

CLASSIC MINING CORP.

IBLA 78-183

Decided October 27, 1978

Appeal from a decision of Wyoming State Office, Bureau of Land Management, denying extension of oil and gas lease, W 8302-A.

Affirmed.

1. Oil and Gas Leases: Drilling--Oil and Gas Leases: Extensions

To qualify for a 2-year extension of an oil and gas lease, pursuant to 43 CFR 3107.2-3, it must be shown that "actual drilling operations" were diligently prosecuted on the last day of the lease term, with reference made to subsequent circumstances. Efforts to secure a large or full-size rig, which are frustrated by unforeseen delays on the part of the contractor supplying the rig so that "actual drilling operations" are not undertaken for more than 60 days do not constitute diligent drilling operations.

2. Oil and Gas Leases: Drilling--Oil and Gas Leases: Extensions

To qualify for a 2-year extension of an oil and gas lease pursuant to 43 CFR 3107.2-3, it must be shown that "actual drilling operations" were diligently prosecuted on the last day of the lease term, with the good faith intent to complete a producing well as demonstrated by all of the circumstances. Where prior approval of the Geological Survey had not been obtained for a change in hole and casing arrangements, drilling that did occur on the last

day of the lease term was not undertaken in good faith and the lease must be held to have expired.

APPEARANCES: Galen J. Ross, President, Classic Mining Corporation, for appellant.

#### OPINION BY ADMINISTRATIVE JUDGE BURSKI

Classic Mining Corporation has appealed from a decision of the Wyoming State Office, Bureau of Land Management (BLM), dated December 30, 1977, denying an extension of its oil and gas lease, W 8302-A, because it was not engaged in diligent drilling operations at the end of its lease term.

Appellant's lease was issued for a 10-year term, with an expiration date of September 30, 1977. Three days prior to the expiration of the lease, appellant submitted an application for a permit to drill (APD) to the Geological Survey in Casper, Wyoming. It sought to drill a 13 and 3/4-inch hole to a depth of 200 feet and to set 10 and 3/4-inch surface casing. This was to be followed by drilling to a depth of 5,000 feet. The Acting District Engineer of the Geological Survey approved the application on September 28, 1977, and enclosed with the approved APD, returned to the appellant, the "Conditions of Approval for Notice to Drill," which notified appellant that it must not deviate from the approved plan without the "prior approval of this office."

Appellant commenced drilling on September 29, 1977. On that date, appellant drilled a 24-inch hole to a depth of 30 feet and set 18-inch surface casing. On November 18, 1977, a Geological Survey technician inspected the site and confirmed that 18-inch surface casing had been used.

Appellant continued drilling, through September 30, 1977, with a second rig to a depth of 200 feet. It ceased drilling on October 3, 1977. The second rig was moved off the site.

On October 14, 1977, appellant contracted with Superior Drilling of Denver, Colorado, for a larger rig to be brought onto the site, presumably to continue the drilling to a depth of 5,000 feet. Appellant paid \$25,000 as a deposit, which deposit subsequently became nonrefundable.

By letter dated November 10, 1977, appellant was notified that it must resume drilling by December 2, 1977 (60 days from "the date the (second) smaller rig was moved off" the site) "or diligent drilling operations will be considered to have ceased." Appellant requested an extension of time. It had been notified by Superior that due to "unforeseen delays" Superior would be unable to make its rig available

any earlier than "sometime during the first ten days of December, 1977." Appellant's request was denied by the District Engineer.

By memorandum of December 19, 1977, the BLM State Office in Cheyenne, Wyoming, was advised by the District Engineer that diligent drilling operations had not been "continued" and that the lease was "considered to have terminated effective September 30, 1977." The BLM State Office subsequently held that appellant's lease had terminated on September 30, 1977. Appellant finally received the Superior rig on January 4, 1978.

[1] The pertinent regulation, 43 CFR 3107.2-3, provides that: "Any lease on which actual drilling operations \* \* \* were commenced prior to the end of its primary term and are being diligently prosecuted at that time shall be extended for 2 years \* \* \*." <sup>1/</sup> (Emphasis added.)

In his statement of reasons for appeal, appellant contends that: "Congress was quite precise that if one is drilling as of date of expiration one is entitled to a two-year extension. Classic Mining was drilling as of midnight and is entitled to such an extension." (Appellant's Brief at 2.) (Emphasis added.)

The regulation is not susceptible to so narrow a construction. It requires not only that drilling operations be conducted on the last day of the least term but that they be "diligently prosecuted at that time." 43 CFR 3107.2-3.

