

EMERY ENERGY, INC.

IBLA 85-155; IBLA 85-913

Decided December 16, 1985

Appeal from a decision by Administrative Law Judge Harvey C. Sweitzer rejecting certain noncompetitive oil and gas lease offers for failure to disclose all parties holding an interest in the offers, as required by 43 CFR 3102.2-7 (1981).

Affirmed as modified and remanded to BLM.

1. Oil and Gas Leases: Applications: Sole Party in Interest

As a general rule, when a partner in a firm engaged in the oil and gas business files an oil and gas lease offer in his own name without disclosure of the interests of the partners, the offer is properly rejected for failure to disclose interested parties in compliance with the regulations. Rejection is mandated notwithstanding the existence of negotiations to terminate the partnership where the record discloses that the partnership agreement has not been terminated at the time the lease offer is filed.

2. Oil and Gas Leases: Cancellation -- Oil and Gas Leases: First-Qualified Applicant -- Oil and Gas Leases: Noncompetitive Leases

The Secretary of the Interior has the authority to cancel by administrative decision a noncompetitive oil and gas lease which was invalid at its inception because it issued to a party other than the first-qualified applicant in violation of statute and Departmental regulations.

3. Oil and Gas Leases: Rentals -- Payments: Refunds

A refund of advance rental payments tendered in connection with a noncompetitive oil and gas lease may be ordered where it is determined after administrative litigation that the lease issued to a party other than the first-qualified applicant and, hence, cancellation is required, if the lessee has been deprived of the benefit of the lease and there has been no intent to defraud the Department and the public.

APPEARANCES: R. Dennis Ickes, Esq., Salt Lake City, Utah, for appellant; C. M. Peterson, Esq., Denver, Colorado, for Rosita Trujillo.

OPINION BY ADMINISTRATIVE JUDGE GRANT

Emery Energy, Inc. (Emery) has appealed from a decision of Administrative Law Judge Harvey C. Sweitzer, dated November 14, 1984, in which he ruled that certain noncompetitive oil and gas lease offers should be rejected 1/ because Emery had failed to disclose, at the time of filing or within 15 days thereafter, the existence of all parties having an "interest" in those offers, as required by 43 CFR 3102.2-7 (1981). 2/ Emery has also appealed from a letter decision of BLM dated November 19, 1984, refusing to suspend appellant's obligation to pay the annual rental for the oil and gas leases pending resolution of this appeal. The two appeals have been consolidated for review.

This is the second time this case has been before the Board. The decision of Administrative Law Judge Sweitzer stems from our previous decision in this case, cited as Rosita Trujillo, 77 IBLA 35 (1983), wherein we set aside a BLM decision denying the Trujillo protest and referred the case to the Hearings Division for an evidentiary hearing. In material part, the BLM

1/ The leases at issue were actually issued to Emery by the Bureau of Land Management (BLM) in November 1982 (with an effective date of Dec. 1, 1982), which was prior to the timely filing of a notice of appeal by the conflicting offeror, Rosita Trujillo, from rejection of her protest of the Emery lease offers. The conflicting lease offers filed by Emery and Trujillo with their respective dates of filing are identified at Appendix A. Accordingly, the issue now is whether the Emery offers should properly have been rejected by BLM and, hence, should now be cancelled, in light of the conflicting offers and the statutory obligation to issue noncompetitive oil and gas leases to the first-qualified applicant. 30 U.S.C. § 226(c) (1982).

2/ That regulation, which was in effect at the time the Emery offers were filed provided as follows:

"(a) The applicant shall set forth on the lease offer, or lease application if leasing is in accordance with Subpart 3112 of this title, or on a separate accompanying sheet, the names of all other parties who own or hold any interest in the application, offer or lease, if issued.

"(b) A statement, signed by both the offeror or applicant and the other parties in interest, setting forth the nature of any oral understanding between them, and a copy of any written agreement shall be filed with the proper Bureau of Land Management office not later than 15 days after the filing of the offer, or application if leasing is in accordance with Subpart 3112 of this title. Such statement or agreement shall be accompanied by statements, signed by the other parties in interest, setting forth their citizenship and their compliance with the acreage limitations of §§ 3101.1-5 and 3101.2-4 of this title."

