



## INTERIOR BOARD OF INDIAN APPEALS

A C Building & Supply Company v. Western Regional Director, Bureau of Indian Affairs

51 IBIA 59 (01/08/2010)



## United States Department of the Interior

OFFICE OF HEARINGS AND APPEALS  
INTERIOR BOARD OF INDIAN APPEALS  
801 NORTH QUINCY STREET  
SUITE 300  
ARLINGTON, VA 22203

A C BUILDING & SUPPLY COMPANY, Appellant,	)	Order Vacating Decision and Remanding
	)	
v.	)	Docket No. IBIA 08-40-A
	)	
WESTERN REGIONAL DIRECTOR, BUREAU OF INDIAN AFFAIRS, Appellee.	)	January 8, 2010

A C Building & Supply Company (Appellant) has appealed the January 4, 2008, decision of the Western Regional Director (Regional Director), Bureau of Indian Affairs (BIA), affirming the August 19, 1998, decision of the Salt River Agency (Agency) Superintendent to cancel Business Lease No. B-179 (Lease) between Herman Dean Ray (now deceased), as the Lessor, and Appellant, as the Lessee.<sup>1</sup> The Regional Director did not rely on the grounds stated in the Superintendent's decision. Instead, the Regional Director rested his decision to affirm the Lease cancellation solely on his conclusion that Appellant had breached Article 27 of the Lease, which the Regional Director construed as requiring Appellant's business to generate sufficient revenue to trigger a "percentage of revenue" rent provision in the Lessee.<sup>2</sup> The Regional Director also found that the breach was "incurable" because Appellant's acceptance of severance compensation, when a portion

---

<sup>1</sup> A complete copy of the Lease, which authorizes the use of Ray's trust land within the Salt River Pima-Maricopa Indian Reservation in Maricopa County, Arizona, can be found in the Administrative Record (AR) at Tab XLIV, Ex. 1 (Appellant's Statement of Reasons (SOR)).

<sup>2</sup> Article 27 requires the Lessee to diligently attempt to keep all parts of the leased premises actively used and to conduct the businesses on the premises during regular and customary hours and on all business days in good faith "so that Lessor will at all times receive the maximum income under the percentage rental provisions of this lease." AR, Tab XLIV, Ex. 1, at 29.

of the property was taken by eminent domain, meant that Appellant's business operations "could not be continued after the taking." AR, Tab III, at 5.

Appellant raises two principal issues on appeal. First, it denies that it breached Article 27, asserting that the Lease does not create an absolute obligation on the part of the Lessee to bring in enough revenue to require the payment of percentage rental and that it conducted its operations on the leased premises with diligence and in good faith. Second, Appellant contends that because the Lease required the parties to submit disputes to arbitration, the Regional Director (and the Superintendent) were precluded from taking any action to cancel the Lease until arbitration had been completed.

We conclude that the Regional Director erred in affirming the cancellation of the Lease based on an alleged breach not clearly described prior to his issuance of the decision, and from which Appellant was not given the notice and opportunity to cure required by both the Lease terms and the applicable regulations. We also reject the Regional Director's reasoning in determining that the breach was "incurable," a conclusion which might otherwise alleviate the need to remand to allow Appellant an opportunity to cure. We therefore vacate the Regional Director's decision and remand the matter to BIA for further proceedings. Because we vacate the Lease cancellation, we do not reach the question of whether BIA was required to withhold its cancellation actions until the completion of any properly invoked arbitration proceedings.

### **Background**

BIA has the authority, pursuant to 25 U.S.C. § 416, to approve leases for business purposes on trust or restricted land located within the Salt River Pima-Maricopa Indian Reservation (Reservation), and such leases may include provisions requiring binding arbitration of disputes arising out of those leases. 25 U.S.C. § 416a(c). Once a lease has been approved, BIA has the responsibility to administer and enforce the lease, 25 C.F.R. § 162.108; BIA, however, may enter into a contract or self-governance compact with a tribe or tribal organization under the Indian Self-Determination and Education Assistance Act, 25 U.S.C. § 450f *et seq.*, pursuant to which a tribe may exercise BIA's regulatory administrative responsibilities other than granting, approving, or enforcing leases. 25 C.F.R. § 162.110. BIA has entered into such a compact with the Salt River Pima-Maricopa Indian Community (SRPMIC).

BIA approved the Lease on December 14, 1984. The Lease has a term of 50 years and originally embraced 5.74 acres, more or less, within Allotment No. 598 on the Reservation. The Lease prescribes and limits the uses of the Lease premises in Article 4, which provides:

Lessee shall use the leased premises for the following purposes:

To conduct a general wholesale and retail building supply sales and appliance store dealing in the items set out in Exhibit "B" attached hereto.<sup>[3]</sup>

If the Lessee uses the leased premises for any purpose not set forth above, such use shall constitute grounds for cancellation of the lease.

Article 27 of the Lease sets out additional parameters for the operation of business pursuant to the Lease:

Lessee agrees that at all times during the term of this lease, it will diligently attempt to keep the leased premises and all parts thereof actively used.

All businesses on the leased premises shall be conducted during the regular and customary hours of such businesses and on all business days in good faith, so that Lessor will at all times receive the maximum income under the percentage rental provisions of this lease.

The percentage rental provisions referenced in Article 27 are included in Article 5 of the Lease, which lists three components of the rental for the Lease: (1) a base rent of \$36,000 per year; (2) additional rent if 1½% of the Lessee's gross income exceeds \$36,000; and (3) in the second and succeeding years of the Lease, a percentage of the excess rent paid in the prior year. Lease, Art. 5.

