

Editor's note: appealed - aff'd sub nom. Geosearch, Inc. v. Watt, Civ.No. C82-0379 (D. Wyo.), aff'd in part, rev'd, in part, No. 83-1408 (10th Cir. Nov. 7, 1983); 721 F.2d 694, cert. denied, S. Ct. No. 83-1480 (May 14, 1984); 104 S.Ct. 2347; 466 US 972

DAVID A. REECE ET AL.

IBLA 80-838

Decided June 21, 1982

Appeal from decision of the Wyoming State Office, sustaining in part protest against the issuance of oil and gas lease W 59243, dismissing bona fide purchaser from the proceeding, declaring overriding royalties null and void, and rejecting drawing entry cards drawn with second and third priority.

Affirmed as modified.

1. Oil and Gas Leases: Applications: Generally -- Oil and Gas Leases: Applications: Sole Party in Interest -- Oil and Gas Leases: First-Qualified Applicant

When an individual files an oil and gas lease offer through a leasing service under an agreement whereby the leasing service is authorized to act as the sole and exclusive agent to negotiate for sublease, assignment, or sale of any rights obtained by the offeror; where the offeror is required to pay the leasing service according to a set schedule, even if the offeror negotiates the sale; and where such agency to negotiate is to be valid for 5 years, the leasing service has an apparent right to share in the proceeds or any sale of the lease or any interest therein, and in any payments of overriding royalties retained. Such an agreement creates for the leasing service an "interest" in the lease as that term is defined in 43 CFR 3100.0-5(b).

2. Estoppel -- Oil and Gas Leases: Applications: Generally
The requirement that an oil and gas lease offeror disclose all parties in interest is not ambiguous, and the rejection of offers filed prior to this Board's decision in Lola I. Doe, 31 IBLA 394 (1977),

for violation of the regulations requiring disclosure of such interests and prohibiting multiple filings did not constitute a retrospective application of a new Departmental interpretation of the regulations.

3. Oil and Gas Leases: Assignments or Transfers -- Oil and Gas Leases: Bona Fide Purchaser -- Words and Phrases

"Bona fide purchaser." A bona fide purchaser of an interest in a Federal oil and gas lease must have acquired his interest in good faith, for valuable consideration, and without notice of violation of Departmental regulations. Assignees are deemed to have constructive knowledge of all BLM records pertaining to the lease at the time of assignment.

4. Oil and Gas Leases: Bona Fide Purchaser

A party which purchased an oil and gas lease is a bona fide purchaser of this interest where, throughout the time it agreed to purchase the lease, paid fair value, and formally requested approval of the assignment, BLM's records indicated that BLM had resolved a question about the validity of the underlying offer in favor of the offeror and had proceeded to issue the lease to him, and where there was no formal protest against the lease pending, provided that the purchaser of the lease pending had no actual knowledge of any defect in the underlying offer.

APPEARANCES: David B. Kern, Esq., Milwaukee, Wisconsin, for appellants David A. Reece, Sr., and Resource Service Company; Melvin Leslie, Esq., Salt Lake City, Utah, for Robert D. Gittler and Geosearch, Inc.; Harold J. Baer, Jr., Esq., Denver, Colorado, for the Bureau of Land Management.

OPINION BY ADMINISTRATIVE JUDGE BURSKI

This appeal represents the second time that circumstances surrounding the issuance of oil and gas lease W 59243 are disputed before the Board. In the initial case, Geosearch, Inc., 41 IBLA 291 (1979), appellant Geosearch argued that this lease, among others, had been improperly issued to a first priority offeror who should have been disqualified. Geosearch purchased such interests in the various leases as were held by second and third priority offerors, including Robert D. Gittler, the second drawee for the lease on appeal here. Geosearch protested the validity of the leases, arguing that the Resource Service Company, Inc. (RSC) had an undisclosed interest in each

offer afforded first priority. Each first priority offeror, including David A. Reece, Sr., the first priority offeror here, had entered into a service agreement with RSC, a leasing service. The Wyoming State Office of the Bureau of Land Management (BLM) had denied Geosearch's protests, noting that since the leases had already issued (except one not relevant here) and most had been assigned, "we do not believe the number 2 drawees of these simultaneous oil and gas drawings have an interest to assign to Geosearch, Inc." Geosearch, Inc., *supra* at 292. BLM, in this original decision, did not determine whether the underlying offers in the leases were actually defective. Geosearch appealed.