This regulation was subsequently repealed effective Feb. 26, 1982. 47 FR 8544. The existence of conflicting noncompetitive lease offers filed while the former regulation was in effect coupled with the obligation of the Secretary of the Interior under 30 U.S.C. § 226(c) (1982) to issue noncompetitive oil and gas leases only to the first-qualified applicant therefor, requires adjudication of these offers under the former regulation.

decision which prompted the initial appeal held that Emery had not failed to disclose any interested party in the lease offers, based on a finding that Emery's partners in a limited partnership agreement executed by Emery on November 23, 1979, had waived their interest in any noncompetitive oil and gas lease offers filed by Emery after September 24, 1980.

In our prior decision we found:

The partnership agreement was executed by Robert Howard as limited partner on October 12, 1979; by Tideway Western, Inc., as both general and limited partner, on October 30, 1979; and by Emery as general partner on November 23, 1979. The agreement was filed for record in the office of the clerk of court, Salt Lake County, Utah, on November 26, 1979. The business of the partnership is defined at Article 3:

[E]ngaging in all aspects of the oil and gas business including * * * acquiring, purchasing, leasing, * * * selling, transferring, and otherwise utilizing land, minerals or water upon, beneath and above certain land located within the general vicinity of the Rocky Mountain States of these United States. Such lands contemplated herein shall include Federal Bureau of Land Management managed lands available for noncompetitive oil and gas leasing.

Under Article 4, the term of the partnership commences on the date of filing and recording the partnership agreement and continues to December 31, 2003, "unless terminated earlier pursuant to this Agreement." The interest of the partners in the partnership assets is defined at Article 8: "All net revenues, minus expenses of the Partnership, including the proceeds of any sale or sublease of Partnership property shall be allocated 33 1/3% to Emery Energy, Inc., and 66 2/3% to the Limited Partners."

77 IBLA at 40.

[1] After examining Article 27 of the partnership agreement, containing the agreement of the partners not to compete for Federal noncompetitive oil and gas leases during the term of the agreement, the Board ruled that the partnership agreement gave rise to an "interest" of the partners in the lease offers as the term is defined at 43 CFR 3100.0-5(b) 3/:

3/ An "interest" was defined in the regulations as:

"An 'interest' in the lease includes, but is not limited to, record title interests, overriding royalty interests, working interests, operating rights or options or any agreements covering such 'interests.' Any claim or any prospective or future claim to an advantage or benefit from a lease, and any participation or any defined or undefined share in any increments, issues or profits which may be derived from or which may accrue in any manner from the lease based upon or pursuant to any agreement or understanding existing

This Board has previously held that where a partner in a firm engaged in the oil and gas business filed an oil and gas lease offer in his own name, the partnership is entitled to participate in the benefits accruing from any issued lease as a consequence of the partner's fiduciary duty to the firm. Johnnie B. Gryder, 38 IBLA 146, 149 (1978). Such a claim is an "interest" within the scope of the definition at 43 CFR 3100.0-5(b). Id. A fortiori, in a case such as the present where Emery is bound by an express covenant not to compete, the partnership agreement gives rise to an interest in the lease offers which must be disclosed on the lease offer form. The fact that the partners might elect not to participate is irrelevant. They had the option to participate which gave them an interest in the lease. Pursuant to the regulation in effect at the time the lease offers were filed, the offeror was required to disclose the names of other parties in interest on the lease offer and to provide a copy of the agreement between offeror and the other parties in interest within 15 days of filing the lease offer. 43 CFR 3102.2-7 (1981). Consequently, the Emery offers must be rejected for failure to comply with the regulations if the partnership is found to have been legally operative at the time the offers were filed. [Footnote omitted.]

77 IBLA at 42.

In our prior opinion, we found the evidence of record insufficient to establish that the partnership had been terminated or the partners had made a legally effective agreement to waive their rights in oil and gas lease offers filed by Emery prior to October and November of 1980, when the protested offers were filed. In light of the allegations of Emery, we ordered a hearing to resolve this issue of material fact.

At the hearing before Judge Sweitzer, testimony was given by Ronald J. Hollberg, Jr., President of Emery, and Dave Gammill, President of Tideway. Judge Sweitzer found from the testimony that in September 1980 Robert Howard, limited partner, notified Tideway that he wanted to terminate the partnership because he did not consider it profitable (Decision at 3, finding 4). Thereupon, negotiations commenced to terminate the partnership. The parties determined that a refund of the investment of partners Howard and Tideway would require withdrawal of previously filed lease offers in order to obtain advance rental refunds and that the withdrawal of the offers would jeopardize Emery's form S-1 registration statement filed with the Securities and Exchange Commission (SEC) in support of Emery's public stock offering. As a result, Emery negotiated to retain use of the partnership funds (Decision at 4, finding 6).

