumption that the natural gas involved is subject to price control, but the gas has in fact been decontrolled, the letter provides no basis for the computation of the amount of royalty due the United States.

3. Oil and Gas Leases: Royalties: Generally--Outer Continental Shelf Lands Act: Oil and Gas Leases

Where a company's gas production from a well on an Outer Continental Shelf oil and gas lease has been valued by MMS on the basis of the highest prices paid for like-quality gas produced from other wells on the same lease, an assertion by that company that it has been treated unfairly because its gas production from

the well has been valued differently than another company's production from the same well during the same period will be rejected based on MMS' explanation that it had not audited the royalty payments of the second company.

APPEARANCES: Robert C. Smith, Esq., George J. Domas, Esq., New Orleans, Louisiana, for appellant; Peter J. Schaumberg, Esq., Geoffrey Heath, Esq., Howard Chalker, Esq., Office of the Solicitor, U.S. Department of the Interior, Washington, D.C., for the Minerals Management Service.

#### OPINION BY ADMINISTRATIVE JUDGE HARRIS

Amoco Production Company (Amoco) has appealed from an April 19, 1988, decision of the Director, Minerals Management Service (MMS), affirming a January 2, 1987, order by the Regional Manager, Tulsa Regional Compliance Office, MMS, directing Amoco to pay additional royalties in the amount of \$2,557,783.56 on non-unit gas production from lease OCS-G 0297, Well No. 30, for the period March 1979 through April 1982.

Although Well No. 30 is located within the geographic area of the Vermilion Block 14 Unit, it was completed and produces from a depth below that which is unitized in the Vermilion Block 14 Unit (Statement of Reasons (SOR) at 3 n.3). Both the unit and the well are operated by Union Oil Company of California (Union). Union and Amoco each own 50 percent of the production from the well. From March 1979 through April 1982, Amoco elected to sell its share of gas produced from Well No. 30 to Florida Power and Light Company (FPLC) under a warranty contract; however, gas from Well No. 30 was not specifically dedicated to that contract.

For purposes of royalty computation, Amoco valued its gas production at the Vermilion Block 14 Unit weighted average sales price. Amoco based its valuation on a January 9, 1975, royalty valuation letter from the Geological Survey (Survey) <sup>1/</sup> to Union, a copy of which was sent to Amoco. This letter stated in pertinent part:

This is to inform you that the price of gas for the purpose of computing royalty for gas delivered under contracts not subject to the jurisdiction of the Federal Power Commission (currently Florida Power & Light Company) from leases OCS-G 0297, OCS 0548, OCS 0549, OCS-G 1329, OCS-G 1356, and OCS-G 1357, committed to the Vermilion Block 14 Unit, will be the weighted average price paid for gas sales from the Unit, subject to the jurisdiction of the Federal Power Commission.

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<sup>1/</sup> Pursuant to Secretarial Order No. 3071, dated Jan. 19, 1982, the functions of Survey relating to oil and gas lease royalty management were transferred to MMS. 47 FR 4751 (Feb. 2, 1982).

In his January 2, 1987 order, the Regional Manager directed Amoco to pay \$2,557,783.56 in additional royalties for the period March 1979 through April 1982. He rejected Amoco's use of the weighted average unit sale price, stating that the January 9, 1975, valuation letter "specific-ally addressed only the Vermilion Block 14 Unit production," and that Well No. 30 gas production was not unit production. He found instead that, "Based upon the geological formation and spud date, [Well No. 30] qualified for Natural Gas Policy Act (NGPA) of 1978, Section 107 prices \* \* \*," which he concluded were applicable for the period from March 1979 through October 1979. <sup>2/</sup> He also referred to two similar value determination letters sent to Amoco: (1) an April 8, 1981, letter from Survey with an effective date of January 9, 1981, which provided in part that "the value for computing royalties shall be based upon the lease delivery volume times the applicable FERC [Federal Energy Regulatory Commission]-approved sales price or higher price if received \* \* \*," and (2) a February 14, 1983, letter from MMS modifying the April 8, 1981, letter to provide that the value for computing royalties "shall be based on the lease delivery volume times the higher of the price actually received or the regulated sales price." The Regional Manager did not explain the significance of either of those letters to his determination.