The Board noted in Geosearch, Inc., *supra*, that because BLM had neither returned the drawing entry cards of the second and third priority offerors nor notified the offerors that their offers were rejected, the offers remained viable. The Board agreed that any bona fide purchasers would be protected under 30 U.S.C. § 184(h)(2) (1976). The Board also noted the possibility that some assignees might not be bona fide purchasers, pointing out that most assignees had not even asserted bona fide purchaser status. Accordingly, the Board vacated BLM's original decision and instructed the State Office to join the assignees to the protest proceeding and to consider whether the underlying offers were defective and, if so, to ascertain the bona fides of any assignee. The Board indicated also that where an assignee asserted bona fide purchaser status, Geosearch would have the burden of establishing the contrary by prima facie evidence.

On remand, BLM found in a decision dated July 25, 1980, that David A. Reece, Sr., the first drawee for parcel WY 55, listed April 18, 1977, filed his simultaneous oil and gas lease offer pursuant to an agreement which gave RSC an interest in the offer (as interest is defined in 43 CFR 3100.0-5(b)) which should have been disclosed pursuant to 43 CFR 3102.7 (1979), citing *inter alia*, Frederick W. Lowey, 40 IBLA 381 (1979). ^{1/} Under this agreement RSC's interest consisted of an exclusive right to participate in the proceeds from any sale or assignment of the lease for a 5-year period after lease issuance. BLM determined that the first drawee's offer violated the party in interest disclosure requirements. BLM held further that a purported disclaimer of interest ^{2/} in any leases RSC might receive was ineffective to avoid the regulatory violation. Once BLM had determined that the underlying offer was defective, BLM examined the status of the assignee.

The decision indicated that lease W 59243 issued November 7, 1977, effective December 1, 1977. Assignment of 100 percent record interest to Diamond Shamrock Corporation (Diamond) was filed with BLM on January 30, 1978. By this assignment, executed December 2, 1977, Reece reserved a 5 percent overriding royalty interest. BLM approved the assignment on March 2, 1978, effective February 1, 1978. On July 17, 1978, RSC filed with BLM an assignment to itself of part of the 5 percent reserved override. Then on October 3, 1978, Geosearch filed the protest which this Board considered in Geosearch, *supra*.

^{1/} The Board's decision in Frederick W. Lowey, *supra*, was subsequently affirmed in Lowey v. Watt, 517 F. Supp. 137 (D.D.C. 1981).

^{2/} The purported waiver was submitted to BLM on Jan. 13, 1977, but it did not appear in this case file until Oct. 6, 1980.

BLM dismissed Diamond from the proceedings, holding that at the time of the assignment nothing in the lease records would have put Diamond on notice of a defect in the underlying offer. BLM stated that "[t]here was no mention in this file of the [Lola I. Doe, supra], decision until eight months after the assignment to Diamond," and that "no copy or quotation from the RSC service agreement was filed in this case until November 13, 1979." Therefore, BLM determined that Diamond had proven its bona fides under the standards outlined in Southwestern Petroleum v. Udall, 361 F.2d 650, 657 (10th Cir. 1966) and in Winkler v. Andrus, 614 F.2d 707, 713 (10th Cir. 1980). BLM also stated that Geosearch had not offered any facts to challenge Diamond's status as a bona fide purchaser. BLM therefore dismissed Diamond rather than order a hearing. BLM declared the interests of Reece and RSC void and rejected the offers of the unsuccessful drawees.

