

GEORGE M. WILKINSON
FIDELITY TRUST BUILDING, INC.

IBLA 92-89

Decided October 2, 1992

Appeal from a decision of the Colorado State Office, Bureau of Land Management, cancelling geothermal resources lease C-29556.

Reversed.

1. Geothermal Leases: Cancellation

A geothermal resources lease was properly cancelled where the lessee failed, as required by 43 CFR 3203.5, to notify BLM of performance of required exploration at any time prior to the end of the sixth lease year or within 60 days thereafter. Because the lessee was not given 30 days to correct the violation prior to cancellation, the decision cancelling the lease is reversed and the lessee is allowed 30 days in which to correct the violation, as provided by 43 CFR 3203.5 in order to retain the lease.

APPEARANCES: George M. Wilkinson, pro se and for Fidelity Trust Building, Inc.

OPINION BY ADMINISTRATIVE JUDGE ARNESS

On May 31, 1991, the Colorado State Office, Bureau of Land Management (BLM), cancelled geothermal resources lease (C-29556) issued to George M. Wilkinson and Fidelity Trust Building, Inc. (Fidelity), because they had failed to demonstrate that they had made diligent exploration expenditures in the amount of \$952 or, in lieu thereof, to submit additional rental in the amount of \$714 prior to the conclusion of the sixth lease year on April 30, 1991, as required by 43 CFR 3203.5. Wilkinson and Fidelity timely appealed from the May 1991 BLM decision.

Before the appeal was reached for review, however, the Regional Solicitor, on behalf of BLM, requested remand of the case so that BLM could review additional proof, submitted after the appeal was taken, that Wilkinson and Fidelity had made the required diligent exploration expenditures and issue another decision on the merits. Accordingly, on August 14, 1991, the Board set aside the May 1991 BLM decision and remanded the case to BLM for further adjudication.

Thereafter, BLM reviewed the additional information submitted by Wilkinson and Fidelity. By decision dated October 8, 1991, the Colorado State Office once again cancelled the subject lease because Wilkinson and Fidelity had failed to satisfy the regulatory requirement regarding proof of diligent exploration expenditures "as no on the ground activities have taken place on the leasehold." BLM found that, while the lessees had submitted a Notice of Intent (NOI) to Conduct Operations, "the information needed to process it and to approve the Application for Permit to Drill [APD] has not been submitted to the authorized officer." Wilkinson and Fidelity have appealed from the October 1991 BLM decision.

In their statement of reasons for appeal (SOR), appellants contend that they made the required diligent exploration expenditures for the sixth lease year and satisfied the requirements of 43 CFR 3203.5. They explain that they had, in prior lease years, expended in excess of \$366,588 in connection with "exploration and permits" and "geophysical exploration" and that these expenditures should, in accordance with that regulation, be carried forward to the sixth lease year (SOR at 3). Appellants argue that the subject lease should not have been cancelled for failure to comply with 43 CFR 3203.5.

[1] Lease C-29556 was issued to appellants for 10 years effective May 1, 1985. It encompasses 237.29 acres of land situated in sec. 2, T. 6 S., R. 90 W., sixth principal meridian, Garfield County, Colorado, near where South Canyon Creek enters the Colorado River. It was issued pursuant to the Geothermal Steam Act of 1970, as amended, 30 U.S.C. §§ 1001-1027 (1988). Section 4 of the lease requires the lessee to engage in diligent exploration "as required by regulations." The applicable regulation, 43 CFR 3203.5, provides that such exploration shall continue until there is a well or wells on the leased lands capable of commercial production.

After the fifth lease year, a lessee is required to establish that his diligent exploration expenditures exceeded minimum per acre amounts. See 43 CFR 3203.5. In the sixth year of the lease, the minimum amount per acre goes to \$4. In lieu of establishing that diligent exploration expenditures have exceeded the minimum amount, a lessee may pay an additional rental of \$3 per acre or fraction thereof. See id. Finally, the regulation provides that "[f]ailure to either pay the additional rental or complete the minimum required diligent exploration by the end of a lease year shall subject the lease to cancellation." Id.