"Diligent operations" are defined as: "Actual drilling operations \* \* \* conducted in such a way as to be an effort which one seriously looking for oil or gas could be expected to make \* \* \*." (Emphasis added.) 43 CFR 3107.2-2. As we held in D. L. Cook, 20 IBLA 315, 317 (1975): "[T]he bona fide intent of the lessee and the diligence with which he carries out that intent must be tested \* \* \* not only by the activity in progress at midnight on the last day, but by what transpires subsequently." (Emphasis added.)

If there was only one critical moment, the lessee who drilled solely to obtain the extension might be able to sustain the appearance of diligence at that time and would be granted an extension. This would thwart the purpose of the regulation. See Thelma M. Holbrook, 75 I.D. 329 (1968). Thus, drilling on the last day of the lease term must be followed "by a showing that the operation was thereafter expeditiously carried forward." (Emphasis added.) D. L. Cook, *supra* at 317.

Along these lines, the Geological Survey Conservation Division Manual provides that, after a "small rig (is used) to spud and set

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<sup>1/</sup> This regulation implements section 226(e) of the Mineral Leasing Act Revision of 1960, 30 U.S.C. § 226(e).

surface pipe, prior to the lease expiration date" (emphasis added), a "large or full-size rig" must be put into operation on the site "normally within thirty days" of that date. Conservation Division Manual 645.6A.3C(2). The Oil and Gas Supervisor for the Northern Rocky Mountain Area reports that "[s]ince 'normally' is not definable, this office has consistently permitted up to a maximum of 60 days if warranted." (Memorandum to Chief, Conservation Division dated June 22, 1978.) The District Engineer gave appellant the full 60 days and held that it ran from the date the smaller rig was moved off the site. <sup>2/</sup>

Appellant alleges that it sought to abide by the District Engineer's interpretation of the Manual provision. When it believed that it could not comply, it requested an extension of time. This was denied. Yet, appellant made no further effort to resume drilling until January 4, 1978, 33 days after the 60-day time limit had expired.

This total failure to engage in "actual drilling operations," as interpreted by the Geological Survey, which exceeded the 60-day time limit fixed by Survey, cannot be considered to be diligent drilling operations within the meaning of the regulation. Appellant did not earn a 2-year extension on its lease, and the lease must be held to

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<sup>2/</sup> There is a certain amount of confusion on this point engendered by appellant's citation of the Conservation Division Manual provision found at 645.6A.3A. The cited provision states:

"Generally, operations should be reasonably continuous with a minimum of delay between cessation of one operation and commencement of another. Reasonable delays may be approved by the District Engineer when warranted. However, delays of more than sixty days between cessation of one operation and commencement of another should normally not be considered as diligent." (Emphasis supplied.)

Appellant places great reliance on the use of the word "normally" in the Conservation Division guideline. The difficulty with appellant's position is that this guideline refers to "diligent operations to restore paying production," under the provisions of 30 U.S.C. § 226(f) (1970), relating to leases which have become subject to termination because of a cessation of production.

The provision which permits an extension for diligent drilling operations at the end of the lease term is found at 30 U.S.C. § 226(e). There are essential differences between these two provisions. Thus, under section 226(f) reworking operations, if commenced within 60 days, will serve to extend the lease. Such reworking operations, however, will not extend a lease under section 226(e). Cf. Morton Oil Company, A-27392 (November 26, 1956).

The provision of the Manual cited in the text is clearly applicable to the situation presented by the instant appeal. By its terms, it allows a period of 30 days, "normally," in which to replace a small rig with a large or full-sized rig. Herein, appellant was actually afforded 60 days. The provision cited by appellant is inapposite.

have terminated as of the end of its primary term. Accordingly, the State Office properly denied the lease extension. See Charles M. Goad, 25 IBLA 130 (1976).

Appellant contends that:

The shortage of rigs during the latter part of last year, the efforts made by Classic Mining to secure a rig (with cash), and the problems that the contracted rig had on prior commitments, all show that Classic Mining was doing everything within its power to diligently pursue drilling operations.

Appellant's efforts to secure a rig cannot be considered to be "actual drilling operations" within the meaning of the regulation, even if diligently pursued. 43 CFR 3107.2-3; Burton W. Hancock, 31 IBLA 18 (1977). Furthermore, unforeseen delays in the arrival of the rig will not excuse appellant's failure to engage in "actual drilling operations." D. L. Cook, supra (breach of contract by first contractor); Burton W. Hancock, supra (inclement weather, personnel shortages and equipment failures).

Moreover, we would note that despite the fact that it was clear to appellant from the outset that it would need a larger rig, it did not even contract for one until October 14, 1977, 11 days after the smaller rig was moved off-site. The letter of October 24, 1977, from the rig contractor states: "We are now drilling on the Integrity Bicentennial #1, and we look forward to drilling for you following the completion of this well and the Supron well immediately thereafter." (Emphasis supplied.)

