

MALLON OIL CO. ET AL.

IBLA 87-557

Decided April 24, 1989

Appeal from that part of a decision of the New Mexico State Office, Bureau of Land Management, denying a request for a lower royalty rate upon reinstatement of oil and gas lease NM-43748.

Affirmed.

1. Federal Oil and Gas Royalty Management Act of 1982: Royalties--Oil and Gas Leases: Reinstatement--Oil and Gas Leases: Royalties--Oil and Gas Leases: Termination

BLM may, in accordance with 43 CFR 3108.2-3(f), reduce the royalty rate for a reinstated lease in three separate circumstances: (1) where it finds undue hardship or premature termination of production would result; (2) where a lessee has expended funds to develop the lease, after the rental was due and not paid, on the basis of any written action of the United States, its agents or employees, which preceded the expenditure of those funds and was a major consideration in their expenditure; or (3) where it finds it is equitable to do so for any other reason.

2. Federal Oil and Gas Royalty Management Act of 1982: Royalties--Oil and Gas Leases: Reinstatement--Oil and Gas Leases: Royalties--Oil and Gas Leases: Termination

Where an oil and gas lessee requests, in accordance with 30 U.S.C. | 188(i)(2) (1982) and 43 CFR 3108.2-3(f), reduction of the increased royalty rate upon reinstatement of its lease on the basis that a written action by BLM preceded and was a major consideration in its expenditure of funds to develop the lands covered by the lease after the rental became due and was not paid, that request is properly denied when the record shows that although the lessee received a letter from BLM after the anniversary date of the lease, that letter did not precede and was not a major consideration in the lessee's expenditure of funds to develop the lands covered by the lease.

APPEARANCES: Tommy Roberts, Esq., Farmington, New Mexico, for appellant; Margaret C. Miller, Esq., Office of the Field Solicitor, Department of the Interior, Santa Fe, New Mexico, for the Bureau of Land Management.

OPINION BY ADMINISTRATIVE JUDGE HARRIS

Mallon Oil Company, et al., 1/ lessees under oil and gas lease NM-43748, have appealed from that part of a May 14, 1987, decision by the New Mexico State Office, Bureau of Land Management (BLM), which denied their petition for reduction of the royalty rate for that lease. 2/

Competitive oil and gas lease NM-43748 was issued effective August 1, 1981, for a primary term of 5 years. In 1986, as the lease was not producing and the end of the primary term was approaching, appellants sought to drill a well to fulfill the requirements for a 2-year extension of the lease pursuant to 43 CFR 3107.1. 3/ In pursuit of such an extension, appellants submitted to BLM on July 15, 1986, a proposed communitization agreement. 4/ Following oral communications between BLM and Mallon Oil Company (Mallon), BLM, by letter dated August 4, 1986, informed Mallon as follows:

On July 15, 1986 we received a communitization agreement covering the E\ section 3, T. 25 N., R. 2 W., NMPM, Rio Arriba County, New Mexico. The area to be communitized contains Federal Lease NM-43748 which covers the E\ E\ section 3. The primary term of this lease ends on July 31, 1986. Due to our offices

1/ The other appellants are Estate of Robert A. Mitchem; Thomas Ltd.; Mallon Minerals Corp.; James Wallis; Colton Exploration Company; R.L. Bayless; KM Production Co.; Kodiak Petroleum, Inc.; American Penn Energy, Inc.; Carlyle A. Peterson; Kevin M. Fitzgerald; David L. Heppe; George O. Mallon, Jr.; Mallon-Mitchell 1984 Ltd. Partnership I; and Mallon-Mitchell 1984 Ltd. Partnership II.

2/ That decision also informed appellants of additional requirements for reinstatement of their lease; however, those additional requirements are not challenged and appellants assert they have submitted the necessary information to BLM.

3/ That regulation provides:

"Any lease on which actual drilling operations were commenced prior to the end of its primary term and are being diligently prosecuted at the end of the primary term or any lease which is part of an approved communi- tization agreement or cooperative or unit plan of development or operation upon which such drilling takes place, shall be extended for 2 years subject to the rental being timely paid as required by | 3103.2 of this title, and subject to the provisions of | 3105.2-3 of this title or 30 CFR 226.12, if applicable. Actual drilling operations shall be conducted in the manner in which someone seriously looking for oil or gas could be expected to pro- ceed in that particular area, given existing knowledge or geologic and other pertinent facts."

43 CFR 3107.1.

4/ The communitization agreement was approved by BLM on Sept. 9, 1986, with an effective date of June 3, 1986.

relocating to a new building, the communitization agreement will not be approved by that date.

