

Appeal from a decision of the Director, Minerals Management Service, affirming a Royalty Management Program assessment of late payment charges on retroactive lump-sum royalty payments. MMS 85-0252-OCS and MMS 86-0105-OCS.

Affirmed as modified.

1. Oil and Gas Leases: Royalties: Interest

Under 30 CFR 218.54, MMS is authorized to assess a late payment (interest) charge if royalty payments for oil and gas leases are unpaid or underpaid on the date the amounts are due. Under 30 CFR 218.50(a), royalty payments are normally due at the end of the month after the month in which the oil and/or gas is produced and sold. However, where a judicial decision is rendered holding that a higher price for certain OCS gas may be retroactively collected, the date the additional royalty on the retroactive payment is due is properly determined by using the date the operator applied with FERC for an amendment of its certificates authorizing collection of the higher price for many of its other leases, in the absence of a convincing showing that it was reasonably prevented from doing so.

2. Oil and Gas Leases: Royalties: Payment

A lessee cannot generally avoid its responsibility to make timely payment to the Government of royalties because of difficulties in obtaining payments from and/or disputes with the purchaser, where there is no evidence indicating that the purchaser was not legally required to make the payment. Where the purchaser initially asserted that terms of its contract barred collection by the lessee of additional monies, but eventually capitulated and paid not only those additional monies to the lessee, but also late payment charges dating back to its receipt of the lessee's initial bill, the lessee may not avoid payment of late payment charges to the Government.

APPEARANCES: George J. Domas, Esq., New Orleans, Louisiana, 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 HUGHES

Oxy USA, Inc. (appellant), successor to the interest of Cities Service Oil and Gas Corporation (Cities), has appealed from a decision of the Director, Minerals Management Service (MMS), affirming in principle the assessment of late payment charges by the MMS Royalty Management Program (RMP) on a retroactive lump-sum royalty payment for Federal Outer Continental Shelf (OCS) leases Nos. OCS-G 1959 and OCS-G 2103. 1/ The late payment charges in question concerned royalty due for production from those leases in December 1978 through December 1980.

The chronology of events is critical to the issues presented by this appeal. In November 1972, Cities entered into a gas sales contract with Tennessee Gas Pipeline Company (TGPC) for the sale of the first half of the natural gas reserves attributable to Cities' interest in those leases, covering Eugene Island Blocks 257 and 258, Offshore Louisiana. In August 1976, Cities entered another contract, this one for the sale of the second half of the gas reserves from those leases (Cities' Suppl. Statement of Reasons (SOR) to the Dir. MMS, Att. 2 Exh. A). It is sales under the second contract that are involved in this appeal.

On February 22, 1977, the Federal Power Commission (FPC) issued a certificate authorizing the sale of gas under the second contract, approving a sales price of the lesser of the contract rate and the applicable national rate set by FPC. Sales under that certificate commenced on December 1, 1978, at which time Cities submitted statements to the Federal Energy Regulatory Commission (FERC) (FPC's successor) showing that it was charging the maximum rates allowed by FERC under section 104 of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. § 3314 (1988) (Cities' Suppl. SOR to the Dir. MMS, Att. 2 Exh. C). Those section 104 rates evidently constituted the "applicable national rate[s]" authorized in the certificate.

Natural gas produced between December 1978 and December 1980 was apparently sold by Cities to TGPC at the section 104 price. 2/ On July 2, 1981, the U.S. Court of Appeals for the Fifth Circuit upheld the right of a producer of natural gas to collect the higher price authorized by section 109(a)(2) of the NGPA, 15 U.S.C. § 3319 (1988), where deliveries of gas in interstate commerce had not been made until after November 8,

1/ As discussed below, the Director affirmed the collection of late payment charges back to a certain date, but remanded the matter to MMS for recalculation of the amount due.

2/ MMS' decision did not address gas produced at any other time.

1978. Tenneco Exploration Ltd. v. FERC, 649 F.2d 376 (5th Cir. 1981). 3/ As discussed below, the gas produced by Cities under its contract with TGPC fell into the category identified by the Court as qualifying for the higher section 109 price.