He concluded that additional royalties were due based on (1) the regulated prices (NGPA Section 107) from March 1979 through October 1979; (2) prices paid to Union for its share of gas production from the well from November 1979 through December 1980; and (3) prices paid to Amoco for gas from other NGPA Section 107 wells on lease OCS-G 0297 for January 1981 through April 1982.

Amoco appealed that order to the Director, MMS. In his decision, the Director also held that the January 5, 1975, royalty valuation letter (upon which Amoco had based its valuation) was not applicable to Well No. 30, and that the Department's "first explicit action to officially determine value of production from Well No. 30 was taken when MMS issued the January 2, 1987, order appealed herein." The Director further stated that the April 8, 1981, valuation letter (to which the Regional Manager had referred) was inapplicable to gas production from Well No. 30 because, "To the extent there was no FERC approved sales price on or after November 1, 1979, there was no basis for determining whether the price received by the lessee was higher than the FERC approved sales price during the period January 9, 1981, through April 1982." The Director then ruled that the Regional Manager had properly valued gas production from Well No. 30 consistent with the criteria in 30 CFR 206.150 (1987), formerly 30 CFR 250.64 (1979).

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<sup>2/</sup> Section 107(a)(1) of the NGPA, 15 U.S.C. § 3317(a)(1) (1982), established a ceiling price for "high-cost" natural gas, which under certain circumstances was gas produced from "a depth of more than 15,000 feet." Well No. 30 was completed on Jan. 28, 1979, at a depth of 15,326 feet. Effective Nov. 1, 1979, high-cost natural gas became deregulated. See 44 FR 61951 (Oct. 29, 1979).

The royalty valuation regulation which was effective at the beginning of the period in question, 30 CFR 250.64 (1979), provided:

The value of production, for the purpose of computing royalty, shall be the estimated reasonable value of the product as determined by the supervisor, due consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field or area, to the price received by the lessee, to posted prices, and to other relevant matters. Under no circumstances shall the value of production of any said substance for the purposes of computing royalty be deemed to be less than the gross proceeds accruing to the lessee from the sale thereof or less than the value computed on such reasonable unit value as shall have been determined by the Secretary. In the absence of good reason to the contrary, value computed on the basis of the highest price paid or offered at the time of production in a fair and open market for the major portion of like quality products produced and sold from the field or area where the leased lands are situated will be considered to be a reasonable value. [3/] [Emphasis added.]

On appeal, Amoco asserts that it correctly valued gas produced from Well No. 30 in accordance with the January 9, 1975, valuation letter because the gas "was produced from Lease OCS-G 0297 and because that lease is committed to the Vermilion Block 14 Unit" (SOR at 5-6). Citing Superior Oil Co., 12 IBLA 212 (1973), Amoco contends that the letter is binding on MMS and suggests that MMS should have issued a new valuation letter if it concluded, during its review period, that the January 1975 letter should not be applicable to non-unitized production from wells within the Vermilion Block 14 Unit. Amoco also argues that the April 8, 1981, valuation letter was issued at a time when "MMS knew full well \* \* \* that there was no regulated price for the gas from Well No. 30," and, therefore, by elimination the only valuation provided for by the letter was the price received by it under the contract (SOR at 8-9).

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3/ Effective Dec. 13, 1979, which was during the period in question, the Department amended 30 CFR 250.64 (1979) to provide that the "value of production shall never be less than the fair market value," which value would be determined considering the highest price paid for a part or for a majority of like-quality products produced from the field or area, the price received by the lessee, posted prices, regulated prices, and other relevant matters. 44 FR 61903 (Oct. 26, 1979). The Department subsequently redesignated the regulation 30 CFR 206.150, effective Aug. 5, 1983. 48 FR 35641 (Aug. 5, 1983). Effective Mar. 1, 1988, the Department significantly amended the regulations applicable to the valuation of oil and gas for royalty computation purposes, but with prospective effect only. See 53 FR 1184, 1230 (Jan. 15, 1988). The regulations applicable to the valuation of gas for royalty computation purposes are currently codified at 30 CFR Subpart D (53 FR 1272 (Jan. 15, 1988)).