Lease NM-43748 will not terminate on July 31, 1986 if both of the following conditions are met. There must be actual drilling operations in progress somewhere in the proposed communitized area at midnight July 31, 1986, and the communitization agreement must be in approvable status. [5/]

Lessees were notified via a decision dated December 1, 1986, that oil and gas lease NM-43748 had terminated automatically by operation of law on August 1, 1986, for failure to pay rent timely. They appealed that decision to this Board (docket number IBLA 87-219). In that case, appellants argued that the obligation to pay rent was not clearly stated in either the regulations or the statutes and that BLM was estopped from applying the automatic termination provision of the law because the conditions set forth in the August 4 letter were fulfilled. By order dated February 19, 1987, we rejected those arguments and affirmed termination of the lease, returning the case file to BLM for action on appellants' petition for a class II reinstatement of the lease, which they had filed on January 8, 1987, pursuant to 30 U.S.C. | 188(d)-(e) (1982) and 43 CFR 3108.2-3. In that petition, appellants also requested a reduction in the royalty rate pursuant to 30 U.S.C. | 188(i)(2) (1982) and 43 CFR 3108.2-3(f). 6/

In its May 14, 1987, decision BLM denied the royalty reduction request, merely stating that the request had been "thoroughly reviewed and a determination * * * made that the lease does not qualify." Lessees filed this appeal. They assert that sufficient information was submitted to BLM to warrant a favorable determination on their request and that BLM's action in denying the request was an abuse of discretion.

Appellants seek to invoke certain provisions of 43 CFR 3108.2-3(f). That regulation reads, in its entirety, as follows:

The authorized officer may, either in acting on a petition for reinstatement or in response to a request filed after reinstatement, or both, reduce the royalty in that reinstated lease on the entire leasehold or any tract or portion thereof segregated for royalty purposes, if he/she determines there are either economic or other circumstances which could cause undue economic hardship or premature termination of production; or because of

5/ The record shows that Mallon fulfilled the conditions outlined in that letter. See BLM memorandum dated Aug. 11, 1986, from the Farmington Resource Area Manager to the Albuquerque District Manager.

6/ 43 CFR 3103.3-1(a)(2)(ii) provides that for a lease reinstated in accordance with 43 CFR 3108.2-3, royalty shall increase 4 percentage points over the competitive royalty schedule in force and used for royalty determination for competitive leases. In their request, appellants sought a continuation of the royalty schedule in the lease as originally issued.

any written action of the United States, its agents or employees, which preceded, and was a major consideration in, the lessee's expenditure of funds to develop the lands covered by the lease after the rental had become due and had not been paid; or if the authorized officer determines it is equitable to do so for any other reason. [7/]

[1] The regulation allows BLM the discretion to reduce royalty rates for reinstated leases in three separate circumstances: (1) where it finds undue hardship or premature termination of production would result; (2) where a lessee has expended funds to develop the lease, after the rental was due and not paid, on the basis of any written action of the United States, its agents or employees, which preceded the expenditure of those funds and was a major consideration in their expenditure; or (3) where it finds it is equitable to do so for any other reason.

In their statement of reasons (SOR) at 12, appellants allege:

The receipt by Mallon Oil Company of the August 4, 1986 letter from the Bureau of Land Management was a major consideration in the decisions of the various lessees of record to expend additional funds on such development activities. * * * Prior to receipt of the August 4, 1986 letter from the Bureau of Land Management, only nominal funds had been expended in the drilling of the [well] * * *.

Appellants' position is that the August 4, 1986, letter from BLM constitutes a "written action of the United States, its agents or employees, which preceded, and was a major consideration in, the lessee's expenditure of funds to develop the property under the lease after the rent had become due and had not been paid." See 30 U.S.C. | 188 (i)(2) (1982).

BLM maintains that the August 4, 1986, letter did not constitute a "written action" within the meaning of 43 CFR 3108.2-3(f); the letter did not precede the lessees' expenditure of funds; and the letter could not have been a major consideration in appellants' decision to expend funds on the lease. 8/

7/ The regulatory language is, in essence, a restatement of the language of sec. 401(i)(2) of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), 30 U.S.C. | 188(i)(2) (1982), which granted the Secretary the authority to reduce royalty under the circumstances set forth therein.

8/ In addition, BLM supports its position by arguing that it followed the guidelines for royalty rate reduction set forth in 43 CFR 3103.4-1 and the Conservation Division Manual at 646.1.3B. Those guidelines, however, are inapplicable to appellants' request for reduction in royalty rate filed pursuant to 43 CFR 3108.2-3(f) because that request was based on BLM's written action, not on appellants' economic circumstances. Those guidelines specifically address economic considerations. Finally, the Conservation Division Manual provisions cited by BLM are dated June 23, 1980, and, thus, predate the enactment of sec. 401(i)(2) of FOGRMA, 30 U.S.C. | 188(i)(2) (1982).