On March 12, 1982, the U.S. Court of Appeals for the Third Circuit remanded the record in a similar appeal involving Texaco, Inc. (Texaco), to FERC to allow it to reconsider the appropriate lawful price for Texaco's sales in light of the Fifth Circuit's Tenneco Exploration decision. Texaco, Inc. v. FERC, No. 80-2857 (3rd Cir. Mar. 12, 1982) (Cities' Suppl. SOR to the Dir. MMS, Att. 2 Exh. D at 3).

On July 22, 1982, following Tenneco v. FERC, supra, FERC issued an order amending the certificate of Tenneco and Texaco and requiring each to file a revised billing statement in its corresponding gas rate schedule that reflects the applicable price for the certificated sale. 4/ The amendment was retroactive to the "effective dates of the certificates" (Cities' Suppl. SOR to the Dir. MMS, Att. 2 Exh. D at 3-4).

On February 22, 1983, FERC issued a document entitled "Findings and Order after Statutory Hearing Amending Certificates of Public Convenience and Necessity," amending the certificates of various producers, including Cities. The order recites that Cities filed a petition to amend orders issuing certificates to authorize collection of the section 109 price, as well as revised billing statements. The FERC order did not address the leases involved in the instant appeal. 5/

3/ For a discussion of the court's holding, see note 11 below.

It does not appear that a petition for certiorari was filed with the Supreme Court. Thus, the decision became final before the end of 1981.

4/ FERC evidently relaxed filing requirements to allow a "blanket affidavit," and by allowing the collection of monthly inflation adjustments without requiring any further filings.

5/ Although MMS alludes to that FERC order, there is no copy of it in the record. Accordingly, we have taken official notice of the order. See 43 CFR 4.24(b). MMS was aware of the order, but alluded only to the fact that the order affected Texaco. It thus appears that MMS was unaware that the certificates of Cities were also affected.

Cities' leases that were affected by the order were: Texas Eastern Transmission Corporation, South Marsh Island Block 136 and 137, Offshore Louisiana; Michigan Wisconsin Pipe Line Company, High Island Block A-355, Offshore Texas; Michigan Wisconsin Pipe Line Company, West Cameron Block 487, Offshore Louisiana; Northern Natural Gas Company, Matagorda Island Block 686, Offshore Texas; Michigan Wisconsin Pipe Line Company, High Island Block A-555, Offshore Texas; Tennessee Gas Pipeline Company, Vermilion Block 119, Offshore Louisiana; Southern Natural Gas Company, Main Pass Block 311, Offshore Louisiana; El Paso Natural Gas Company, Matagorda Island Block 526, Offshore Texas; Texas Eastern Transmission Corporation, High Island Area, Block A-573, Offshore Texas; Transcontinental Gas Pipe Line Corporation, Eugene Island Blocks 242 and 243, Offshore Louisiana;

In the meantime, on December 20, 1982, Cities began its review of the applicability of the Tenneco case criteria to the gas being sold pursuant to the second contract with TGPC covering the second half of the reserves attributable to Cities' interest in leases OCS-G 2103 and OCS-G 1959, and investigation of the appropriate method to obtain the FERC authority for the section 109 price was commenced. On February 3, 1983, following such review and investigation, the necessary rate filings were submitted to FERC (Cities' Suppl. SOR to the Dir. MMS, Att. 2 Exhs. E-1 and E-2). Finally, on July 12, 1983, some 5 months and 9 days following Cities' application, FERC issued its order amending the original certificate authorizing the sale of gas from the second half of the gas reserves attributable to these leases and permitted the collection of the section 109 maximum lawful price retroactively to the date of first production (Cities' Suppl. SOR to the Dir. MMS, Att. 2 Exh. F; see generally Suppl. SOR to IBLA at 6-7). 6/