It is impossible to discern from the total factual milieu surrounding the instant appeal the diligence which the regulations presuppose for the grant of a 2-year extension. 3/

[2] Appellant's failure to obtain prior approval for the change in its approved hole and casing arrangements is itself a sufficient basis upon which to deny appellant's lease extension.

"Diligent drilling operations are defined as an effort made in good faith that one seriously interested in looking for oil and gas

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3/ Given this factual background, we find it difficult to give any credence to the statement of the rig contractor, contained in a letter dated November 21, 1977, that "we recognize that you had anticipated our being able to move our Rig No. 6 to your Government Classic #32-1 in time to commence drilling by September 30, 1977." Appellant hardly could have had any rational basis for its "anticipation" that the rig would be in place by September 30, 1977, when it had not even entered into an agreement for the rig until October 14, 1977.

\*\*\* would be expected to make." (Emphasis added.) Daisy E. Hook, 21 IBLA 147, 148 (1975). The willful failure to comply with clear regulatory obligations, when engaged in drilling operations, is evidence that such operations were undertaken principally to obtain an extension of the lease and not undertaken in good faith. In such circumstances, a lease extension must be denied. Daisy E. Hook, *supra*.

The pertinent regulation, 30 CFR 211.58(b), provides that: "Where unexpected conditions necessitate any change in the plans of proposed work already approved, complete details of the changes must be submitted to the supervisor and approval thereof obtained before the work is undertaken." (Emphasis added.) This requirement was set out in the "Conditions of Approval for Notice to Drill" sent to appellant with its approved application. Yet, appellant proceeded to change its hole and casing arrangements without the prior approval of the district office of the Geological Survey.

Appellant's failure to comply with the regulation clearly shows that its drilling operations were undertaken principally to obtain an extension of its lease and not undertaken in good faith. For this additional reason, the State Office properly denied the lease extension.

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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James L. Burski  
Administrative Judge

I concur.

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Edward W. Stuebing  
Administrative Judge

ADMINISTRATIVE JUDGE GOSS DISSENTING:

That substantial drilling operations have been shown despite deviations from approved plans is indicated by the October 7, 1977, Memorandum of the Geological Survey District Engineer, Casper, Wyoming, addressed to Manager, U.S. Land Office, Casper, Wyoming. The District Engineer stated:

Classic Mining Corporation well No. 32-1, \* \* \* commenced drilling operations September 30, 1977, and continued drilling operations thereafter.

In our opinion, the subject lease may be entitled to a two year extension if diligent operations are continued pursuant to 43 CFR 3107.2.

It would appear that appellant's drilling would have been considered sufficient were it not for an interruption after reaching the 200-foot depth, while appellant waited for the larger rig to be furnished under its contract with Superior Drilling, Kenai Drilling Limited. The interruption raised questions as to whether appellant's drilling operations were nominal, rather than actual diligent operations under 43 CFR 3107.2-2 and 3107.2-3. Those regulations provide:

§ 3107.2-2 Diligent operations.

Actual drilling operations must be conducted in such a way as to be an effort which one seriously looking for oil or gas could be expected to make in that particular area, given existing knowledge of geologic and other pertinent facts.

§ 3107.2-3 Period of extension.

Any lease on which actual drilling operations, or for which under an approved cooperative or unit plan of development or operation, actual drilling operations were commenced prior to the end of its primary term and are being diligently prosecuted at that time, shall be extended for 2 years and so long thereafter as oil or gas is produced in paying quantities. [Emphasis supplied.]

I feel that appellant has shown substantial compliance with statute and regulation. Assuming that appellant commenced what would normally be deemed substantial drilling operations, the issue is whether such operations were "actual" under 43 CFR 3107.2-2. Was there an informed, serious, and diligent effort as of the end of the lease primary term? Subsequent actions are only relevant as an indication of the meaning of appellant's actions on September 30, 1977.

Appellant claims expenditures of \$5,000 for spud in and location costs plus a \$25,000 non-refundable payment under its contract with

Superior Drilling. In a letter of November 21, 1977, to appellant, Superior asserts an understanding that Superior was to commence drilling by September 30, 1977.

I submit that appellant has alleged sufficient informed, serious, and diligent drilling operations as to constitute actual drilling operations on September 30, 1977. A substantial property right is involved. If there is any doubt as to the veracity of the allegations, then a hearing should be ordered. 43 CFR 4.415. Otherwise, appellant should be granted the statutory extension.

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Joseph W. Goss  
Administrative Judge