MMS contends that the January 9, 1975, letter is not applicable to gas production from Well No. 30, because that well was not a unit well. It also claims that neither the April 8, 1981, nor the February 14, 1983, valuation letters barred it from subsequently collecting additional royalties. MMS asserts that the 1981 and 1983 letters clearly state that the price received by the lessee will be accepted only if it is higher than the FERC-approved sales price and that since there was no FERC-approved sales price on or after November 1, 1979, there was no basis for determining whether the price received by the lessee was reasonable.

The applicable royalty valuation regulation, 30 CFR 250.64 (1979), as amended, establishes two general rules. One is that in the absence of a determination of reasonable unit value by the Secretary, the highest price paid for the major portion of like-quality products sold from the field or area will normally be considered reasonable value. The second is that in no circumstances shall the value be less than the gross proceeds actually accruing to the lessee. Transco Exploration Co., 110 IBLA 282, 317-18, 96 I.D. 367, 386 (1989). While the regulation does not specify all of the factors which are to be considered or indicate the exact weight each is to be given, it does give the Director, MMS, a great deal of discretion in establishing value for the purposes of computing royalty, including, in this case, utilization of the regulated price for the period March 1979 through October 1979. See Marathon Oil Co. v. United States, 604 F. Supp. 1375, 1382 (D. Alaska 1985), aff'd, 807 F.2d 759 (9th Cir. 1986), cert. denied, 107 S. Ct. 1593 (1987); Amoco Production Co., 112 IBLA 77, 81 (1989).

[1] The January 9, 1975, letter specifically addressed royalty computation for gas delivered under the FPLC contract from lease OCS-G O297, "committed to the Vermilion Block 14 Unit." That letter gave no instructions regarding valuation, for royalty purposes, of non-unitized gas production. Well No. 30, a non-unitized well, was not completed until January 28, 1979. Amoco knew or should have known that the 1975 letter was not controlling as to gas production valuation from Well No. 30. 4/

Superior Oil Co., supra, cited by Amoco, held, inter alia, that Survey could not change the royalty base of production retroactively where the royalty base which had been accepted by the Oil and Gas Supervisor for a period of years was "within the ambit of his authority." 12 IBLA at 226. In this case, Amoco claims that the authority for making its payments was the January 9, 1975, letter. That letter, however, did not purport to establish a royalty base for non-unit production, which is the production in question. Consequently, there can be no issue concerning

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4/ The fact that Amoco included a statement on its monthly "250.67 worksheets" commencing in March 1979, which stated "Florida Power & Light prices computed in accordance with your letter to us dated 1-9-75," is of no consequence, because the referenced letter was not applicable to the production from Well No. 30.

retroactive change of a royalty base, since none was established by that letter for the production from Well No. 30.

[2] Likewise, the April 8, 1981, and February 14, 1983, valuation letters did not establish a formula by which MMS was required to compute royalties on gas production from Well No. 30 during the disputed period. First, the 1983 letter has no bearing on this case because the valuation period in question is from March 1979 through April 1982. Second, the 1981 letter stated that the value for computing royalties should be based on applicable FERC-approved prices, "or higher price, if received." Clearly, Amoco's contention that this letter constitutes approval for utilizing its price under the FPLC contract has no merit.

There is no dispute that the production in question was high-cost natural gas subject to section 107 of the NGPA and that the price of such gas was deregulated effective November 1, 1979. Therefore, at the time of the issuance of the 1981 letter there were no FERC-approved sales prices with which to compare Amoco's contract price.

The situation involving the 1981 letter is similar to that presented in Transco, supra, which involved July 16, 1979, instructions from the Oil and Gas Supervisor, directing the lessee to compute royalty "based on the lease delivery volumes times the applicable FERC-approved sales price, or higher price, if received." As we observed in Transco, 110 IBLA at 316, 96 I.D. at 386, after deregulation, the July 16, 1979, valuation instructions ceased to have a bearing on gas valuation and did not prevent MMS from assessing value for royalty purposes based on other criteria. We explained:

Once production \* \* \* was price-decontrolled, however, the [July 16, 1979 valuation] letter had no continuing applicability, as there was no longer any applicable FERC-approved sales price which could be used to establish the price paid for the major portion of like quality products. Thus, the first benchmark once again reverted simply to the highest price paid for the major portion of like quality products.

Transco at 318, 96 I.D. at 387.