On August 12, 1983, Cities invoiced TGPC for the differential between the section 104 price and the higher section 109 price from the date of first production through June 30, 1983. The invoice was also revised on November 16, 1983, to reflect the retroactive price increase resulting from FERC's re-imposition of the so-called "wet rule" for calculating the energy content of the gas, and to assess interest from TGPC for the period from the date of the original invoice to the date the revised invoice was received. On December 29, 1983, Cities received a lump-sum payment from TGPC, including 3-percent simple interest on TGPC's payment from the date TGPC received Cities' revised invoice, November 19, 1983, to the date of TGPC's payment (Cities' Suppl. SOR to the Dir. MMS, Att. 2 at 4-5). Cities did not pay additional royalty on that lump-sum payment from TGPC until January 31, 1985, more than a year later. 7/

To summarize, the gas sold by Cities to TGPC under the contract in question after December 1, 1978, fell within the category described in

fn. 5 (continued)

Sea Robin Pipeline Company, South Marsh Island Blocks 112 and 113, Offshore Louisiana; and Trunkline Gas Company, South Timbalier Block 86, Offshore Louisiana.

In addition to Texaco and Cities, the order affected the certificates of Shell Oil Company, Exxon Corporation, Conoco, Inc., Tenneco Exploration, Ltd., General American Oil Company of Texas, Texas Gas Exploration Corporation, and Amoco Production Company.

6/ By the same order, FERC also approved other applications by Cities concerning other leases and purchasers, as well as similar applications by Getty Oil Company.

7/ MMS' decision and answer state that the royalty was paid on Jan. 31, 1985 (Director's Decision at 3; Answer at 3). Appellant states that, on both "Jan. 31 and Feb. 28, 1985, Cities paid royalties to the MMS on the amount received from [TGPC]" (Suppl. SOR before IBLA at 8-9). Although this discrepancy will affect the amount of late payment charges, it is unnecessary for us to resolve it now. MMS should consider this question in determining the amount of late payment charges, which it has yet to do. See note 8, below.

Tenneco v. FERC, *supra*, so that Cities was authorized by FERC to charge TGPC the higher section 109 price retroactively to the date of first delivery, apparently in December 1978 or shortly thereafter. That additional charge generated additional royalty, which Cities paid to MMS in an admittedly untimely manner. The issue presented by this appeal is, how untimely was Cities' payment?

The Director's decision assessed Cities for late payment charges dating back to March 31, 1983, the month following the month in which (he held) Cities could have received the lump-sum payment if it had diligently pursued collection (Decision at 3). Appellant counters that late payment charges should be calculated from no earlier than January 28, 1984, that is, 30 days after December 30, 1983, the date Cities actually received the lump-sum payment from TGPC. Thus, at issue in the present appeal are late payment charges for the period from April 1, 1983, through January 28, 1984. 8/

8/ On Aug. 13, 1985, RMP issued an order to Cities assessing a late payment charge of \$2,134,531.89. Appellant appealed \$1,777,240.72 of that charge, and its appeal was docketed by the Director, MMS, as MMS 85-252-OCS. On Jan. 12, 1986, RMP issued a second order assessing an additional \$646,614.82 for interest that MMS omitted from its initial order. Appellant appealed \$547,486.57 of the second invoice to the Director, MMS, and that appeal was docketed as MMS 86-0105-OCS. The two appeals were consolidated by the Director, MMS.

According to the Director's decision, the late payment charges originally assessed by RMP (aggregating \$2,769,330.23) dated back to the dates of production from 1978 through 1980 (Director's Decision at 4). Cities did not appeal the late payment charges insofar as they applied to the period between Jan. 31, 1985, the date of the lump-sum payment, and Jan. 28, 1984, which was 30 days after Dec. 30, 1983, the date Cities received additional payments from TGPC. The amount that was not appealed represents Cities' calculation of the amount of late payment due if the due date were set at Jan. 28, 1984.

It appears that RMP conceded on appeal to the Director that its original assessment using the dates of production as the due dates was incorrect, and that RMP had arrived at a new due date of Feb. 28, 1983, the date when, according to RMP, Cities would have received payment if it had been diligent (Director's Decision at 4). The Director's decision further set the due date back to Mar. 31, 1983, and remanded the matter to RMP to recalculate the late payment charges using that date (Director's Decision at 9). The late payment charges were thus substantially reduced.