Appellants were required, prior to the conclusion of the sixth lease year on April 30, 1991, to establish that they had either made diligent exploration expenditures in the amount of \$952 (\$4 per acre x 238 acres) or submitted additional rental in the amount of \$714 (\$3 per acre x 238 acres). They were notified by decision dated September 4, 1990, that they would be required by 43 CFR 3203.5 to establish the performance of diligent exploration expenditures or to pay additional rental for the sixth lease year on or before April 30, 1991. BLM stated that "[f]ailure to meet this requirement within the time allowed may subject your lease to cancellation."

Appellants argue that they complied with 43 CFR 3203.5 by expending \$366,588 in exploration during the first 5 years of the lease and that this amount should be carried forward to the sixth lease year. The regulation does indeed provide that "[a]ll expenditures qualifying as diligent exploration during the first 5 years of a lease * * * shall be credited by the authorized officer against the requirement for successive years." 43 CFR 3203.5 (emphasis added). Consequently, the critical question raised on review concerns whether expenditures claimed by appellants to have been made during the first 5 years of the subject lease qualify as "diligent exploration" within the meaning of the regulation. Id. "Diligent exploration" is defined in the regulation as "postlease field operations, conducted by the operator, on or related to the leased lands." Id. (emphasis added). Such operations "include, but are not limited to, geochemical surveys, heat flow measurement, core drilling or test drilling of test wells." Id.

Purportedly "qualified" expenditures were made by appellants in connection with "exploration and permits" and "geophysical exploration" (SOR at 3). These expenditures are further explained in an attachment to the SOR entitled "F.T.B. Geothermal Drilling and Developing Program South Canyon #1, 1988, Prospectus" [Prospectus]. In the prospectus, Fidelity set forth its "[p]rojection" of expenditures for the first two (as well as later) stages of its planned development of the "South Canyon Creek Thermal Lease Area" (Prospectus at 8). Some of the expenditures have, according to appellants, been made. They state they prepared and submitted a "Multi-Point Surface Operations Plan" on December 1, 1985 (resubmitted April 23, 1986), a "Notice of Intent to Conduct Geothermal Exploration and Drilling Operations" on April 25, 1986, and a "Notice of Intent to Drill and Application for Permit to Drill Geothermal Wells" on April 23, 1986. See SOR at 3-4.

It is BLM's position that the expenditures involved in preparing and submitting a plan of operations, an NOI, and an APD do not qualify as diligent exploration since they do not involve field operations conducted on or related to the leased lands. See Memorandum from the District Manager, Grand Junction District, Colorado, BLM, to the Deputy State Director, Mineral Resources, Colorado, BLM, dated Aug. 9, 1991, at 1, 2.

It is plain that, in order to qualify as diligent exploration under 43 CFR 3203.5, claimed activities must consist of "field operations." On its face, preparation and submission of the plan of operations, NOI, and APD did not involve any on-the-ground activity and would not amount to a qualifying expenditure. Nonetheless, appellants assert that, in connection with the claimed preparatory work, they performed activities in the field, including geologic investigations which consisted of outcrop sampling and analysis, geologic mapping of existing outcropping and faults, soil sampling, surface spring water temperature testing, mapping of existing surface hot springs, mapping of existing old roads, location of known survey boundary corners, and preparation of drill site maps (including a field survey of drill site ties to known section corners). See SOR at 6. They

state that the cost of such activity formed part of the purported \$220,488 cost for "Exploration and Permits," as set forth in the Prospectus at pages 8-9.

