Editor's note: Reconsideration denied by order dated Feb. 27, 1975

KERR-McGEE CORPORATION

IBLA 70-664 Decided August 15, 1973

Appeal from the royalty and rental provisions of a preference right coal lease (NM-A-0558062 Okla.) offered by decision of the New Mexico State Office, Bureau of Land Management.

Affirmed as modified.

Coal Leases and Permits: Royalties

> Royalty rates for a proposed preference right coal lease will not be reduced when they are in line with rates in issued coal leases in the area and the applicant's claim for more favorable treatment rests on a desire to better its competitive position because of unusual conditions which may increase the costs of mining the coal.

Rules of Practice: Appeals: Hearings

> When no fact question is involved, a plenary, adversary administrative proceeding involving evidence and cross-examination of witnesses is not obligatory.

APPEARANCES: Francis S. Irvine, Esq., Kerr, Davis, Irvine, Burbage & Foster, Oklahoma City, Oklahoma, for the appellant; David C. Branand, Esq., Office of the Solicitor, U.S. Department of the Interior, Washington, D.C., for the Government (U.S. Geological Survey), appellee.

OPINION BY MRS. LEWIS

Kerr-McGee Corporation appeals from the royalty and rental provisions in preference right coal lease NM-A 0558062 (Okla.) offered to it by decision of April 16, 1970, of the New Mexico State Office, Bureau of Land Management, as a reward for discovery of a valuable coal deposit, pursuant to the Acquired Lands Mineral Leasing Act of August 7, 1947, as amended, 30 U.S.C. §§ 351-359 (1970). 1/

1/ Sec. 10, Mineral Leasing Act for Acquired Lands, 30 U.S.C. § 359 (1970), authorizes the Secretary of the Interior to prescribe necessary rules and regulations to implement the Acquired Lands Act, which rules and regulations shall be the same as those prescribed under the Mineral Leasing Act of 1920, as amended, to the extent they are applicable.

The lands involved are located in T. 8 N., Rs. 21 and 22 E., I.M., Haskell County, Oklahoma, and contain 247.70 acres, of which the United States owns only an undivided one-half interest in the mineral estate. The remaining one-half interest is held by Kerr-McGee under a private coal lease.

The appeal is essentially a plea for the Secretary to exercise his discretionary authority and lower the royalty rate to 15 cents per ton and the rental rates to the minimum rates provided in 43 CFR 3503.3-1(b)(1) (1970), in order to bring the lease in line with the provisions of the private leases covering the "East Stigler Block."

Based upon recommendations of the Geological Survey, the offered lease contains the following royalty and rental provisions:

> Royalty: To pay to the lessor a royalty of 20 cents on every ton of 2,000 pounds of coal produced by strip or auger mining methods during the first 10 years of the lease and 22 1/2 cents a ton for the remainder of the first 20-year period. To pay the lessor a royalty of 17 1/2 cents on every ton of 2,000 pounds of coal produced by underground methods during the first 10 years of the lease and 20 cents a ton for the remainder of the first 20-year period.
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> Rental: To pay the lessor annually, in advance, for each acre or fraction thereof covered by this lease, beginning with the date hereof, the following rentals: 25 cents for the first year; 50 cents for the second, third, fourth and fifth years, respectively; and $1 for the sixth and each succeeding year during the continuance of the lease, such rental for any year to be credited against the first royalties as they accrue under the lease during the year for which the rental was paid. Provided, that if by the end of the fifth lease year production royalty for any lease year has not equaled or exceeded $5 an acre, the rental for the sixth and each succeeding year shall be increased from $1 to $5 an acre or fraction of an acre until such time as production royalty for any lease year equals or exceeds the latter amount, whereupon the rental shall revert to $1 an acre.

The private Kerr-McGee lease provides for a royalty of 15 cents per ton of coal, together with the following "Favored Nations Clause":

> If, however, lessees of coal deposits on lands of the United States located in the vicinity of the above described lands are required, pursuant to the * * * [Mineral Leasing Act of 1920] to pay royalties on coal mined therefrom in excess of the royalties in this paragraph provided to be paid lessor, then and in that event, lessee shall pay to lessor royalties on coal equivalent to the royalties on coal provided to be paid by said Act, * * *.

43 CFR 3503.3-1(b)(1) specifies that annual rental per acre for coal leases <u>shall be not less than</u> 25 cents for the first year, <u>not less than</u> 50 cents for the second, third, fourth, and fifth years, and <u>not less than</u> $1 per acre for each and every year thereafter during the continuance of the lease, and that the rental paid for any year shall be credited against the royalties for that year.

Kerr-McGee states in its appeal that the land contained in the offered lease lies within what is commonly referred to as the "East Stigler Block," which is estimated to contain approximately 46.5 million tons of low sulphur, metallurgical grade coal underlying an area of approximately 7,189 acres; that it has under lease a total of 7,039 acres of this area, the only unleased acreage being that covered by the subject offered lease; and that each of the leases which cover the 7,039 acres now under lease provides for a royalty of 15 cents per ton of coal and contains a "Favored Nations Clause" similar to that contained in the Kerr-McGee lease, <u>supra</u>.

The Geological Survey has objected to any revision in the royalty rate in the offered lease, but recommended that the rental section be altered to read as follows:

> (b) <u>Rental</u>. To pay the lessor annually, in advance, for each acre or fraction thereof covered by this lease, beginning with the date hereof, the following rentals: 25 cents for the first year; 50 cents for the second, third, fourth, and fifth years, respectively; $1 for the sixth, seventh, eighth, ninth, and tenth years, respectively; and $1.50 for the eleventh and each succeeding year during the continuance of the lease, such rental for any year to be credited against the first royalties as they accrue under the lease during the year for which the rental was paid.