As appellant asserts that the due date is no earlier than Jan. 28, 1984, the Director's decision still adversely affects appellant, as it imposes approximately 10 additional months of late payment charges.

Cities requested a suspension of the effect of the MMS orders to pay, pending appeal pursuant to 30 CFR 243.2. Upon denial by the Director, MMS, Cities filed an emergency motion for stay of the MMS order denying suspension of the RMP orders with the Board. On Oct. 9, 1985, this Board issued

[1] Section 111(a) of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), 30 U.S.C. § 1721(a) (1988), provides that, if royalty payments on oil and gas leases are not received when they are due or are less than required, the Department "shall charge interest on such late payments or underpayments." The implementing regulation, 30 CFR 218.54(a), states that "an interest charge shall be assessed on all unpaid and underpaid amounts from the date the amounts are due." (Emphasis added.) Under 30 CFR 218.50(a), "[r]oyalty payments are due at the end of the month following the month in which the oil and gas is [sic] produced and sold."

MMS used as a guide in calculating the late payment charges the date that a reasonable operator would have received the payment. MMS treated that date as "the month in which the oil [and/or] gas [is/are] produced" under 30 CFR 218.50(a) and held that the "due" date under 30 CFR 218.54(a) (from which late payments were charged) was the end of the month following the month in which a reasonable operator would have received the payment.

We generally regard this procedure as consistent with a broad reading of the regulations quoted above. Royalty payments are due at the end of the month following the month in which the oil and/or gas is/are produced and sold. In view of the fact that a fundamental term of the sale is altered when the FERC-approved sales price is changed, we deem it appropriate to affirm MMS' decision to measure compliance with the royalty payment timing requirements for any increases in royalty from that time.

MMS took two different routes to its result. It ruled that Cities should have received FERC approval no later than the date Texaco received its approval, and also that Cities could reasonably have applied within a certain time of learning of FERC's initial approval of the amendment to Tenneco's certificates. <sup>9/</sup> However, in making those rulings, the Director

fn. 8 (continued)

an order vacating the Director's decision of Sept. 19, 1985, and granted a temporary stay conditioned upon appellant's filing of a bond as an assurance of reimbursement of the costs if appellant was unsuccessful. Cities Service Oil & Gas Corp., IBLA 86-9.

<sup>9/</sup> The Director held:

"I conclude that in the exercise of reasonable diligence Cities could have filed its application with FERC no later than 2 months after the July [22], 1982, FERC order. I further conclude that FERC required approximately 5 months to process and approve [Cities'] application. And since MMS policy regarding this type of retroactive lump-sum payment dictates that payment shall be made by the end of the month following the month in which FERC approval was (or could have been obtained), [Cities'] royalty payment should have been received by MMS no later than March 31, 1983 (i.e., the end of the month following the month in which Texaco received FERC approval)."

(Decision at 6-7). This holding sets out two different methods of determining when Cities should have made payment, each resulting in the same date.

was apparently unaware that Cities, like Texaco, had also received approval from FERC on February 22, 1983, to charge the higher section 109 price for some of its leases. Clarification of that significant fact compels us to affirm the decision of the Director, MMS, for reasons other than those stated in his decision. Accordingly, we affirm that decision as modified below.

There is precedent in royalty matters for holding a lessee to the same schedule met by a lessee in comparable circumstances. See Transco Exploration Co., 110 IBLA 282, 324-26, 96 I.D. 367, 390 (1989). <sup>10/</sup> It is a logical extension of that principle to hold that Cities should have applied for the higher price for all of its leases at the same time, in the absence of a convincing showing that it was reasonably prevented from doing so. If it had done so, it would have been authorized to collect the higher price on February 22, 1983.