[1] Reece, RSC, Geosearch, and Robert D. Gittler, as second drawee, all appeal BLM's decision to this Board. RSC and Reece continue to dispute the determination that their leasing service agreement gave RSC an "interest" in this first drawn offer, as this Board held in Lola I. Doe, supra, and Sidney Schreter, 32 IBLA 148 (1977). However, their primary contention on appeal is that the Doe decision should not be retroactively applied. RSC and Reece submit the January 13, 1977, waiver/disclaimer as evidence of their good faith.

[2] This Board has considered and rejected RSC's retrospective argument in a number of cases. See, e.g., James Koch, 61 IBLA 235 (1982); Inexco Oil Co., 54 IBLA 260 (1981); Home Petroleum Corp., 54 IBLA 194, 204, 88 I.D. 479, 484 (1981), aff'd, Geosearch v. Watt, Civ. No. C81-0208 (D. Wyo. filed Aug. 7, 1981); D. R. Weedon, Jr., 51 IBLA 378 (1980), appeal dismissed, Weedon v. Watt, Civ. No. 81-749 (D.D.C. Oct. 9, 1981). As we noted in D. R. Weedon, Jr., supra, both RSC and its clients participated in the creation of an illegal interest -- an exclusive right to participate in a precise share of proceeds from sale or assignments of a lease -- so neither had the status of "innocent offerors." We adhere to our prior holding. Reece failed to disclose RSC's "interest" in his offer, as required by 43 CFR 3102.7, and his offer must be rejected for that reason alone. In addition, to the extent that other RSC clients filed in the same drawing under this same arrangement, RSC thereby increased its chances of success in the drawing in violation of 43 CFR 3112.5-2, and therefore all such offers should be rejected.

We have also noted in many cases that the purported waiver/disclaimer was ineffective as it was a unilateral action unsupported by consideration and was not communicated to the other parties. See, e.g., Frederick W. Lowey, supra; Alfred L. Easterday, 34 IBLA 195 (1978).

On appeal, Geosearch and Gittler argue primarily that Diamond could not have been a bona fide purchaser, since, according to Geosearch, it knew or should have known that RSC had prohibited interests in the first drawn offers. In addition, they maintain that such interests as are canceled should not be put up for sale by competitive bid but rather should be issued to them as the next qualified offeror.

[3] As this Board has noted, the interest in a Federal oil and gas lease held by a bona fide purchaser is not subject to cancellation even though the lease offer filed by a predecessor in title was defective and the lease was

subject to cancellation while title was held by the predecessor. 30 U.S.C. § 184(h)(2) (1976); 43 CFR 3102.1-2. A bona fide purchaser must have acquired his interest in good faith, for valuable consideration, and without notice of violation of Departmental regulations. Winkler v. Andrus, 614 F.2d 707, 711 (10th Cir. 1980); Southwestern Petroleum Corp. v. Udall, 361 F.2d 650, 656 (10th Cir. 1966). Assignees who seek to qualify as bona fide purchasers are deemed to have constructive knowledge of all BLM records pertaining to the lease at the time of assignment. Winkler v. Andrus, supra at 713; O'Kane v. Walker, 561 F.2d 207 (10th Cir. 1977).

Geosearch alleges that the assignee, Diamond, had actual or constructive knowledge of the service agreement between the first drawn offeror and RSC which created undisclosed interests in the lease offers and, therefore, that Diamond cannot qualify as a bona fide purchaser. Geosearch contends that previous dealings with RSC and with other clients of RSC should have alerted Diamond to a pattern of operations which, in turn, should have alerted it to the probability of agreements between RSC and the first drawn offerors that would violate Federal oil and gas leasing regulations.