[1] Judge Sweitzer found that, pursuant to the September 24, 1980, letter from Emery to Tideway (Exh. 1 at 262; quoted in our prior decision,

at the time when the application or offer is filed, is deemed to constitute an 'interest' in such lease." 43 CFR 3100.0-5(b) (1981). A revised version of the definition is now codified at 43 CFR 3000.0-5(1).

77 IBLA at 43), Tideway agreed to allow Emery to continue using partnership funds for 60 to 90 days at which time Tideway could elect to either continue the partnership or be reimbursed according to the partnership agreement. In return, Emery agreed to "carry" Tideway for a 1/8 interest in gross proceeds from Federal oil and gas lease offers "in number equal to the dollars that Tideway Oil Co. has invested in Federal oil and gas applications at the date of this letter" as well as a two percent overriding royalty on any leases sold (Decision at 4, findings 8 and 9). Judge Sweitzer found the letter of September 24, 1980, contradicted the testimony of Hollberg and Gammill that Howard and Tideway had no further interest in anything Emery did after the intention to withdraw from the partnership was communicated in September of 1980 (Decision at 4-5, findings 11 and 12). Further, Judge Sweitzer found that the carried interest in certain acreage in oil and gas lease offers might require granting an interest in subsequent offers if a sufficient number of prior offers were withdrawn to cause the total acreage to drop below the agreed minimum (Decision at 5-6, finding 15).

In addition, Judge Sweitzer found that according to the terms of the partnership agreement, Emery had no authority, without prior written consent of all partners, to possess partnership property or to amend or terminate the partnership (Decision at 6, finding 17). Hence, Judge Sweitzer found the partnership had an interest which should have been disclosed in the lease offers filed by Emery in October and November 1980.

In the statement of reasons for appeal, Emery argues that it understood Gammill had authority to act for both Tideway and Howard and it understood the agreement contained in the letter of September 24, 1980, to be binding on all the partners. Further, appellant contends Tideway and Howard agreed to cease joint operations with Emery in the late summer of 1980 and that Gammill advised Emery of this fact. Appellant contends Tideway, Howard, and Emery all understood that there were to be no activities on behalf of the partnership after September 1980 and the other partners were to have no interest in lease offers filed by Emery thereafter.

In answer to appellant's statement of reasons, Trujillo argues that the testimony of Hollberg and Gammill regarding the termination of the partnership as of September 24, 1980, is inconsistent with the documentary evidence submitted by Emery. In particular, she cites an SEC registration statement dated March 9, 1981, stating that the partners agreed to terminate the partnership in December 1980 and a letter dated December 1, 1980, describing a "proposed agreement" to terminate the partnership. Further, Trujillo asserts that the 18-month "carried" interest in Federal oil and gas lease offers constitutes an interest requiring disclosure.

Upon review of the record, including the testimony and the documentary evidence introduced at the hearing, we conclude that the decision of the Administrative Law Judge must be affirmed as supported by the record. The testimony of Hollberg and Gammill supports the finding that Emery's partners had communicated a desire to terminate the partnership shortly before the September 24, 1980, letter (Tr. 29; Tr. 34). However, the testimony of Hollberg (Tr. 30) was that Emery was not in a position at that time to liquidate the partnership assets (primarily lease offers) and distribute the proceeds in the manner set forth in Article 15 of the partnership agreement

(Exh. 1 at 203-205) because it would jeopardize Emery's stock registration statement and, hence, issuance of the stock.

The letter of September 24, 1980, from Emery to Tideway (Exh. 1 at 262), signed by Hollberg, on behalf of Emery, and Gammill, on behalf of Tideway, constituted an attempt to resolve the predicament. As found by the Administrative Law Judge, this letter agreement was described by the parties as an "extension." Under its terms, the letter provided an "extension of sixty to ninety days" for Emery to control and utilize partnership assets subject to the option of Tideway to obtain reimbursement of its share of the assets at the end of the period. In return, Emery agreed to "carry" Tideway for a 1/8 interest in gross proceeds from Federal oil and gas lease offers filed by Emery "that are in number equal to the dollars that Tideway Oil Co. has invested in Federal oil and gas applications at the date of this letter." (Exh. 1 at 262). Further, Emery agreed to give Tideway a two percent overriding royalty on any leases sold. *Id.* Thus, the express terms of the letter of September 24, 1980, support Judge Sweitzer's finding that the partnership remained in existence, notwithstanding the testimony of Hollberg and Gammill that they did not consider the partners to have an interest in lease offers filed by Emery after that date.

