

Editor's note: Reconsideration denied by Order dated Feb. 3, 1994; appealed -- Affirmed Santa Fe Energy Products Co. v. McCutcheon, 90 F. 3rd 409 (10th Cir. 1996). -- see that decision for distirct court history.

SANTA FE ENERGY PRODUCTS CO.

IBLA 90-509

Decided September 28, 1993

Appeal from a decision of the Director, Minerals Management Service, requiring production of sales contracts and exchange agreements for crude oil produced from Federal leases. MMS 87-0342-O&G.

Affirmed.

1. Federal Oil and Gas Royalty Management Act of 1982: Royalties--Oil and Gas Leases: Royalties: Payments

Acting under authority provided by sec. 103 of FOGRMA, MMS properly required production of sales contracts and exchange agreements needed to ascertain whether gross proceeds from sales of Federal crude oil exceeded the value reported by the Federal lessee from a transfer between affiliated corporations that was not an arms-length transaction.

APPEARANCES: Joyce Colson, Esq., Houston, Texas, for Santa Fe Energy Resources, Inc.; Geoffrey Heath, Esq., Office of the Solicitor, Washington D.C., for the Minerals Management Service.

OPINION BY ADMINISTRATIVE JUDGE ARNESS

Santa Fe Energy Products Company (Products Company) and Santa Fe Energy Company (Energy Company) have appealed from a June 7, 1990, decision by the Director, Minerals Management Service (MMS), that required Products Company to produce sales contracts, exchange agreements, ledger entries, and settlement statements for crude oil transactions originating from Federal leases operated by Energy Company in the Midway-Sunset, Sespe, and North Kern Front fields. The June 1990 decision affirmed a September 30, 1988, order from the Royalty Compliance Division, MMS, directed to Products Company, that unless such production were made penalties would be incurred as provided by Departmental regulation.

On October 27, 1988, appellants, both of which are subsidiaries of Santa Fe Natural Resources, Inc., timely sought review of the Compliance Division order by the Director, MMS. Before the Director, appellants argued that royalties were properly paid on the price for crude oil reported in the transfer between Products Company (the Santa Fe marketing entity) and Energy Company (the Santa Fe oil producing entity). Although the transfer

between the two Santa Fe affiliates was admittedly not an arms-length transaction, it is argued that the reported price was the price posted for crude oil in each producing field except for the Kern field, for which field an average posted price was reported for royalty purposes. Arguing in reliance on arguments advanced in an appeal later decided as Amoco Production Co., 123 IBLA 278 (1992), appellants concluded that "[i]f a lessee has received

a posted price that falls within the range of the highest and lowest posted prices listed in appropriate commercial price bulletins, that value will

be accepted by the MMS for royalty valuation purposes" (Statement of Reasons (SOR) at 3). Appellants also contended before the Director that Products Company was not obligated to respond to the demand by MMS for documents because no rule had been promulgated to require production of documents "beyond the point of first sale or royalty computation." Id. at 5. Because Products Company was not signatory to the lease agreement,

it was argued that MMS "has no jurisdiction" that would permit issuance of an order to Products Company to produce records of any kind. Id. at 2.

In their notice of appeal to this Board, appellants restate the objections previously made to the Director and add an objection that regulation 30 CFR 206.102, promulgated to implement the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), does "not apply retroactively to establish the point of royalty computations as the point of sale by the marketing affiliate" (Notice of Appeal at 2). Although they have not filed a

SOR in support of their notice of appeal, MMS has filed an answer to the SOR filed before the Director that treats their pending appeal as though appellants had filed a SOR identical to that filed with the Director that repeated verbatim their arguments before him. We reject the objections made by appellants and affirm the June 1990 decision here under review.

Concerning the central issue on appeal, the question whether product valuation can be ascertained simply by reference to the posted price when the reported transfer on which royalty was paid was not an arms-length transaction, it is the position of the primary auditor of these accounts that audit is not possible without more information concerning actual sales of crude by appellants. The Chief, Special Audits Branch, Comptroller of the State of California, explains that

we are naturally skeptical about the use of the transfer price as the sole basis for establishing the value of the crude oil for federal royalty purposes. Whereas we do not object to considering this transfer price in arriving at the royalty value, we object most emphatically with the prospect of being limited to its use as the sole indicator of value in this instance. At the very least, we need the ability to verify the gross proceeds ultimately received by [appellants]. * * * To limit the auditor's analysis to a consideration of the transfer price alone is unreasonable and is contrary to the objectives of the federal leasing program.

(Comptroller Field Report dated Jan. 17, 1989, at 3, 5).

MMS has endorsed this analysis, and concludes that:

Because of the interlocking relationship[] between [appellants] and the non-arms-length nature of oil sales between these entities, the State's and MMS's position is that the royalty computation point is the point at which oil is sold from the overall corporation (of which [appellants] are individual parts) to a non-interested third party. This requires that the State and MMS have access to the [Products Company] records demanded [by MMS] in order to determine the most reasonable oil royalty value that is consistent with FOGRMA and * * * applicable * * * regulations.

(Memorandum dated Apr. 27, 1989, MMS, RCD, at 2).