In this case, however, deregulation occurred prior to the issuance of the 1981 letter. Thus, the 1981 letter was ineffective upon issuance, and the relevant question was simply whether the production had been valued as explained in Transco, i.e., based on "the highest price paid for the major portion of like quality products."

Amoco asserts that even if it is concluded that the valuation letters are not applicable, it was arbitrary for MMS to value Amoco's share of gas production from Well No. 30 for the period of January 1981 through April 1982 on a basis different than that for Union's share of the gas production for the same time period. For the period January 1981 through April 1982, MMS valued Union's share of gas production from Well No. 30 on the basis

of the price Union received from its purchaser, Trunkline Gas Co. This valuation, Amoco asserts, was less than half that used by MMS to calculate royalty on gas sold by Amoco to FPLC during the period January 1981 through April 1982 (Supp. SOR at 3). <sup>5/</sup>

Amoco points out that in July 1985, the Royalty Valuation and Standards Division, MMS, concluded that "the prices received by Union for their share of the gas production in question from November 1979 through December 1980 are acceptable for valuing Amoco's share of gas production from the wells that qualified as NGPA Section 107(c)(1)" (Supp. SOR, Exh. F-12). While the record shows that MMS, in fact, utilized those prices to value Amoco's gas for the period November 1979 through December 1980, Amoco asserts that MMS' position is "devoid of any suggestion" why the prices received by Union should not also be applied to production in the period subsequent to December 1980.

MMS responds, with reason, that its valuation of Amoco's gas production from January 1981 through April 1982 was based on the fact that Amoco could have sold its gas from Well No. 30 for the same price it received for other NGPA Section 107 gas produced from lease OCS-G 0297. MMS further explains that since Union has not been audited, MMS "is unsure if Union sold similar gas at a higher price. Therefore, MMS does not know if Union could have sold its gas from the Well for a higher price" (Answer at 7).

Amoco has submitted various exhibits indicating that MMS valued its gas production for royalty purposes differently than it valued Union's in the period from January 1981 through April 1982. Amoco does not dispute, however, that it could have sold gas from Well No. 30 at prices higher than those it received from FPLC. Amoco's contention is directed to the fairness of MMS's disparate treatment for royalty purposes of the gas production from the same well during the same time period.

The controlling royalty valuation regulation provides that the value of production shall not be less than fair market value, and that the Director shall consider the highest price paid for a part or for the majority of like-quality products produced from the field or area, the price received by the lessee, posted prices, regulated prices, and other relevant matters. In this case, for the period January 1981 through April 1982, gas production from the well has been valued differently for Amoco and Union. Amoco's production has been valued by MMS based on the highest prices paid for Amoco's production of NGPA section 107 gas from other wells on the lease. These prices fall within the regulatory definition of value of production. Therefore, we conclude that MMS properly valued Amoco's gas production from Well No. 30 for the period January 1981 through April 1982.

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<sup>5/</sup> For a comparison of those different valuations and the royalties based thereon, see Exhibits 1 and 2 attached to Exhibit D of Amoco's SOR.

[3] As of the date of the Director's decision, Union had valued its gas production on the basis of its Trunkline contract price, which is significantly lower than the value assigned to Amoco's identical production. MMS explains that such valuation is not arbitrary because it has not audited Union. We accept that explanation, yet we note that MMS' further statements that it is "unsure" whether Union sold similar gas at a higher price and it does not know whether Union could have sold its gas at a higher price are irrelevant, and, in fact, contrary to the general principle that the reasonable value of production for the purpose of calculating the royalty due the United States is the highest price paid for a major portion of like-quality products produced or sold from the same field or area, or the gross proceeds actually received by the lessee, whichever is higher. See Transco Exploration Co., 110 IBLA at 320-23, 96 I.D. at 388-89. Clearly, since Amoco's prices for NGPA section 107 gas from other wells on the lease were, during the period January 1981 through April 1982, the highest prices paid for a major portion of like-quality gas produced from the lease, Union's gas production should also be valued accordingly.