We further find that the letter agreement did not identify the lease offers in which Tideway was to retain an interest. Hollberg testified at the hearing that lease offers filed on behalf of the partnership were occasionally withdrawn (Tr. 58). Indeed the investment approach to be employed by Emery on behalf of the partnership described in Article 18 of the partnership agreement clearly contemplates withdrawals of lease offers prior to acceptance by BLM (Exh. 1 at 206-210). The letter does not specify whether the carried interest applies only to lease offers filed by Emery prior to September 24, 1980. Although Hollberg testified that they intended the carried interest to apply only to lease offers filed prior to that date (Tr. 38), the terms of the letter support Judge Sweitzer's finding that if some of the offers were withdrawn, bringing the acreage below the amount Emery agreed to carry on behalf of Tideway, Emery would be contractually obligated to recognize a partnership interest in other lease offers (Decision at 5-6, finding 15).

The Hollberg letter of December 1, 1980, to Tideway which transmitted a "proposed agreement to terminate the limited partnership as requested by Dave Gammill" (Exh. 1 at 264) is further evidence that the partnership had not terminated prior to the time the protested lease offers were filed by Emery.

Finally, the record discloses that an agreement terminating the partnership (Exh. 1 at 259-261; Exh. B) was signed by partners Tideway and Emery on December 17, 1980. The signature of partner Howard is undated. The registration statement (Amendment No. 1 to Form S-1) filed by Emery with the SEC in connection with its public stock offering specifically referred to the partnership and stated that, "In December, 1980, all of the partners agreed to terminate the partnership" (Exh. 2 at 28-29). The registration statement further referred to the terms of the agreement, describing it as "amend[ing] the provisions of the Partnership agreement" and describing the consideration provided for "waiver of the other partners' rights to participate in the

Company's leasing activities" (Exh. 2 at 29). Consequently, we must conclude that the partnership agreement was not effectively terminated and the right to participate in Emery lease offers was not waived until December 1980, after the protested lease offers were filed. 4/

[2] The Secretary of the Interior has the authority to cancel by administrative decision an oil and gas lease which was invalid at its inception because it issued in violation of Departmental regulations. Boesche v. Udall, 373 U.S. 472 (1963); McKay v. Wahlenmaier, 226 F.2d 35 (D.C. Cir. 1955). Although the Department has discretion whether or not to issue an oil and gas lease for a given tract of land, if a noncompetitive lease is issued the Department is under a statutory duty (30 U.S.C. § 226(c) (1982)) to issue the lease to the first-qualified applicant. Udall v. Tallman, 380 U.S. 1, 4 (1965). The Department is bound by its regulations, and administrative cancellation of a lease is required where, subsequent to issuance, BLM discovers that the lease issued in violation of the regulation governing disclosure of parties in interest to an offeror other than the first-qualified applicant. See McKay v. Wahlenmaier, *supra*. Accordingly, the decision of the Administrative Law Judge is affirmed as modified and the case is remanded to BLM for cancellation of the Emery leases and adjudication of the Trujillo lease offers.

[3] By letter dated November 8, 1984, Emery, asserting that the administrative litigation has deprived the lessee of the beneficial use of the leases, applied to BLM for a suspension of the rental payments due on the protested leases, and requested a refund of all monies paid, except those amounts required to maintain Emery as a lessee. BLM responded by letter dated November 19, 1984, acknowledging that the leases are in administrative litigation and finding that they are outside the immediate jurisdiction of BLM. For this reason, BLM declined to rule on the requests. Further, BLM advised Emery that failure to pay rentals on or before the anniversary date would automatically terminate the leases by operation of law.

Emery filed an "appeal" from BLM's November 19, 1984, "decision." 5/

Although BLM declined to rule on the merits of Emery's request for a refund of rentals paid in 1982, 1983, and 1984 for the leases subject to this appeal, the issue is properly considered by this Board, as we have determined

4/ The Dec. 17, 1980, termination agreement contains a term stating that "The Limited Partners confirm that they previously agreed on September 24, 1980, to waive any interests in any Federal non-competitive oil and gas lease applications filed by Emery on or after September 24, 1980." (Exh. 1 at 260; Exh. B). This statement, made after the denial of the Trujillo protest and the filing of an appeal therefrom, is contradicted by the letter of Sept. 24, 1980. A retroactive waiver, agreed to after the filing of the protested lease offers by Emery, is not effective to eliminate an undisclosed interest.