Appellants have not denied that the practical effect of their refusal to provide sales documentation to the auditors has been as described by the Comptroller and MMS. As appellants contended in their brief filed with the Director, the "key issue" in their appeal before him was whether Products Company "received the proper price upon which royalties were paid." See SOR at 3. At all times relevant to this appeal, the value of production, for purposes of royalty computation, was "the estimated reasonable value of the product * * * 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, to the price received by the lessee, to posted prices, and to other relevant matters." See 30 CFR 206.103 (1987). This guidance was subject to the proviso, however, that "[u]nder no circumstances shall the value of production of any of said substances for the purposes of computing royalty be deemed to be less than the gross proceeds accruing to the lessee from the sale thereof." *Id.* While appellants have agreed, as between themselves, to report the transfer price between them at the same level as the posted price, it is understood that the purpose of that transfer is to permit the final marketing of the crude oil by Products Company, which is organized for that purpose.

The Director dealt with all the issues raised by appellants in his decision. After finding that the single case relied upon by appellants for the proposition that payment of the posted price relieved them of any further duty to report prices actually received, he determined the case had not been decided as appellants predicted it would be (the case was pending before the Board when the SOR was filed by appellants on October 27, 1988). The Director therefore concluded that "[t]he decision in Amoco does not support the proposition that prices for natural gas liquid products which fall within the range of posted prices must be accepted for royalty value" (Decision at 4). Appellants have not shown that his finding concerning this issue was in error (nor have they argued that it was). It is the responsibility of persons making an appeal to this Board to show how the decision from which appeal is taken, in this case the Director's decision, is in error. See In Re Mill Creek Salvage Timber Sale, 121 IBLA 360, 362 (1991) (and cases cited therein), finding that where there was "a comprehensive decision fully addressing each of the allegations [made by appellant and] appellant has not attempted to show any error in the decision" that we

would summarily affirm. This rule is properly applied here, because of the failure of appellants to directly address the Director's decision here under review.

Citing Transco Exploration & TXP Operating Co., 110 IBLA 282, 286 (1989), appeal filed, No. 90-191-L (Cl. Ct. Mar. 1, 1990), the Director determined that transactions between affiliates such as took place in the instant case "must be examined relative to arm's length transactions between the buyer and non-affiliated third parties" (Decision at 5). Once again, appellants do not directly challenge this finding by the Director, nor have they attempted to show that his reliance on the Transco decision was mistaken. We conclude that he ruled correctly on this issue, in the absence of any argument or showing to the contrary. See In Re Mill Creek Salvage Timber Sale, supra.

Considering the argument that the Secretary's authority to obtain documents required further rulemaking, the Director found that 30 CFR 212.51 (1989) implemented FOGRMA section 103, 30 U.S.C. § 1702(12) (1988) to provide authority for MMS to obtain "information necessary to conduct an audit, and therefore, make a valuation determination." He concluded that the rule provided MMS with authority to obtain records from any affected "person" involved in purchasing or selling oil, and that MMS was not limited to dealing exclusively with the signatory lessee concerned (Decision at 6). He therefore determined that the obligation to report "gross proceeds accruing to the lessee" cannot be avoided by an inter-affiliate transfer made

in contemplation of later sale to third parties. Id. Appellants have shown no error in these findings, and they are affirmed. In Re Mill Creek Salvage Timber Sale, supra. See also Phillips Petroleum Co. v. Lujan, 951 F.2d 257, 260 (10th Cir. 1991), where the court observed, concerning the application of section 103, that "[a]dministrative agencies vested with investigatory power have broad discretion to require the disclosure of information concerning matters within their jurisdiction." (And see Phillips Petroleum Co. v. Lujan, 963 F.2d 1380, 1385 (10th Cir. 1992), where the court followed the approach taken in the earlier Phillips decision that gave broad scope to the authority conferred by FOGRMA section 103). Consistent with the Phillips decisions, this Board has rejected the argument that further rulemaking beyond that already issued was needed to give effect to section 103. See Amoco Production Co., 123 IBLA 278, 285-86 (1992).

Finally, the Director determined that 30 CFR 206.102(b)(1)(i), a rule promulgated after appeal was initiated in this case, and which determined that "the point of royalty computation is the point of sale by the marketing affiliate," was a statement of "longstanding policy" in the Department. He found that such policy was properly applied here. In their notice of appeal appellants have objected that this finding "is incorrect and misleading" and that it is an attempt to conduct rulemaking "in a retroactive manner." These objections are not otherwise explained, however, nor does it appear that the finding made by the Director on this final question was incorrect. Appellants have failed to support their allegation of error, as they must do if they are to prevail on appeal. See Glenville Farms Inc., 122 IBLA 77, 85 (1992).

We therefore conclude that the Director, MMS, correctly determined that Products Company, the marketing affiliate of the Federal lessee, was obliged to produce sales and exchange records of sales of Federal oil to arms-length purchasers pursuant to a demand for production made by MMS. Products Company could not satisfy the request for production by a report that, as between the affiliated corporations, the posted price was used to facilitate transfer of Federal crude oil to the marketing company.

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 affirmed.

Franklin D. Arness
Administrative Judge

I concur:

Gail M. Frazier
Administrative Judge