Finally, Amoco charges that even if additional royalty were due, which it disputes, the right of MMS to claim additional payments accrued at the time the underpayment was made and the statute of limitations, 28 U.S.C. § 2415(a) (1982), which allows 6 years for the United States to file an action for money damages based on contracts, precludes recovery. <sup>6/</sup> MMS responds, citing Foote Mineral Co., 34 IBLA 285 (1978), that the purpose of this administrative proceeding is to determine the royalty obligation and that a statute of limitations relates to the remedy rather than the obligation. <sup>7/</sup> It argues that Amoco's assertion of the statute of limitations presents no issue for resolution in this forum. Whether or not the 6-year statute of limitations may bar an "action based on contract" to collect additional royalties is not an issue before this Board. <sup>8/</sup> We

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<sup>6/</sup> Amoco states that it is premitting a determination of whether the Louisiana 3-year statute of limitations found at section 3494(5) of the Louisiana Civil Code Article is applicable under 43 U.S.C. § 1333(a)(2)(A) (1982). We note that such an argument was fully addressed and rejected in Amoco Production Co., 112 IBLA at 87-88.

<sup>7/</sup> The Foote Mineral case involved a question of royalties on lithium extracted from brines on lands covered by potassium and sodium leases, as well as by unpatented placer mining claims. Although the company argued that no royalties were required because lithium was a locatable, rather than a leaseable mineral, the Board ruled that royalties were properly owed. The Court of Claims reversed, finding that the leases were invalid for lack of valuable deposits of potassium and sodium and it directed that any royalties paid by the company be refunded. Foote Mineral Co. v. United States, 654 F.2d 81 (1981). Nevertheless, the rationale of the Board's decision regarding the statute of limitations is viable.

<sup>8/</sup> We note that in Phillips Petroleum Co. v. Lujan, No. 88-C-1487-E (N.D. Okla., Oct. 18, 1989), the court ruled that the 6-year statute of limitations contained in 28 U.S.C. § 2415(a) (1982) prohibits MMS from auditing royalty payments made more than 6 years prior to the initiation of the audit. The Government has sought amendment of the court's judgment in that case. No action has been taken on that request.

are reviewing the Director's determination that Amoco is obligated to pay additional royalties. With that determination, we agree.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision appealed from is affirmed.

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Bruce R. Harris  
Administrative Judge

I concur:

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David L. Hughes  
Administrative Judge

June 13, 1990

IBLA 88-551	:	MMS 87-0066-OCS
114 IBLA 42	:	
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AMOCO PRODUCTION CO.	:	Offshore Gas Royalties
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	:	Motion for Reconsideration
	:	Granted;
	:	Motion to Vacate Board Decision
	:	Reported as 114 IBLA (1990)
	:	Granted; Appeal Dismissed

ORDER

On April 3, 1990, the Board issued its decision in this case. On June 1, 1990, counsel for the Minerals Management Service and counsel for Amoco Production Co. (Amoco) filed a "Joint Motion for Reconsideration and Motion to Vacate Decision." Therein, they explain that on March 30, 1990, Richard L. Flury, Vice President, Amoco, and David C. O'Neal, Assistant Secretary--Land and Minerals Management, executed an agreement settling a addressed in 114 IBLA 42 (1990. As part of that settlement, the United States agreed to dismiss with prejudice the January 2, 1987, order of the Regional Manager, Tulsa Regional Compliance Office, which was the underlying subject of this appeal.

Counsel represent that the Board's decision addresses issues beyond the scope of the matters involved in the settlement agreement and that Amoco will be adversely affected to the extent the Board's decision constitutes precedent with respect to such issues. Counsel jointly request that we reconsider our April 3, 1990, decision and vacate it.

Under 43 CFR 4.403, the Board may grant reconsideration in extraordinary circumstances where sufficient reason is shown. In this case extraordinary circumstances exist in that a settlement affecting this appeal was finalized prior to issuance of our decision. 1/ The parties have shown sufficient reason for granting both the motion for reconsideration and the motion to vacate.

Accordingly, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the motion for reconsideration is granted, and the Board's decision reported at 114 IBLA 42 (1990) is vacated. Amoco's appeal in this case is dismissed, and the case is returned to MMS in order to carry out the terms of the settlement.

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Bruce R. Harris  
Administrative Judge

I concur:

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David L. Hughes  
Administrative Judge

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1/ In the future, where parties are seriously negotiating the settlement of issues which would resolve an appeal or appeals pending before the Board, the parties should seek a stay of the Board's consideration thereof during the pendency of such negotiations. In that way, the Board may concentrate its resources on cases not amenable of settlement.

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