5/ Appellant requested expedited consideration of the appeal in light of the ongoing obligation to pay rental during the pendency of this litigation. In light of the deprivation of the beneficial use of the leases, the Board previously suspended the leases and the obligation to pay the advance rental pending the outcome of this appeal by order dated Nov. 14, 1985.

that the leases must be cancelled. We note this Board held in J. V. McGowen, 9 IBLA 133 (1973), where an oil and gas lease had been cancelled because all parties having an interest in the lease had not timely complied with the disclosure requirements, that the Department may examine the circumstances to ascertain whether the rentals should be refunded pursuant to section 204(a) of the Public Land Administration Act of July 14, 1960, as amended, 43 U.S.C. § 1734(c) (1982). ^{6/} The rule that has been applied in determining whether a refund of rentals is proper in cases such as this was set forth in J. V. McGowen, supra at 138:

This Board, while holding that a refund of rentals could be made where a lease was issued to other than the first qualified applicant as a result of a mistake of law or fact not attributable to the lessee, warned that a refund might not be made if the cancellation of the lease is due to some fault of the lessee himself or if he stands to benefit through any arrangement with parties seeking the cancellation of the lease. Beard Oil Company, [77 I.D. 166, 169 (1970)].

Applying this standard, the Board in J. V. McGowen, supra, found no mala fides in the appellant (lessee) and ordered a refund.

This may be contrasted with the situation in Charles J. Babington, 17 IBLA 435 (1974), where a refund of rental for a cancelled lease was not allowed because a portion of the lease had previously been sold to a bona fide purchaser and was, consequently, protected by statute from cancellation.

Application of these precedents to the present case leads to a conclusion that the advance rental previously paid for the leases to be cancelled should be refunded. Although the cancellation of the leases is the result of the failure of the offeror to disclose the other parties to the partnership, the record does not disclose an intent to defraud the public or the Department. Rather, the testimony supports a finding that Hollberg, President of Emery, believed (erroneously) the partners had no interest in the lease offers. Further, although Emery's interest in two of the leases was assigned, the Board previously ruled that the assignee did not qualify as a bona fide purchaser, 77 IBLA at 39-40, and the leases are subject to cancellation.

In addition, we note that, in light of the Trujillo protest, BLM erred in issuing the leases to Emery prior to lapse of the time for the junior offeror to file a timely appeal from rejection of her protest of the Emery lease offers. The filing of a timely protest stays the action protested (lease issuance) until adjudication of the protest and any timely filed

^{6/} Following is the text of 43 U.S.C. § 1734(c) (1982):

"In any case where it shall appear to the satisfaction of the Secretary that any person has made a payment under any statute relating to the sale, lease, use, or other disposition of public lands which is not required or is in excess of the amount required by applicable law and the regulations issued by the Secretary, the Secretary, upon application or otherwise, may cause a refund to be made from applicable funds."

appeal therefrom. 43 CFR 4.21(a); see Goldie Skoldras, 72 IBLA 120, 123 (1983). The advance rental payments for which appellant seeks a refund would not have been made except for this error. Accordingly, on remand, appellant's rental payments should be refunded.

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 Judge Sweitzer is affirmed as modified, and the case is remanded to BLM for cancellation of the Emery leases, refund of Emery's rental payments, and adjudication of the Trujillo lease offers.

C. Randall Grant, Jr.
Administrative Judge

We concur:

R. W. Mullen
Administrative Judge

Wm. Philip Horton
Chief Administrative Judge

APPENDIX A

The lease offers filed by Emery and the conflicting offers filed by Trujillo together with the respective dates of filing are:

| Emery <u>Lease Offer</u> | Date <u>Filed</u> | Trujillo <u>Lease Offer</u> | Date <u>Filed</u> |
|-----------------------------|----------------------|--------------------------------|----------------------|
| I-16942 | 10/16/80 | I-18568 | 2/22/82 |
| I-16943 | 10/16/80 | I-18567 | 2/22/82 |
| I-16944 | 10/16/80 | I-18569 | 2/22/82 |
| I-16946 | 10/16/80 | I-18570 | 2/22/82 |
| I-16982 | 11/16/80 | I-18565 | 2/22/82 |
| I-16983 | 11/16/80 | I-18566 | 2/22/82 |

