

JERRY CHAMBERS EXPLORATION CO.  
JOHN M. BEARD

IBLA 87-287

Decided February 10, 1989

Appeal from decision of the Director, Minerals Management Service, affirming orders requiring payment of additional royalties and orders assessing late payment charges. MMS-86-0086-O&G, MMS-86-0087-O&G, MMS-86-0078-O&G, MMS-86-0079-O&G.

Affirmed.

1. Oil and Gas Leases: Communitization Agreements--Oil and Gas Leases:  
Royalties

The lessee of a Federal oil and gas lease committed to a communitization agreement providing for the apportionment of production among the leases committed thereto is responsible for payment of royalty to MMS on the share of production allocated to his lease. The lessor's entitlement to a royalty on the allocated share of production from any lessee/operator producing and selling communitized substances from the unit will not diminish the responsibility of the lessee where the operator has defaulted on the royalty obligation.

APPEARANCES: Kent L. Jones, James C. Hodges, Orval E. Jones, Tulsa, Oklahoma, for appellant; Peter J. Schaumberg, Geoffrey Heath, Howard W. Chalker, Office of the Solicitor, U.S. Department of the Interior, Washington, D.C., for the Minerals Management Service.

OPINION BY ADMINISTRATIVE JUDGE GRANT

Jerry Chambers Exploration Company (Chambers), John M. Beard (Beard), and Joseph F. Hoffman, lessees of Federal oil and gas leases NM 15074 and NM 23555, appeal from a decision of the Director, Minerals Management Service, dated December 18, 1986, affirming orders dated July 19, 1985, requiring payment of additional royalties in the amount of \$1,430,313.34 and affirming orders dated January 10, 1986, requiring total late payment charges of \$200,336.62.

Chambers' lease NM 15074, embracing the SW<sup>^</sup>, sec. 8, T. 12 N., R. 26 W., Indian Meridian, Roger Mills County, Oklahoma, was issued effective February 1, 1972. The Beard/Hoffman lease, NM 23555, which included

the NE<sup>^</sup> of the same section, was issued effective February 1, 1975. Both leases were issued for a term of 10 years and so long thereafter as oil or gas is produced in paying quantities and specify that the lessee shall pay the United States a royalty of 12.5 percent of the oil or gas sold or removed from the leased lands.

The Corporation Commission of Oklahoma issued Order No. 162189 in Conservation Division Cause No. 64717 on January 4, 1980, effective December 13, 1979. That order created a drilling and spacing unit for development of gas from certain formations which embraced the entire 640 acres in sec. 8. The order provided: "That all royalty interests within any spacing unit shall be communitized and each royalty owner within any unit shall participate in the royalty from the well drilled thereon in the relation that the acreage owned by him bears to the total acreage in the unit." Order No. 162189, at 2, `4. Subsequently, the appellants and other mineral interest owners holding the oil and gas rights to the lands within sec. 8, which could not be independently developed and operated in accordance with the state-approved well-spacing plan, entered into a communitization agreement dated February 3, 1981. Communitized substances thereunder included natural gas and associated liquid hydrocarbons produced from the Upper Morrow formation underlying sec. 8. The agreement provided in part that "communitized substances produced \* \* \* shall be allocated among the leaseholds comprising said area in the proportion that the acreage interest of each leasehold bears to the entire acreage interest committed to this agreement." Out of the 640-acre communitized area, the Federal leases of which appellants are the lessees embrace 160 acres each for a combined total of 320 acres constituting 50 percent of the communitized acreage.

The Davis No. 8-1 is the unit well located within the communitized area. The well was completed August 4, 1980, as a gas well with first sales of production on February 20, 1981. Based on MMS' review of leases NM 23555 and NM 15074, MMS determined that royalties in the amount of \$1,518,421.90 had not been paid for the period February 1981 through December 1984. On March 8, 1985, MMS ordered Matrix Energy, Inc., operator of the communitized area, to pay the royalties due. On June 7, 1985, MMS reduced this figure to \$1,430,313.34 to reflect a partial payment of \$88,108.56 from ANR Pipeline. MMS was unable to collect from Matrix and on July 19, 1985, it issued demand letters to appellants requiring them to pay the royalties due. It appears from the record that royalty payments in the amount of \$337,774.66 were tendered by other companies. On August 29, 1985, Chambers and Beard paid the remaining balance due under protest by each tendering checks in the amount of \$590,323.62.

Thereafter, on September 30, 1985, MMS issued a bill to Matrix for payment of interest charges for late royalty payments in the amount of \$200,336.62. Subsequently, MMS learned that Matrix had filed for bank-ruptcy on September 16, 1985. By order dated January 10, 1986, MMS demanded payment of the late payment charges on the royalty payments for the Federal leases from lessees Chambers and Beard. Payment was apparently tendered under protest and appeals of the late payment charge were filed with MMS.