The Lease anticipated the possibility of a taking of some or all of the property by eminent domain. Article 23 defines a "total taking" as a taking of the entire property and a "partial taking" as the taking of less than the whole property. The Lease grants the Lessee the option of treating a partial taking affecting one-quarter or more of the Leased premises as a total taking. Lease, Art. 23.A. In the case of a total taking, the Lease terminates. Lease, Art. 23.B. In the case of a partial taking, the Lease terminates only as to the taken portion, but continues in full force and effect as to the remainder of the leased land. For a partial taking, the base rent is reduced pro rata, but the percentage-based rent trigger (\$36,000) remains unreduced. Lease, Art. 23.C. Article 23.E sets out the allocation of the compensation and damages awarded for both the total and partial taking of the leased land and/or improvements, and provides that the Lessee is entitled to a portion of the award

---

<sup>3</sup> Exhibit B lists various products and supplies directly related to the hardware and building supply business, as well as sporting goods and related items.

equal to “the reasonable cost of alterations, modifications and repairs necessary to place the remaining portion of the leased land in suitable condition for continuance of Lessee’s tenancy.”

The applicable notice-of-default, cure, and cancellation provisions are set out in Article 24 of the Lease. Article 24.B.2 authorizes the Lessor and the Secretary, *inter alia*, to terminate the Lease

[s]hould Lessee default in any payment of monies or fail to post bond as required by the terms of this lease, and if such default shall continue uncured for the period of ten (10) days after written notice thereof by the Secretary<sup>[4]</sup> to Lessee, or should Lessee breach any other covenant of this lease, and if the breach of such other covenant shall continue uncured for a period of sixty (60) days after written notice thereof by the Secretary to Lessee . . . .

BIA has the responsibility to determine whether a lease has been violated, and that determination is guided not only by the lease provisions, but also by the regulations. The regulation applicable at the time the Lease was executed and approved, 25 C.F.R. § 162.14 (1998), provided:

Upon a showing satisfactory to the Secretary that there has been a violation of the lease or the regulations in this part, the lessee shall be served with written notice setting forth in detail the nature of the alleged violation and allowing him ten days from the date of receipt of notice in which to show cause why the lease should not be cancelled. . . . If within the ten-day period, it is determined that the breach may be corrected and the lessee agrees to take the necessary corrective measures, he will be given an opportunity to carry out such measures and shall be given a reasonable time within which to take corrective action to cure the breach. If the lessee fails within such reasonable time to correct the breach or to furnish satisfactory reasons why the lease should not be cancelled, the lessee shall forthwith be notified in writing of the cancellation of the lease . . . . <sup>[5]</sup>

---

<sup>4</sup> The Lease defines “Secretary” as “the Secretary of the Interior or his authorized representative.” Lease, Art. 1.A.

<sup>5</sup> Under the current regulations, which became effective in 2001, when BIA concludes that a lease violation has occurred, it is required to send the lessee (and its sureties) a notice of  
(continued...)

Article 45 (Amendment #1) of the Lease<sup>6</sup> addresses arbitration of Lease disputes between the Lessor and Lessee:

Any controversy which shall arise between the Lessor and the Lessee regarding the rights, duties or liabilities hereunder of either party, except such in which there is a claim for money damages against the Lessor . . . shall be settled by arbitration . . . . Such arbitration shall be conducted, upon the request of either the Lessor or the Lessee . . . .

Lease, Art. 45.<sup>7</sup>

Appellant began operations on the leased premises in 1985. The record reveals that 1987 was the only year during which Appellant had sufficient sales to require the payment of percentage rental (\$5,584).<sup>8</sup> In the early 1990's, the Arizona Department of Transportation (ADOT) condemned approximately half of the leased premises for highway

---

<sup>5</sup>(...continued)

the violation by certified mail, return receipt requested, within 5 days. 25 C.F.R.

§ 162.618(a). The lessee then has 10 business days after receipt of the notice to “(1) [c]ure the violation and notify [BIA] in writing that the violation has been cured; (2) [d]ispute [BIA’s] determination that a violation has occurred and/or explain why [BIA] should not cancel the lease; or (3) [r]equest additional time to cure the violation.” 25 C.F.R.

§ 162.218(b). If a lessee fails to cure the violation within the requisite time period, BIA, in consultation with the landowner, may, *inter alia*, cancel the lease. 25 C.F.R.

§ 162.619(a)(1).

<sup>6</sup> AR, Tab XLII, Ex. 3, and Tab XLIV, Ex. 1.

<sup>7</sup> The Lease also requires the posting of a rental bond in an amount not less than the annual minimum rent (Art. 12), the carrying of public liability insurance (Art. 15) and fire and damage insurance (Art. 42), the filing of semi-annual employment reports documenting compliance with the Lease’s employment preference provision (Art. 39), and the submission of certified audit reports of gross receipts (Art. 43). The Lease also provides for attorney fees: “If action be brought by Lessor or Lessee . . . to enforce performance of any of the covenants and conditions of this lease, the losing party shall pay reasonable attorney’s fees of the prevailing party, to be fixed by the Court as part of the costs in any such action.” Lease, Art. 25.

