

COTTON PETROLEUM CORP.

IBLA 87-492

Decided November 8, 1989

Appeal from a decision of the Assistant Director, Minerals Management Service, affirming assessment of interest charges for late payment of royalties on production from Federal oil and gas leases. MMS-86-0587-O&G.

Affirmed in part, appeal dismissed in part.

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

An assessment of interest charges for late payment of royalty pursuant to the regulation at 30 CFR 218.54(a) will be upheld on appeal where the error in payment resulted from a defect in the manufacture of the metering equipment used to measure production. The fact that the defect was caused by the negligence of a third party (the manufacturer) and was not readily apparent to the lessee will not absolve the lessee of liability for accurate measurement of production and payment of interest on any royalty thereon not timely paid.

APPEARANCES: Patricia A. Patten, Esq., Tulsa, Oklahoma, for appellant; Peter J. Schaumberg, Esq., Geoffrey Heath, Esq., and Howard W. Chalker, Esq., Office of the Solicitor, U.S. Department of the Interior, Washington, D.C., for the Minerals Management Service.

OPINION BY ADMINISTRATIVE JUDGE GRANT

This appeal is brought by Cotton Petroleum Corporation (Cotton) from a decision of the Assistant Director, Minerals Management Service (MMS), affirming an assessment of \$92,863.50 for late payment of royalties on production from Federal oil and gas leases.

An explanation of the basis for the late payment charges is found in the record in the field report prepared by MMS with respect to the prior appeal of the billing to the Director. It is explained that the bills were generated from late payment of royalties for Federal onshore leases

submitted on Form MMS-2014. Interest in the amount of \$86,964.67 was assessed for late payment of royalties on production from the Trigg Federal No. 28-1 well resulting from adjustments made by Northwest Central Pipeline Corporation (Northwest), the purchaser of gas from the well, from March 1980 through November 1985. It appears from the field report that the balance of the interest was assessed in connection with late payments from the Tierney Unit II production for the months of January 1981 through November 1985 as a result of expansion of the unit.

Cotton asserts in its statement of reasons for appeal that the late payment of royalties was the consequence of an error of measurement in the gas produced from the well and that this error was not the fault of the lessee as it was caused by defectively manufactured metering equipment. Appellant argues that it adhered to prudent operating practices; that the meter was checked and calibrated on a regular basis; that the error was discovered only by chance when an employee of Northwest noticed something unusual about the equipment; and that the error could not have been discovered sooner within the scope of the standards expected of an ordinarily prudent operator. Further, Cotton asserts that the State of Wyoming initially assessed interest for late payment of royalties as a result of volume adjustments made by Northwest in the same field but subsequently waived the interest when it ascertained that the error in measurement was not the fault of the lessee.

Cotton argues that the position of MMS in assessing interest where the late payment is not the fault of the lessee is contrary to the intent of the regulation at 30 CFR 218.54 as revealed by the preamble to the rulemaking. Appellant also contends that assessment of interest where the lessee had not received the payment on which the royalty was based is inconsistent with the legislative intent behind section 111 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), 30 U.S.C. § 1721 (1982), authorizing the assessment of interest at a penal rate in order to remove the incentive to hold and invest the funds rather than make timely payment.

In response to Cotton's statement of reasons for appeal, MMS points out that, under the regulations, royalty payments are due by the end of the month following the month in which the oil or gas is produced and sold and MMS has the authority to assess interest where payments are late. Further, MMS contends that appellant cannot escape the responsibility to report and pay royalty on production accurately and timely by asserting the circumstances of measurement of production were beyond its reasonable control. While acknowledging that an interest assessment may be waived in certain instances where the lessee is precluded from paying royalty by circumstances beyond its control (e.g., pending conclusion of controlling administrative proceedings), MMS contends that this is not such a situation because it is the lessee's duty to ensure proper measurement of production and the failure in this case was not outside the control of those responsible for lease operations.

In a reply brief, appellant reiterates that it acted as an ordinarily prudent operator. Cotton essentially asserts the defect was a hidden defect of such a nature that it could not reasonably be charged either with notice of the defect or negligence in failing to discover it earlier.

[1] The regulation at issue here provides in pertinent part that: "An interest charge shall be assessed on unpaid and underpaid amounts from the date the amounts are due." 30 CFR 218.54(a). This regulation was promulgated as part of a rulemaking implementing provisions of FOGRMA, 30 U.S.C. §§ 1701-1757 (1982). 49 FR 37336 (Sept. 21, 1984). Section 111(a) of FOGRMA provides in pertinent part that "where royalty payments are not received by the Secretary on the date that such payments are due, or are less than the amount due, the Secretary shall charge interest on such late payments or underpayments * * *." 30 U.S.C. § 1721(a) (1982). ^{1/} Royalty payments are due at the end of the month following the month in which the oil or gas is produced. 30 CFR 218.50(a). Although the language of the regulation contains no exception regarding assessment of interest charges where payment is made after it is due, it is true (as appellant asserts) that MMS indicated in the preface to the rulemaking that: "If a late payment or underpayment is not the fault [of] the lessee in the judgment of MMS, assessment of interest will be waived." 49 FR 37340 (Sept. 21, 1984).

In applying this regulation the Board has previously rejected the contention that the payment of additional royalty is not due until the gas purchaser has paid the lessee the additional consideration resulting from a subsequent adjustment in the price of gas and affirmed an assessment of interest from the date on which royalty is due under the regulations (i.e., the end of the month following production). ANR Production Co., 108 IBLA 387 (1989); Cities Service Oil & Gas Corp., 104 IBLA 291 (1988). No basis has been shown for reaching a different result in the present case. Regardless of the hidden nature of the defect in the metering equipment and the apparent negligence of the manufacturer of the equipment, we agree that this does not obviate the responsibility of the lessee/operator to accurately measure and pay royalty on all production from the leasehold. Accordingly, the application of the regulation at 30 CFR 218.54(a) to assess interest charges on the amount of royalty which was underpaid is properly sustained.

Appellant has not addressed the question of interest assessed as a result of unit expansion in the statement of reasons for appeal. In view of the failure of appellant in the statement of reasons to assert any error in this aspect of the Director's decision, this portion of the appeal is properly dismissed. See United States v. Reavely, 53 IBLA 320 (1981).

^{1/} It should be recognized that the authority of the Secretary to assess interest for late payment of royalty obligations has previously been recognized under other statutory and regulatory authority in affirming interest assessments for production occurring prior to enactment of FOGRMA. See Coastal Oil & Gas Corp., 108 IBLA 62, 66 n.8 (1989); Christmann Energy Corp., 107 IBLA 179, 181-82 (1989); Atlantic Richfield Co., 21 IBLA 98, 82 I.D. 316 (1975).

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 in part and the appeal is dismissed in part.

C. Randall Grant, Jr.
Administrative Judge

I concur:

Wm. Philip Horton
Chief Administrative Judge