We have noted in the past that the mere fact that an offeror was a client of RSC did not establish that the arrangement which we found violative of the regulations in Lola I. Doe, supra, had been entered into in every case. See, e.g., Wilbur G. Desens, 54 IBLA 271, 278 (1981); Inexco Oil Co., supra at 267. Geosearch's suppositions to the contrary are insufficient to establish prima facie that Diamond was not a bona fide purchaser. See Geosearch v. Andrus, 508 F. Supp. 839, 846 (D. Wyo. 1981). Therefore, in order to determine whether Diamond was on notice of a defect in Reece's offer, it is necessary to examine the BLM record for this lease at the time of assignment.

As we have pointed out in the past, while the general rule is that the relevant date to determine bona fides is the date that the consideration for the assignment was paid, Winkler v. Andrus, 614 F.2d at 712, citing 77 Am. Jur. 2d, Vendor & Purchaser § 706 (1975), the Tenth Circuit indicated in Winkler that the critical time was when the agreement was formed. It is not clear from the record exactly when Diamond tendered consideration for the lease. However, in this case it is immaterial whether consideration was tendered when Reece executed the assignment document or later. The case record remained the same.

The record reveals that BLM received two submissions prior to the issuance of this lease: One, a protest, from Donald D. Bruce, filed May 16, 1977, and another, in the nature of an inquiry, from Mrs. D. Belknap, filed May 18, 1977. ^{3/} The Bruce protest did not elaborate on its general assertion that the lease application directly conflicted with BLM regulations governing simultaneous filing. BLM dismissed this protest on May 19, 1977, stating that the protestant had offered no proof of his assertions. Bruce did not exercise his right of appeal.

^{3/} Belknap did not refer to her inquiry as a "protest" and it is clear from the case file that the State Office did not treat it as such.

However, the Belknap inquiry was more detailed. Belknap inquired as to the issuance of six oil and gas leases, including this one, to individuals, including Reece, using RSC's post office boxes for their addresses. She stated:

In the past, the customers of Resource Service Company were subject to a binding service agreement whereby Resource Service Company would automatically have an interest in any lease issued to one of their customers because of an exclusive 5 year sales right clause in the agreement.

Apparently on January 13, 1977, there was an affidavit filed with the Bureau of Land Management in Cheyenne, Wyoming which seeks to remove the objectionable portions of the contract obligations.

My inquiry into this matter takes the following form:

1. In order to amend their original contract with Resource Service Company, must each of the persons named above have signed an amendment between themselves and Resource Service Company acknowledging any changes or deletions to their original contract?
2. If no amendment was issued to or signed by these customers of Resource Service Company, does that imply that their bid was filed while the original contract was still in effect in its original form?

* * * * *

On June 29, 1977, BLM responded:

* * * You are correct in stating that the post office boxes you list are those used by Mr. Engle dba Resource Service Company. The six pending oil and gas leases have been suspended and will not be issued until we receive the decision of the Interior Board of Land Appeals concerning the appeals from our decision rejecting several lease offers filed through the Resource Service Company. We expect that decision any day now.

The affidavit submitted by Mr. Engle is designed to allow Resource Service Company to continue using its old forms until the IBLA decision is made and until it becomes clear that new forms will be required. As you point out, a modification to a contract requires the consent of both parties. In Mr. Engle's case we are merely preventing him from exercising the exclusive agency set out in the agreement form unless he notifies his winners that they are free to enter into any new contract they wish.

For now we are waiting on the IBLA decision. If we are sustained in our view that the prior executed exclusive sales agency is against the regulations unless disclosed, and that it provides

sufficient interest in an offer as to cause multiple filings problems, we will check to see that Mr. Engle has notified his winners and renounced the objectionable elements of the existing agreements. We are not now requiring the filing of any additional statements of interest or evidence of amended contracts in advance of the drawing from each of the clients. We are regarding the objectionable portions of the service agreement as a nullity because the powers given thereby will not be exercised if our view is sustained. We have various means of insuring that Mr. Engle abides by his agreement with us.

This response indicated that BLM had strong reservations about the validity of these offers, including that of Reece. BLM emphasized that it was waiting for an IBLA determination. The response raised a serious question as to a potential multiple filings problem but did not resolve that question.