<sup>8</sup> Appellant contends that a Home Depot opened near the leased premises in the early 1990’s and that this competition negatively impacted its sales. *See* Appellant’s [Amended and Substituted] Opening Brief (Opening Brief) at 34.

purposes.<sup>9</sup> ADOT paid Appellant a total of \$1,056,000 as compensation for the taking. This sum included \$778,100 for Appellant's leasehold interest and \$277,900 in severance damages. *See* AR, Tab XV, Summary Statement of Offer to Purchase, Jan. 16, 1992 (attached to letter from Regional Director to Appellant's Attorney, Dec. 9, 2004). ADOT included severance damages in the payment because its appraiser had concluded that the improvements remaining on the portion of the leased premises not subject to the taking "cannot be used for the same use as in the before state and therefore contribute no value to the remainder. The value of the remainder is therefore land value only." AR, Tab XV, Letter from Robert F. Temple to Steve Hansen, ADOT, Feb. 28, 1990 (attached to letter from Regional Director to Appellant's Attorney, Dec. 9, 2004), at 5. As authorized by Article 23.C. of the Lease, Appellant reduced the basic rent payable under the Lease to \$18,000 per year to reflect the taking of 50% of the leased premises. The record does not reflect whether Appellant reinvested a portion of the compensation from ADOT into its operations on the remainder parcel.

The Lessor died in 1998.

As part of the realty program functions BIA had contracted pursuant to the self-governance compact (AR, Tab XLIV, Ex. 34), SRPMIC began to conduct lease compliance reviews throughout the Reservation in 1998. SRPMIC Amicus Curiae Brief at 3. By letter dated April 21, 1998, SRPMIC notified Appellant that the lease file for the Lease did not contain several required documents relating to proof of a rental performance bond, public liability insurance, an employment report for 1997, fire and damage insurance, and a financial audit report for 1997. AR, Tab XLII, Ex. 43, at 1; *see supra* note 7, describing various Lease requirements. SRPMIC informed Appellant that the Lease required the submission of the listed documents and that failure to comply with the letter within 10 days of receipt of the notice would constitute a breach of the Lease and trigger initiation of default enforcement action. AR, Tab XLII, Ex. 43, at 1. The letter did not assert that Appellant was presently in breach of any Lease provisions, nor did it invoke the notice and "show cause" provisions of the regulations governing lease cancellations. The letter also stated that SRPMIC "had reason to believe that your operations are not consistent with the lease terms," and requested that Appellant submit "an official statement that warrants and represents to [SRPMIC] your existing use of the leased property, your permitted use of the leased property, and a description of your existing business operations." *Id.* at 2. With respect to the latter request, SRPMIC did not identify any provision of the Lease to indicate what lease term or terms were at issue.

---

<sup>9</sup> Appellant chose not to exercise its option under the Lease of treating the partial taking of more than one-quarter of the premises as a total taking.

Appellant responded, explaining the omission of some of the documents and providing or offering to provide the missing documents. *See* AR, Tab XLII, Exs. 51 and 55. In response to the operations issue, Appellant stated that, consistent with the Lease, it continued to use the leased premises as a wholesale and retail building supply and materials business, noting that prior to the ADOT taking, its business had been robust. It added that since the taking, it had been interested in developing the leased premises for other uses and had submitted various proposals to SRPMIC to achieve the highest and best use of the property, including a mixed use project, but that none of its proposals had been accepted.<sup>10</sup>

By letter dated June 22, 1998, SRPMIC advised Appellant that it was in default of the Lease with respect to proper proof and documentation of a valid rental bond, public liability insurance, employment reports, fire and damage insurance, and audit reports for 1992-1996.<sup>11</sup> AR, Tab XLII, Ex. 59. SRPMIC also asserted that Appellant was in default for “insufficient showing of permitted use,” stating:

Pursuant to Article 4 and Article 27, the Lessee is permitted to conduct business specific to the general wholesale and retail sales of building supplies and the sale of appliances in a manner [that] is consistent with normal business operations and maximizes income. [Appellant] has failed to operate [its] business pursuant to these provisions. [Appellant] has no signage, no evidence of gross receipts, no improved facilities, no record with national reporting agencies as to its existence, no employees, no evidence of insurance for a four-year period, paid no more than the minimum rental, and clearly has no consistent normal business operation. The Lessee is in default of Articles 4 and 27.

---

<sup>10</sup> Appellant also questioned both the apportionment of monies ADOT had paid as compensation for the taking — asserting that it should have received more money than it actually did — and SRPMIC’s good faith in refusing to consider the proffered development proposals. AR, Tab XLII, Ex. 55, at 2.

<sup>11</sup> We note that the April 21, 1998, letter mentioned only the need to submit the 1997 audit report and not any earlier reports.

*Id.* at 2.<sup>12</sup> SRPMIC’s letter did not refer to or invoke the regulations governing lease cancellations, nor did it order Appellant to cure the alleged defaults within 60 days or to show cause why the Lease should not be cancelled in the absence of a cure. Instead, relying particularly on Appellant’s receipt of compensation for its leasehold interest and its failure to operate its business to maximize SRPMIC’s interest, SRPMIC asserted that it considered the Lease invalid, but also stated that action “will be taken to terminate [the Lease]” in accordance with Article 24 of the Lease, and that Appellant would be apprised of further details. *Id.* at 3.