Kerr-McGee presents two major arguments in support of its contention that the proposed rental and royalty rates are unrealistic and unfair. The first relates to the difficult mining conditions and high costs experienced during initial development work at its Choctaw Mine. The second expresses concern that the proposed rates will trigger the "Favored Nations Clause" in its existing private leases.

It contends that it began its development of the coal deposit in 1967 at its Choctaw Mine located near Stigler, Oklahoma. Two shafts were sunk to a depth of 1,400 feet to the coal seam. The floor of the coal seam was found to consist of a sandy shale, and the roof was found to be comprised of short-jointed, brittle shale with numerous slickensided planes. Upon attempting to enter the coal deposit and extract the same, it was discovered that the slickensided surface of the roof possessed a unique and uncommon characteristic. In particular, it was found that as coal was withdrawn, horizontal pressures developed over, and adjacent to, the extracted area which resulted in a flowing condition within the strata and caused such strata to attempt to fill any extracted area.

As a result of this unique stratigraphic condition, the extraction of coal from the East Stigler Block has proven extremely difficult and has given rise to many unique and yet unsolved problems. Of particular significance in this regard is the inability to provide adequate roof support for safe mining operations economically. All conventional systems of roof support which are adequate under normal mining conditions are totally inadequate for the purposes of safe operation in the East Stigler Block. Through the use of outside consultants, Kerr-McGee has been unable to discover a system of roof support, conventional or otherwise. While Kerr-McGee has, through its own efforts, discovered a potential means of support by which to control the unique "squeezing" condition which exists within the strata, the economics of such means are prohibitive. As a result of the difficulties encountered, Kerr-McGee has suffered an average loss of $42.45 per ton of coal as opposed to an earlier projected loss of $11.97 per ton for the same period of development under normal conditions.

Kerr-McGee also argues that the effect of the higher royalty rate in the offered lease would be to "trigger" the "Favored Nations Clause" in all existing leases and thus increase royalty payments for all leases. As a result, the already economically strained operation of the East Stigler Block would be burdened ever further and the costs of operating the project would rise to such a degree as to make further operations very problematical.

The Geological Survey admits the severe mining conditions encountered at the Choctaw Mine but argues that the high cost of development work does not require a lower royalty. The Survey noted that the excessively high coal extraction costs appellant refers to in the statement of reasons are for the initial development work at the property, and states that any royalty rate now established commits the Government resources for the next 20-year period. It points out, and correctly so, that 30 U.S.C. § 209

(1970), permits a reduction in royalty on a leasehold whenever it is considered necessary in order to promote development, or whenever a lease cannot be successfully operated under the terms provided therein (emphasis supplied); and states that when production begins on the subject lease, and upon a showing as required by 43 CFR 3503.3-2(d) (1972), the Secretary could, in the interest of conservation, reduce the royalty rate for as long a period as such reduced rate may be justified.

The Geological Survey also argues that the "Favored Nations Clauses" in appellant's private leases have already been triggered by an outstanding Federal lease (BLM-017564) in Haskell County issued pursuant to the Mineral Leasing Act of 1920 that requires the lessee to pay for coal produced by underground mining methods a royalty of 17 1/2 cents a ton for the first 10 years and 20 cents a ton for the second 10 years. This lease, which was adjusted to the present rate on January 29, 1968, covers lands within four miles of the subject proposed lease, and the Survey contends that the Department would be remiss in not insisting on obtaining an equivalent rate on the proposed lease with appellant. Also, the Survey states that another lease in Haskell County (BLM-C-021851) is currently pending adjustment of lease terms; and that the recommendation for royalties on that lease is 4 percent of the gross value of the coal produced but not less than 17 1/2 and/or 20 cents per ton, which is the level of all current Geological Survey royalty recommendations in Oklahoma. The lands embraced within lease BLM-C-021851 are within two miles of the subject proposed lease.

After due consideration of the arguments advanced by both parties, this Board finds that a reduction in the royalty rate of the proposed lease would not be in the public interest. Since the proposed lease contains the same royalty rates as all current and new coal leases being issued in Oklahoma, we hold that all lessees should be treated the same in the same geographical area.

In any event, in the case of hardship, appellant may avail itself of the provisions which permit a reduction in royalty whenever a lease cannot be successfully operated under the terms provided therein.

In a somewhat analogous situation, in The Montana Power Company, 72 I.D. 518 (1965), the Department held (syllabus):

> An increase in royalty rates for an additional 20-year extended period of a coal lease is properly provided when it has been determined that these rates are in line with those required of other coal lessees in the area and the lessee's claim for more favorable treatment rests on a desire to better its competitive position with other sources of power and to overcome in part a state tax.

Accordingly, we hold that the royalty rates in the proposed lease may not be altered.

Kerr-McGee has requested a fact-finding hearing in accordance with 43 CFR 4.415 (1972). As the Geological Survey acknowledged the difficult mining conditions encountered, and as Kerr-McGee did not dispute the allegation made by the Survey that the "Favored Nations Clauses" in the private leases have already been triggered by other Federal leases in the area, there is no fact question involved. When no fact question is involved, a plenary, adversary administrative proceeding involving evidence and cross-examination of witnesses is not obligatory. See United States v. Consolidated Mines & Smelting Co., Ltd., 455 F.2d 432, 453 (9th Cir. 1971). The request is, therefore, denied.

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 as modified herein. Upon return of the case file, the New Mexico State Office will alter the rental provisions of the proposed lease and resubmit it to the appellant for execution with no further right of appeal.

Anne Poindexter Lewis, Member

We concur:

Douglas E. Henriques, Member

Joan B. Thompson, Member