This Board has previously considered appeals involving requests for reduced royalties for reinstated leases under 43 CFR 3108.2-3(f). Alta Energy Corp., 100 IBLA 313 (1987); Gulf Oil Corp., 83 IBLA 289 (1984). In Gulf Oil Corp., 83 IBLA at 292, we reviewed the legislative history of 30 U.S.C. | 188(i)(2) (1982) and determined that Congress had intended, by imposing higher royalty rates for reinstated leases, to penalize the lessee who failed to make timely rental payments. However, neither of those cases nor the legislative history discussed in Gulf provides any guidance as to Congressional intent regarding the "written action" circumstance. Thus, we are left to analyze the wording of the regulation, as applied to the facts of this case.

[2] We find that appellants clearly do not qualify for relief under the "written action" circumstance. Even assuming that BLM's letter could qualify as a "written action," the record does not show that the letter preceded and was a major consideration in appellants' expenditure of funds to develop the lease after the lease terminated.

Appellants commenced drilling the well on July 30, 1986, one day before the end of the primary term of Federal oil and gas lease NM-43748 (SOR, Exh. C). ^{9/} Thus, appellants were actively engaged in expending funds in hopes of receiving an extension of lease NM-43748 by drilling in accordance with 43 CFR 3107.1, prior to receipt of the August 4, 1986, letter from BLM. Although additional funds were expended following receipt of the letter (SOR, Exh. D), commitment of funds for preparation of the drillsite and drilling operations would have been made prior to the commencement of drilling. Furthermore, both parties admit that the letter represented written confirmation of oral assurances that BLM had made to Mallon, and the conditions set forth therein had to have been satisfied prior to receipt of the letter in order for the lease to qualify for an extension.

Appellants state that based on the knowledge that lease NM-43748 was in a non-producing status and that its primary term was due to expire, Mallon "decided to conduct its operations with respect to the lease, and the lands covered thereby, in a manner designed to obtain a two (2) year extension of the primary term of the lease in accordance with the provisions of applicable federal regulation" (SOR at 6). Thus, appellants sought the benefits of 43 CFR 3107.1, which provides that an extension by drilling is available for "any lease which is part of an approved communitization agreement." Appellants' inquiry of BLM was to ensure that drilling on lease NM-04077 would inure to the benefit of NM-43748, when it had filed a communitization agreement prior to lease expiration, but the agreement had not yet been approved. BLM's response to that inquiry was proper. See Devon Corp., 57 IBLA 131 (1981).

The thrust of the "written action" circumstance is that there be some detrimental reliance by the lessee on that action. In this case, there was

^{9/} The well in question was drilled on Federal oil and gas lease NM-04077, one of three leases communitized under the agreement approved effective June 3, 1986.

none. Appellants had complied with the conditions set forth in the letter before its receipt. Appellants admit utilizing 43 CFR 3107.1 to secure an extension of NM-43748, but they do not acknowledge that that same regulation states that lease extension is "subject to the rental being timely paid as required by | 3103.2 of this title * * *." (Emphasis added). Appellants complain that the August 4, 1986, letter made no mention of any other requirement or condition for extension of the lease. 10/ Nevertheless, it is clear that 43 CFR 3107.1 makes an extension subject to the rental payment requirement. 11/ Appellants expended funds in an attempt to gain the benefits of that regulation; they cannot escape its burdens. Appellants have failed to show that BLM's August 4, 1986, letter preceded and was a "major consideration" in their expenditure of funds to develop the lease.

Finally, to the extent appellants may be seeking royalty rate relief for any other reason in accordance with the third circumstance of 43 CFR 3108.2-3(f), outlined above, there are no equities in their favor. By awaiting the near expiration of the primary term of NM-43748 before drilling, appellants took a gamble. Had they drilled earlier, NM-43748 may have been on royalty status, and the 6-year rental would have been unnecessary. Appellants must accept the consequences of that decision. Cf. Hiko Bell Mining & Oil Co. (On Reconsideration), 100 IBLA 371, 393, 398 95 I.D. 1, 13, 15-16 (1988).

We find no evidence that BLM abused its discretion in denying the request for reduction of the royalty rate. All else being regular, BLM should reinstate NM-43748 at the increased royalty rate.

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.

Bruce R. Harris
Administrative Judge

I concur:

Will A. Irwin
Administrative Judge

10/ As BLM points out, the Minerals Management Service, not BLM, is the agency to which rental payments are made. Further, BLM alleges that appellants did not request information about rental payments, but about approval of the communitization agreement and its effect on termination. Appellants do not dispute that allegation.

11/ All persons dealing with the Government are presumed to have knowledge of relevant statutes and duly promulgated regulations. Venlease I, 99 IBLA 387 (1987).