By letter dated June 30, 1998, SRPMIC, purportedly on behalf of the Lessor’s estate, requested that BIA terminate the Lease. AR, Tab XLII, Ex. 64.<sup>13</sup> The stated reasons for the requested termination were (1) that Appellant was not a bona fide business because its operations were inconsistent with the intent of the Lease in that it had failed to conduct a normal business operation, to maximize income to the Lessor, and to maintain or improve business conditions even after it had received cash from the taking of its leasehold interests, and (2) that Appellant had not cured its Lease defaults despite being notified of them in the April 21, 1989, letter and provided with an ample cure period.

Appellant responded by denying that SRPMIC had made a sufficient showing of any material Lease violation or any alleged breach that had not long since been waived by Lessor. *See* AR, Tab XLII, Ex. 73, Tab XLII, Ex. 77, and Tab XLII, Ex. 79.<sup>14</sup> Appellant asserted that it was a “bona fide business,” while also asserting that the term did not appear in the Lease, and that, contrary to SRPMIC’s unsupported assertions, it ran a normal

---

<sup>12</sup> SRPMIC also addressed the additional issues Appellant raised, *see supra* note 10, finding that Appellant had waived any claim for additional money as part of its payment agreement with ADOT, had no right to any redevelopment options under the Lease, and needed to apply for a new business lease if it wanted to conduct a business on the leased premises different from the current permitted use. AR, Tab XLII, Ex. 59 at 2.

<sup>13</sup> SRPMIC repeated its request that the Superintendent cancel the Lease on July 17, 1998. AR, Tab XLII, Ex. 76.

<sup>14</sup> Appellant also sent a letter to SRPMIC’s counsel addressing the alleged breaches identified in SRPMIC’s June 22, 1998, letter, asserting, *inter alia*, that it had cured the identified defaults and that it was in full good faith compliance with the Lease’s business use provisions, but that SRPMIC was not acting in good faith in its dealings with Appellant. AR, Tab XLII, Ex. 70. This letter was attached to Appellant’s July 10, 1998, letter to the Superintendent as Ex. A.

business operation, hired and paid employees, and bought and sold building materials and supplies to customers. Any failure to maximize income, Appellant averred, was created by SRPMIC's refusal to allow changes in the use of the property and thus SRPMIC, not Appellant, was responsible for any failure to maximize income to Lessor. Appellant further contended that it had provided sufficient documentation to cure any alleged breach and that SRPMIC had never identified any concerns with those submissions, but instead had raised new issues not identified as issues of concern in the initial April 21, 1998, letter. Appellant also maintained that SRPMIC's letters did not constitute show cause orders as contemplated by 25 C.F.R. § 162.14 (1998) because only the Secretary, not an Indian tribe, can issue such orders, and that SRPMIC had no authority to declare the Lease in default because, under the Lease and regulations, only the Secretary had such authority.

In the meantime, by letter dated June 19, 1998, Appellant notified Lessor's estate, Lessor's widow Mrs. Herman Ray, and SRPMIC that it had filed a demand for arbitration with the American Arbitration Association (AAA) on that day and attached a copy of the demand. AR, Tab XLII, Ex. 57. The arbitration demand sought a declaration that the Lease was in full force and effect; that the Lessee was not in default; that the Lessee was entitled to additional proceeds from the 1990 ADOT condemnation; and the Lessor could not terminate the Lease. By separate letters dated July 8, 1998, counsel representing both Mrs. Ray and SRPMIC moved to dismiss the demand for arbitration, asserting (1) that Mrs. Ray was not a party to the arbitration agreement nor was she a successor in interest to Lessor because Lessor's estate had not yet been probated and his heirs, therefore, were still undetermined (AR, Tab XLII, Ex. 71), and (2) that SRPMIC was not a party to the arbitration agreement or to the Lease (AR, Tab XLII, Ex. 72). Appellant withdrew its arbitration demand in a letter to AAA, dated July 15, 1998, stating

In light of the position of the [SRPMIC] and Mrs. Ray's current status as an undetermined heir of the original lessor, it seems that this matter is best handled by the Department of Indian Affairs in the local office. Consequently, it appears that arbitration will not be going forward, at least at this time. Please take this case off your active calendar.

. . . .

. . . Please send a refund of our \$500 fee . . . .

AR, Tab XLII, Ex. 75. AAA confirmed the withdrawal of the matter by letter dated July 23, 1998. AR, Tab XLII, Ex. 69, third document.

The Superintendent issued her decision cancelling the Lease on August 19, 1998. AR, Tab XLII, Ex. 87. After explaining that SRPMIC had contracted with the United States to assume real estate services programs, including administering and managing the daily operational aspects of approved leases, but that BIA continued to exercise the Secretary's authority to approve and cancel leases, the Superintendent essentially adopted the analysis and conclusions set out in SRPMIC's June 22, 1998, letter. The Superintendent agreed with SRPMIC that Appellant had violated the Lease by failing to produce the required rental bond (Art. 12), to show proof of public liability insurance (Art. 15), to provide SRPMIC with copies of the employment reports (Art. 39), to show proof of fire and damage insurance for 1992-November 1997 (Art. 42), and to timely submit its certified audit report for 1997 or to submit any audit reports for the prior 4 years (Art. 43). The Superintendent also agreed that Appellant had failed to conduct its business in a manner consistent with Articles 4 and 27 of the Lease because it "had no signage, no evidence of gross receipts, no improved facilities, no record with national reporting agencies as to its existence,<sup>[15]</sup> no employees, no evidence of insurance for a four-year period, paid no more than the minimum rental, and clearly no consistent normal business operation." *Id.* at 2-3. The Superintendent therefore cancelled the Lease for violations of Articles 4, 27, 12, 15, and 43.