Appellants contend in the statement of reasons for appeal that all lessees, including non-Federal lessees of private leases committed to the communitization agreement, are responsible for payment of royalties due the United States on all gas sales from the unit. Appellants argue they are liable to MMS only for their pro rata share of the royalties on production. In support of this contention, appellants cite Shell Oil Co. v. Corporation Commission, 389 P.2d 951 (Okla. 1964) (referred to as the Blanchard decision), a court precedent interpreting an Oklahoma statute governing allocation of production among unitized leases. This case is read by appellants to require MMS to look to the non-Federal lessees for payment of the additional Federal royalty attributable to their pro rata share of the production. Under this theory, appellants would be liable for only 50 percent of the additional royalty as their leases constituted only 50 percent of the acreage committed to the agreement.

[1] The lessee of a Federal oil and gas lease is obligated pursuant to the terms of the lease contract to pay the United States a royalty of 12.5 percent (one-eighth) on oil and gas removed from the leased lands.

See 30 CFR 218.100(a). A lessee may designate an operator to act for the lessee in matters relating to lease operations, but this does not relieve the lessee from ultimate responsibility for compliance with the lease terms. 43 CFR 3162.3(a); Supron Energy Corp., 45 IBLA 181, 192 (1980).

Section 17 of the Mineral Leasing Act of 1920, as amended, authorizes the commitment of lands within a Federal lease to a communitization agreement providing for apportionment of production or royalty among the separate tracts of land where, as in this case, the Federal leased lands cannot be independently developed in accordance with well-spacing requirements. 30 U.S.C. | 226(j) (1982) (recodified as section 226(m) by Federal Onshore Oil and Gas Leasing Reform Act of 1987, P.L. 100-203, 101 Stat. 1330-257). This provision of the Act further provides that "production pursuant to such an agreement shall be deemed to be \* \* \* production as to each lease committed thereto." 30 U.S.C. | 226(j). It was pursuant to this statutory authority that appellants entered into the communitization agreement allocating production among the leaseholds in the proportion that the acreage interest of each lease bears to the entire acreage committed to the agreement. Accordingly, in the context of the present appeal where 50 percent of the communitized acreage is embraced in Federal leases (25 percent in the Chambers lease and 25 percent in the Beard/Hoffman lease), MMS is entitled to receive a royalty on the 50 percent of the production allocated to the Federal leases, regardless of which lessee/operator produced the gas and sold the production. This is consistent with the holding of the Blanchard decision.

The litigation in that case was initiated by Blanchard, the lessor of a communitized lease who was not receiving any royalty on gas produced and sold from the communitized well on the other lease by the other lessee. To protect his interest, Blanchard petitioned the state corporation commission and, after a hearing, obtained a clarification of the communitization order to the effect that production of communitized substances would be allocated to the separate leases on an acreage basis for purposes of payment of royalty. On appeal, the court held that each lessor is entitled to receive, in

the ratio that his acreage bears to the unit acreage, a one-eighth royalty on the value of gas sold as required by the terms of his lease and that each lessee producing and selling gas from the well is obligated to pay royalty to the lessors accordingly. 389 P.2d at 954-55. This ruling clarifies the entitlement of the lessor to his pro rata share of the one-eighth royalty from the sale of all communitized substances and the corresponding obligation of the producing lessee. We find the Blanchard decision does not support the contention which appellants urge upon this Board. The entitlement of the lessor to a royalty on a pro rata share of production removed and sold by any lessee/operator does not diminish the responsibility of the lessee for royalty on production allocated to the leased lands. The producing operator is the agent of the lessee and the lessee must bear the ultimate responsibility for his default. <sup>1/</sup>

Having determined that MMS' royalty assessment was proper, we also find that assessment of late payment charges in the amount of \$200,336.62 is correct under 30 CFR 218.54 and 30 CFR 218.102. See Federal Oil and Gas Royalty Management Act of 1982, | 111, 30 U.S.C. | 1721 (1982). The Board has repeatedly recognized that the imposition of late payment charges is appropriate to compensate for the loss of use of funds due but not paid. Cities Service Oil & Gas Corp., 104 IBLA 291 (1988), and Sun Exploration & Production Co., 104 IBLA 178 (1988)(imposition of late payment charges on offshore oil and gas leases); see Yates Petroleum Corp., 104 IBLA 173 (1988) (interest on late payments of onshore royalty).

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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C. Randall Grant, Jr.  
Administrative Judge

I concur:

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Kathryn A. Lynn  
Administrative Judge  
Alternate Member

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<sup>1/</sup> We make no finding with respect to the issue of the liability of the non-Federal lessees to appellants for contributions to the additional royalties due MMS on gas sold by them or on their behalf as this question is beyond the scope of our jurisdiction in deciding this appeal.