Nevertheless, regardless whether the required expenditures were made during the first 5 years of the lease, BLM concluded that appellants failed to timely notify the authorized officer of the fact. Appellants contend that BLM was in fact notified "as part of the Plan of Operations and Notice of Intent to Drill," filed with BLM in December 1985 and April 1986 (SOR at 6). Departmental regulation 43 CFR 3203.5 states that "[t]o qualify as diligent exploration, the results and associated expenditures of operation shall be submitted to the authorized officer in accordance with applicable regulations." (Emphasis added.) In addition, 43 CFR 3264.3 provides that "[f]or exploration expenditures to be considered for qualification as diligent exploration under 43 CFR 3203.5, the operator shall submit to the authorized officer a report of the expenditures no later than 60 days after the end of a lease year if the expenditures are to be credited for that lease year or future lease years." (Emphasis added.)

Departmental regulation 43 CFR 3203.5 provides that, in the absence of payment of additional rental, "[f]ailure to * * * complete the minimum required diligent exploration by the end of a lease year shall subject the lease to cancellation." (Emphasis added.) This means that exploration that does not qualify as "diligent exploration" because it was not timely reported to BLM will not be credited and will subject the lease to cancellation. This is so even if the exploration was completed by the end of the year. That is the case here.

The record shows that appellants submitted no report of expenditures to BLM at any time during the first 5 years of the lease, nor during the sixth lease year (May 1, 1990-April 30, 1991), nor within 60 days thereafter. This is so despite the fact that appellants were notified by the September 1990 BLM decision that they would be required to demonstrate they had made minimum exploration expenditures or should pay an additional rental by April 30, 1991, or face lease cancellation.

Appellants assert, however, that their plan of operations and NOI to drill, submitted in December 1985 and April 1986, contained the necessary notification of claimed diligent exploration expenditures. That is not the case. The NOI to drill notifies BLM of proposed drilling and requests permission to drill at wellsite "No. 1, 45-2" on the leased land. The plan of operations notifies BLM of proposed drilling at a number of sites on the leased land. Both documents set forth in some detail planned drilling operations. Nowhere in either the NOI to drill or the plan of operations is there mention of any exploration already conducted by appellants on the leased land. We cannot conclude that the NOI to drill and plan of operations constitute submission to BLM of the "results and associated expenditures" of field operations, as required by 43 CFR 3203.5. They are merely proposals for future drilling. Nor is it surprising that the NOI and plan of operations make no mention of performance of diligent exploration since

they were submitted in December 1985 and April 1986, before the alleged performance of exploration activities in June 1986 and seismic survey in 1987.

Accordingly, we conclude that appellants have failed to satisfy the requirement of 43 CFR 3203.5 by failing to timely report exploration expenditures. As a result, the lease was subject to cancellation under that regulation. Union Texas Exploration Co., 81 IBLA 153, 157, 91 I.D. 238, 240 (1984).

Before a geothermal resources lease can be cancelled for a violation of Departmental regulations however, section 12 of the Geothermal Steam Act of 1970, 30 U.S.C. § 1011 (1988), and 43 CFR 3244.3 require that the Department afford the lessee notice of the violation and 30 days to correct it. See Union Texas Exploration Co., *supra* at 158, 91 I.D. at 240. No notice was afforded to appellants in the present case. BLM simply cancelled the subject lease by issuing the May 1991 and subsequent October 1991 decisions. Therefore we conclude that because BLM failed to allow appellants the required 30-day notice period before cancellation, lease C-29556 was not properly cancelled for failure to either make minimum exploration expenditures or pay an additional rental in lieu thereof, as required by 43 CFR 3203.5 and we reverse BLM's October 1991 decision.

The proper remedy for this error is to afford appellants the required time to comply. *Id.* Accordingly, we hold that appellants will have 30 days following receipt of this decision to comply with 43 CFR 3203.5. If they fail to do so within 30 days of receipt of this decision, we hold that the subject lease will be deemed cancelled without further notice.

Appellants also seek to raise a question concerning whether BLM should have approved the NOI to drill and APD so that appellants could begin drilling. This question is beyond the scope of this appeal and we therefore do not reach the issue.

Accordingly, 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 reversed.

Franklin D. Arness
Administrative Judge

I concur:

James L. Burski
Administrative Judge