Appellant appealed the Superintendent's decision to the Regional Director.<sup>16</sup> In addition to maintaining that it had submitted sufficient documentation and evidence to prove that it had either cured the identified defaults or shown that the default did not exist or had been waived by Lessor, Appellant also challenged, *inter alia*, the Superintendent's failure to order the parties to arbitrate the dispute in accordance with the mandatory arbitration provision of the Lease; the adequacy and effectiveness of the notices of alleged lease defaults it had received under the Lease and regulations; and SRPMIC's authority to issue the notices, its role in administering the Lease, and its good faith in dealing with Appellant. *See* AR, Tab XLIV, Appellant's SOR, and AR, Tab XXXIV, Supplement to Appellant's SOR.

---

<sup>15</sup> The Superintendent and SRPMIC based this finding on a May 7, 1998, Dun & Bradstreet report stating that its information indicated that Appellant was no longer active at the leased premises. *See* AR, Tab XLII, Ex. 52.

<sup>16</sup> Appellant also sent a letter to the Superintendent, dated August 31, 1998, pointing out numerous alleged falsehoods and arbitrary and capricious conclusions in the decision, in the hope that she might reconsider her decision. AR, Tab XLII, Ex. 92.

Despite numerous inquiries from both SRPMIC and Appellant as to the status of the appeal, the appeal languished before the Regional Director.<sup>17</sup> The Regional Director's first official reference to the appeal came in a letter to Appellant dated December 9, 2004, discussing the effect of the 1992 agreement between Appellant and ADOT establishing the compensation for the 1992 taking. AR, Tab XV. The Regional Director stated that newly discovered documents revealed that, in addition to receiving compensation for the value of the improvements on the "taking" parcel, Appellant had also received severance damages equal to the full value of the improvements on the remainder parcel, which signified ADOT's determination that damage to the remaining portion of the leased land could not be mitigated and that Appellant's tenancy could not be continued. The Regional Director concluded that, since the remainder parcel was unsuited for continued operations under the Lease, the taking had resulted in a complete frustration of purpose and that the Lease, therefore, should be viewed as having terminated upon completion of the physical taking by ADOT, and that the compensation for the taking should be reallocated with the Lessor receiving additional funds, including \$143,062 in damages from Appellant. He bolstered the conclusion that the Lease had terminated by suggesting that the parties had anticipated that the option to continue the tenancy would be exercised only if the remainder parcel had income-producing potential, asserting that continued operations on the remaining portion of the Lease had proved to be incapable of generating sufficient income to require the payment of the percentage rental "that was intended to ensure that the landowners received annual payments that met/exceeded the market rent over the term of the Lease." *Id.* at 6.<sup>18</sup> While effectively concluding that the Lease had terminated, *id.* at 5, the Regional Director purported to be reviewing the issue only in the hypothetical context and did not issue the letter as a decision, nor did he provide appeal rights.

---

<sup>17</sup> Both Appellant and SRPMIC submitted 25 C.F.R. § 2.8 demands for action to the Regional Director, but neither followed up by appealing his inaction to the Board.

<sup>18</sup> Appellant responded to this letter on February 24, 2005, asserting that it had "continually used the 'remainder' parcel as 'a general wholesale and retail building supply sales and appliance store'" and that it alone had the right to determine the suitability of the remainder for that purpose; that the purpose of the Lease had not been frustrated, despite the fact that no percentage rental was paid; and that any claim for damages was barred by the statute of limitations or by the doctrine of laches. *See* AR, Tab XIII.

The Regional Director issued his decision on the appeal on January 4, 2008. AR, Tab III.<sup>19</sup> Citing 25 C.F.R. § 162.607 (formerly 25 C.F.R. § 162.8 (1998)), which requires rent to be reviewed at 5-year intervals unless the rent is “primarily based” on percentages of income from the leased land, the Regional Director inferred that the Lease’s omission of periodic adjustments for the basic rent had stemmed from the underlying assumptions that (1) additional, percentage rental would be payable throughout the Lease term, and (2) such additional rental would rise throughout the Lease term so that the total rent (basic plus percentage) would approximate the market rental value of the property. He found support for that inference in Article 27’s requirement that the Lessee maintain continuous operations sufficient to ensure that the Lessor receive “maximum income” under the percentage-based rent provisions. Accordingly, he concluded that, “based on this negotiated rental structure, it is undisputable that additional rental was intended to be an essential part of the consideration for the Lease.” AR, Tab III, at 4. In light of the “fundamental nature of the additional rent obligation,” *id.*, the Regional Director focused solely on the alleged breach of Article 27, and eschewed reliance on any other default issue raised in SRPMIC’s April and June, 1998, letters and in the Superintendent’s cancellation decision. *Id.*

The Regional Director determined that Appellant had breached Article 27 of the Lease by failing to generate sufficient income and by being incapable of continuing its Lease operations on the remainder parcel:

[T]he Lease narrowly defines the permitted uses of the leased premises, and does not provide the Lessee with an exemption or right to re-negotiate if those uses become economically infeasible (for any reason). Immediately following buildout (and prior to the taking by ADOT), it is our understanding that the Lease was generating as much as \$5,000/year in additional rent, and — with the (unabated or abated) basic rent remaining flat — the additional rent payable on a per acre basis would normally have been expected to rise with inflation, so long as business operations remained constant. Since the taking by ADOT, it is our understanding that no additional rent has been paid, and in fact the minimal level of gross receipts reported does not even come close to the “break point” level at which additional rent would begin to accrue. As indicated above, the Lease includes