[4] In Ervin Staacke, 62 IBLA 278 (1982), we noted that pendency of a protest that a service agreement had created a prohibited interest in RSC, together with a copy of the agreement which did create such a prohibited interest, placed in the record by RSC "was sufficient to put individuals on notice of the deficiencies of [the applicant's] offer had they had actual knowledge thereof." Id. at 285. In that case, the protest had been filed after not only lease issuance but after the subsequent filing with BLM of an assignment from the applicant to the assignee. We held, consistent with the Tenth Circuit's opinion in Winkler v. Andrus, supra, that bona fides was to be judged from the date that the assignment was made, and that there was nothing in the record on that date which would have put the assignee on either actual or constructive notice of any deficiencies.

In the instant case, however, the critical documents were filed prior to lease issuance. Despite the detailed inquiry of Belknap, the State Office subsequently issued the lease. A similar situation arose in Jack Zuckerman, 56 IBLA 193 (1981). Therein, we noted that "[v]iewed objectively against this background, BLM's proceeding to issue the lease to Zuckerman was a signal that it had decided that Zuckerman was entitled to a lease because any and all doubts concerning his qualifications had been addressed and resolved in his favor." Id. at 202. We then drew a distinction between the right to rely on BLM's decisions from the point of view of an assignee in attempting to show bona fide purchaser status vis-a-vis RSC's claim that the Government should be equitably estopped from rejecting its purported waiver/disclaimer. Thus, we stated:

We expressly note the distinction between May's right to rely on BLM's erroneous decision that the defect in Zuckerman's offer had been cured and that the lease should issue, and the absence of a right in Engle to assert his reliance on this decision as a basis for estopping the Government, discussed above. To May, all that was apparent was that a question about the validity of Zuckerman's offer had apparently been raised and duly resolved in his favor by BLM. No appeal of this resolution was pending or foreseeable. Accordingly, in the absence of an apparent challenge to the correctness of this decision, May could rely on it in good faith, and so become a bona fide purchaser.

The adequacy of Engle's reliance on BLM's erroneous decision as a basis for his invoking the extraordinary relief of equitable estoppel is measured by different, and much stricter, standards. As an insider to the dealings with BLM, Engle understood more clearly than could May the possibility that it would ultimately be found to have violated the regulations, yet he took no steps to secure his position.

Id. at 202-03 n.7.

So, too, in this case, Diamond had a right to rely on the actions of BLM in issuing the lease as a rejection by BLM of any contention that the waiver/disclaimer would not cure the defects inherent in Reece's offer. As we noted in Ervin Staacke, supra, a prospective assignee must exercise "ordinary care" and is not held to the standard of what an extraordinarily careful prospective assignee might do or not do. 62 IBLA at 285. See also O'Kane v. Walker, supra.

We disagree with BLM's holding that the retained overriding royalty interests were null and void ab initio and find instead, as discussed in Home Petroleum Corp., supra, that the interest was merely voidable. We hold that BLM properly canceled the overriding royalties retained by Reece and RSC, for the reasons set out in Wilbur G. Desens, supra at 279-80; Inexco Oil Co., supra at 269-70; Wayne E. DeBord, 50 IBLA 216 n.1, 87 I.D. 465 n.1 (1981) (appeal pending).

We must finally consider Geosearch's objection to the sale of the canceled interests. The second drawn offers were not rejected; they remained viable in case the first drawn offers were found defective. Since Diamond has been determined to be a bona fide purchaser, its interest in this lease is protected by the provision of 30 U.S.C. § 184(h)(2) (1976). Under this chapter, partial interests which are canceled or forfeited must be sold by the Secretary to the highest qualified bidder.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision of the Wyoming State Office is affirmed as modified.

James L. Burski
Administrative Judge

We concur:

Bernard V. Parrette
Chief Administrative Judge

Edward W. Stuebing
Administrative Judge