---

<sup>19</sup> He excused the long delay between the filing of the appeal and the issuance of the decision by explaining that his office’s review of the case had led it to believe that the Lease had terminated as a result of the 1992 agreement between Appellant and ADOT, which would render the default issues moot.

an express provision which contemplates “continuous operations” sufficient to generate additional rent, and (based on the inclusion of the additional rent “requirement” in the Lease) does not provide for the adjustment of the basic rent that would otherwise be required under the regulations . . . . As indicated in our December 9, 2004, letter arguing that the Lease terminated at the time of the taking (a position we believe has merit, but which is not incorporated in this decision on the appeal), a factual determination was made at the time of the taking that the “remainder” parcel could not be used for the purposes described in the Lease. Please note that our December 9, 2004, letter is being incorporated in this decision for the sole purpose of establishing factual support for our conclusion that the Article 27 “continuous operations” requirement has been incurably breached (based on the Lessee’s negotiation and acceptance of severance damages, premised on the finding that the Lessee’s operations could not be continued after the taking).

*Id.* at 4-5.

The Regional Director also addressed Appellant’s notice and arbitration arguments. While agreeing that the SRPMIC letters did not provide proper notice of the cure period for non-monetary breaches, he nevertheless found the error to be immaterial because Appellant had disputed whether a breach had, in fact, occurred; 10 years had elapsed without Appellant making any attempt to cure; and Appellant’s responses to the April 21, 1998, letter “clearly” indicated that the April letter contained the requisite specificity with respect to the continuous operations issue. He also dismissed Appellant’s insistence that SRPMIC had no authority to issue the default letters, pointing out that SRPMIC’s self-governance compact established its authority to provide notice of a lease default. With respect to Appellant’s assertion that the dispute had to be settled by arbitration, the Regional Director noted that Appellant’s demand for arbitration of the original default letter had been withdrawn in 1998 and that the Superintendent’s subsequent issuance of the cancellation decision had ended Appellant’s right to demand arbitration, pending resolution of the appeal. The Regional Director therefore affirmed the Superintendent’s August 1998 decision to cancel the Lease. *Id.* at 5.<sup>20</sup>

---

<sup>20</sup> The Regional Director informed Appellant that if it chose to appeal his decision, “any further appeal will be made contingent upon payment in full of all amounts owed under the Lease,” including the payment to the Lessor of the entire \$277,900 in severance damages ADOT had paid to Appellant for the value of the remainder of the Lease. AR, Tab III, at 5. Appellant objected to the requirement to pay the severance monies to the Lessor as a

(continued...)

This appeal followed.

## Discussion

### Standard of Review

The Board exercises de novo review over questions of law, which include interpreting a lease and determining whether BIA has complied with its regulations. *See Smartlowit v. Northwest Regional Director*, 50 IBIA 98, 104 (2009); *State of South Dakota and County of Charles Mix v. Acting Great Plains Regional Director*, 49 IBIA 129, 141 (2009). In addition, we review de novo the sufficiency of evidence to support a BIA decision. *Smartlowit*, 50 IBIA at 104.<sup>21</sup> An appellant, of course, bears the burden of proving that BIA's decision was in error or not supported by substantial evidence. *Id.*; *State of South Dakota and County of Charles Mix*, 49 IBIA at 141.

### Analysis

Appellant raises two principal issues on appeal. First, it denies that it breached Article 27 of the Lease, asserting that the Lease does not create an absolute obligation on the Lessee to bring in enough revenue to require the payment of percentage rental and that it conducted its operations on the leased premises with diligence and in good faith. Second, Appellant contends that the Regional Director (and the Superintendent) erred in failing to refrain from acting until the parties had arbitrated the dispute and that this failure nullifies the cancellation of the Lease. We vacate the cancellation of the Lease and remand the matter to BIA for further proceedings because the Regional Director based the Lease cancellation on an alleged breach not clearly described prior to his issuance of the decision

---

<sup>20</sup>(...continued)

condition of the appeal, but conceded that it remained obligated to pay rent under the Lease. The Regional Director, apparently recognizing that he had no authority to demand payment of the severance monies as a condition for Appellant exercising its appeal rights to the Board, has not pursued the demand. We therefore will not address the matter further.

<sup>21</sup> If BIA has complied with all legal prerequisites relating to the cancellation of a lease, its ultimate decision becomes one involving discretion, and one for which the Board does not substitute its judgment. *See, e.g., Gourneau v. Acting Rocky Mountain Regional Director*, 50 IBIA 33, 43 (2009); *Wallowing Bull-C'Hair v. Rocky Mountain Regional Director*, 49 IBIA 120, 123 (2009). The present case, however, involves the threshold legal issues, and thus does not give rise to our deference to BIA's exercise of discretion.

and without first providing Appellant the notice and opportunity to cure required by both the Lease terms and the applicable regulations. Moreover, we cannot find that the procedural violation was harmless because we do not agree that the record demonstrates an “incurable breach.” Because we vacate and remand the Lease cancellation, we do not reach the question of whether BIA was required to withhold its cancellation actions until the completion of any properly invoked arbitration proceedings.<sup>22</sup>

Appellant strenuously argues that it did not breach the continuous operations (or any other) Lease provision. Appellant also contends that the Regional Director’s decision is procedurally defective because the Regional Director relied on an entirely new rationale for cancelling the Lease and failed to give Appellant proper notice and an opportunity to cure or dispute the alleged breach. We do not reach the merits of the alleged breach because we find that the Regional Director failed to give Appellant the requisite notice and opportunity to either cure or dispute the violation underpinning his cancellation decision before he issued that decision. This failure mandates that his decision be vacated and remanded for compliance with those procedural due process requirements. In addition, on the record before the Board, we cannot agree that Appellant’s alleged breach of Article 27 of the Lease, even if present, has been shown to be “incurable,” such that an opportunity to cure is not required. Finally, we conclude that SRPMIC’s letters did not comply with either the Lease or the regulations, and thus the Superintendent’s decision must be vacated as well.

Article 24 of the Lease and both the current and 1998 versions of the applicable regulation, 25 C.F.R. § 162.618 and 25 C.F.R. § 162.14 (1998), require that the Secretary or his delegate provide a lessee with notice of a violation of a lease provision or regulation and allow the lessee a period of time in which to respond to the notice by agreeing to cure and actually curing the lease breach or to dispute the existence of the default.<sup>23</sup> Failure to give the requisite notice invalidates a cancellation decision. *Chippewa Cree Tribe of the Rocky*

---

<sup>22</sup> Nothing in our decision precludes Appellant from invoking the Lease’s arbitration provision on remand, should such an invocation be appropriate.

<sup>23</sup> As discussed *supra* at 6 and n.5, Article 24 of the Lease grants the lessee 10 days to cure monetary breaches and 60 days to cure non-monetary breaches; 25 C.F.R. § 162.14 (1998) allows the lessee 10 days after receipt of a notice detailing the nature of the alleged violation to show cause why the lease should not be cancelled and an additional reasonable time period to take any admittedly necessary corrective action; and 25 C.F.R. § 162.618 affords a lessee 10 business days to (1) cure the violation, (2) dispute the determination that a violation occurred and/or explain why the lease should not be cancelled, or (3) request additional time to cure the violation.

*Boy's Reservation v. Acting Billings Area Director*, 32 IBIA 251, 261 (1998); *Chissoe v. Acting Muskogee Area Director*, 25 IBIA 146, 152 (1994); *cf. Gourneau*, 50 IBIA at 45 (BIA's violation of appellant's procedural due process rights to notice and an opportunity to cure warranted vacating and remanding Regional Director's decision affirming lease cancellation). The SRPMIC letters did not comply with the requirements of the regulations. In addition, when the Regional Director abandoned the previous rationale for cancelling the Lease and relied on a new breach not clearly identified or explained earlier, he was required to give Appellant notice and an opportunity to cure or dispute that new breach, and his failure to provide that notice vitiates the cancellation decision based on the previously unraised breach. *See Chissoe*, 25 IBIA at 151.

In this case, although the Superintendent found that Appellant was in breach of Article 27 of the Lease and relied on that as a ground for cancelling the Lease, Appellant's failure to pay more than minimum rent was only one of several factors listed, with no clear explanation of its significance or relationship to interpreting Article 27. Neither the Superintendent's decision nor the SRPMIC's instigating letters specifically advised Appellant that the percentage rental provision was intended to be an essential, fundamental part of the consideration for the Lease; that failure to trigger percentage rent, over time, would be construed as a breach; or that Appellant's acceptance of compensation for the partial taking might be considered relevant to determining whether Appellant breached the Lease. Nor did the Regional Director's December 9, 2004, letter addressing the effect of ADOT's payment of severance damages for the remainder portion of the leased premises foreshadow the import that this finding, which was based on an ADOT appraiser's opinion, would have in the cancellation decision.<sup>24</sup> We find these earlier general references to Appellant's failure to generate sufficient income to pay more than the basic rent insufficient to notify Appellant of the crucial role this failure would play in the Regional Director's decision.

Moreover, we find that the Regional Director's conclusion that Appellant's breach of Article 27 of the Lease was "incurable" is not supported by the record presently before the Board, and thus we conclude that the Regional Director's violation of Appellant's procedural rights was not cured by this appeal. The record does not support the Regional Director's conclusion, based on ADOT's appraisal and compensation to Appellant, that a "factual determination" had been made that the remainder parcel "could not be used for the purposes described in the Lease." AR, Tab III, at 5. What ADOT's appraisal said was that

---

<sup>24</sup> Although the Regional Director's December 9, 2004, letter suggested that Appellant's acceptance of compensation might have "terminated" the Lease, he did not suggest it was relevant to determining Appellant's compliance with (or breach of) the Lease.

the “remaining *improvements* on the easterly parcel cannot be used for the same use as in the before state and therefore contribute no value to the remainder.” AR, Tab XV, Letter from Robert F. Temple to Steve Hansen, ADOT, Feb. 28, 1990 (attached to letter from Regional Director to Appellant’s Attorney, Dec. 9, 2004), at 5 (emphasis added). The same appraisal also concluded, however, that “[t]he two remainders make a desirable property.” *Id.* at 4. Additionally, the appraisal had no reason to consider to what extent alterations, modifications, and repairs on the remainder parcel could return Appellant’s business operations to a pre-taking state.

The Regional Director apparently concluded that Appellant’s failure to generate sufficient income to trigger percentage rent, and its acceptance of the ADOT compensation, constituted per se proof that Appellant could not continue its operations on the remainder property and had thus “incurably” breached Article 27 of the Lease. We do not agree that an “incurable” breach has been demonstrated on this record because, in reaching his conclusion, the Regional Director failed to focus on the actual language of Article 27, related Lease provisions, Appellant’s representations, and additional evidence relevant to determining whether Appellant is in breach.

Article 4 of the Lease provides that “Lessee shall use the leased premises . . . [t]o conduct a general wholesale and retail building supply sales and appliance store.” As recently as 2005, Appellant represented to BIA that it had “continuously used the ‘remainder’ parcel as ‘a general wholesale and retail building supply sales and appliance store.’” *See supra* note 18. Although the Superintendent made some conclusory findings, neither the Superintendent nor the Regional Director discussed, in detail, the evidence that would show whether Appellant has operated and continues to operate the site in this manner.<sup>25</sup>

Article 27 of the Lease requires Appellant to “diligently attempt to keep the leased premises and all parts thereof actively used . . . so that the Lessor will at all times receive the maximum income under the percentage rental provisions.” Appellant argues that outside competition significantly impacted its operations and reduced the profitability of its

---

<sup>25</sup> The Lease gives BIA a broad right to inspect Appellant’s books and records, which presumably would show gross receipts during the duration of the Lease for wholesale sales, retail sales, and appliance sales. In its amicus brief, SRPMIC makes various allegations concerning the nature of Appellant’s operations, and submits photographs to support its allegations. Appellant denies SRPMIC’s allegations and submits its own photographs. None of this evidence is appropriate for the Board to consider in deciding the issues on appeal, and we leave it to the Regional Director to consider such evidence on remand.

business. In failing to give Appellant proper notice and an opportunity to show cause why the Lease should not be cancelled, the Regional Director did not allow Appellant to submit evidence to substantiate its contention that the lack of profitability was caused by third-party competition, and to prove that it has diligently attempted to actively use all parts of the property in a way that a reasonable business owner could be expected to do in order to maximize profits from the use of the property for the agreed-upon purpose.<sup>26</sup>

Another Lease provision may also be relevant in evaluating Appellant's compliance with Article 27 of the Lease. Anticipating the possibility of a taking by eminent domain, the parties to the Lease also included a provision expressly allowing Appellant to be compensated for "the reasonable cost of alterations, modifications and repairs necessary to place the remaining portion of the leased land in suitable condition for the continuance of the Lessee's tenancy." Lease, Art. 23. The record does not disclose, nor did either the Superintendent or the Regional Director consider, whether Appellant reinvested proceeds from ADOT's compensation into the remainder parcel in order to continue its operations in a manner that would fulfill the purposes of the Lease, including maximizing percentage rental to the Lessor. Presumably, Appellant's investment (or non-investment) in the remainder parcel could be relevant, when considered with other evidence, to determining Appellant's compliance with Article 27.

Article 27 does not provide the same kind of "bright line" that other provisions in the Lease provide with respect to the existence or nonexistence of a breach (e.g., requirement to submit proof of insurance). Thus, in order to determine whether Appellant is in breach of Article 27, BIA must evaluate the evidence as a whole, including evidence proffered by Appellant, to consider in objective terms the level of Appellant's operations, compare Appellant's activities and business operations with comparable businesses, and consider whether the failure to generate percentage-based rent is attributable to third-party competition, rather than a breach of the Lease. To the extent that the evidence shows that Appellant has made diligent efforts to use the property for the purposes specified in the Lease, but that, notwithstanding those diligent efforts, there are external factors (e.g.,

---

<sup>26</sup> BIA appears to presume that Appellant's active expressed interest in negotiating a new lease to permit a different use of the property necessarily constituted evidence that Appellant was not diligently using the property for its permitted purpose and in a manner that would maximize profits for that permitted use. The two are not mutually exclusive. We do agree with the Regional Director, however, that nothing in the Lease entitles Appellant to renegotiate the purpose for which the property is to be used under the Lease, in contrast to the provision allowing a sublease with the approval of the Lessor and the Secretary, and for which approval may not unreasonably be withheld.

competition from Home Depot) that have prevented Appellant from obtaining gross sales sufficient to trigger percentage-based rent, Appellant's failure to generate such a level of sales does not constitute a breach of Article 27.

Given the Regional Director's violation of Appellant's regulatory and contractual due process rights, we vacate the Regional Director's decision cancelling the Lease and remand the matter to him for further action consistent with this order.<sup>27</sup>

Therefore, pursuant to the authority delegated to the Board of Indian Appeals by the Secretary of the Interior, 43 C.F.R. § 4.1, the Board vacates and remands the Regional Director's decision.

I concur:

\_\_\_\_\_  
// original signed  
Sara B. Greenberg  
Administrative Judge\*

\_\_\_\_\_  
// original signed  
Steven K. Linscheid  
Chief Administrative Judge

\*Interior Board of Land Appeals, sitting by designation.

---

<sup>27</sup> Appellant has asked that we award it attorney's fees pursuant to Article 25 of the Lease. That article provides that the losing party in an action brought, *inter alia*, to enforce performance of any covenants or conditions of the Lease "shall pay reasonable attorney's fees to the prevailing party, to be fixed by the Court as a part of the costs in any such action." AR, Tab XLII, Ex. 1, at 28. The proceeding before the Board was not an action against the Lessor, nor do the Lease provisions concerning costs (and attorney's fees) apply to BIA or SRPMIC, neither of which is a party to the Lease. Accordingly, we deny Appellant's request for attorney's fees.