Cities has made no convincing showing as to why it could not have reasonably filed for the section 109 prices for the leases covering Eugene Island Blocks 257 and 258, Offshore Louisiana, at the same time it applied for the other leases listed above. Appellant has admitted that Cities took notice of the Tenneco decision upon its release on July 2, 1981, and of FERC's amendment of Tenneco's certificate on July 22, 1982, reflecting the section 109 price change.

fn. 9 (continued)

The first method uses July 22, 1982, the date of the FERC order approving the amendment of Texaco's and Tenneco's certificates, but requiring each to file a revised billing statement. To that date is added 2 months during which Cities should have filed its application with FERC, taking the time to Sept. 22, 1982. MMS allowed a period of "approximately 5 months" for FERC to process and approve the application, taking the date to approximately Feb. 22, 1983. Finally, MMS set the date the royalty payment was "due" at March 31, 1983, the end of the month following the month in which FERC would have approved the application to amend the certificate had Cities filed in a reasonably timely manner. The second method also adopts as the due date Mar. 31, 1983, the end of the month following Feb. 22, 1983, the date in which Texaco received final FERC approval to collect. Thus, the Director also appears to adopt the conduct of Texaco as the standard that a prudent operator should meet.

<sup>10/</sup> In Transco, we ruled that a lessee (Transco) which did not promptly secure a rate increase was liable to pay additional royalty on production representing increased value resulting from a FERC-approved price increase for a period in which another lessee in similar circumstances (Enstar) had secured the rate increase. The circumstances in that case were slightly different, in that FERC did not award the rate increase retroactively to the date certificates were issued. Instead, Transco's failure to file with FERC promptly resulted in its losing authority to collect the higher price for several months, as compared with Enstar. We held that Transco was liable for royalty on the increased rates from the time that Enstar was authorized to receive them. 110 IBLA at 327-28; 96 I.D. at 391-92.

We reject appellant's argument that the delay from the time of the issuance of the Tenneco decision until the time of its filing for an amended certificate with FERC was reasonable because it was not clear from that decision whether Cities could charge the higher NGPA section 109 prices. We find that the Tenneco decision, although identifying a number of factual questions, is reasonably clear as to what gas was subject to the section 109 price change and is not prohibitively complex in its holding and its potential application to similar gas leases, particularly to parties versed in the pricing schemes imposed by the governing legislation. <sup>11/</sup> Appellant admits that Cities did not begin its review of Federal leases Nos. OCS-G 1959 and OCS-G 2103 until December 20, 1982, and did not file with FERC for an amended certificate until February 3, 1983. We see no reason why it would take 19 months after the Tenneco decision and over 6 additional months after the initial FERC ruling in Tenneco for Cities to determine that these leases presented the same situation, particularly as it was able to do so as to many of its other leases in time to receive FERC approval to collect the higher rate on February 22, 1983.

Thus, we hold, the additional royalty was (as the Director held) due by the end of March 1983, the month following the month in which approval could

<sup>11/</sup> The Court held that, although sections 104 and 109(a)(2) of NGPA both required the natural gas to be "committed or dedicated to interstate commerce" on Nov. 8, 1978, section 104 additionally required that a "just and reasonable rate" under the Natural Gas Act (NGA) be in effect on Nov. 8, 1978, whereas section 109 required the opposite, that a "just and reasonable rate" under the NGA not be in effect on that date. Tenneco, 649 F.2d at 378.

The Court further held that OCS natural gas which, if sold, would be required to be sold in interstate commerce (within the meaning of the NGA) under the terms of any contract, would properly be "committed or dedicated to interstate commerce on November 8, 1978" under both sections 104 and 109(a)(2). As the gas met that test, the applicability of section 104 or section 109(a)(2) hinged on whether or not a "just and reasonable rate under the [NGA]" was in effect on that date. In answering that question, the Court adopted Tenneco's argument that an NGA rate applied if the gas came under FERC's NGA jurisdiction, that is, if the gas was "dedicated to interstate commerce." Unlike the NGPA's broader term "committed or dedicated to interstate commerce," the NGA term "dedicated to interstate commerce" required not just a contract to sell the gas in interstate commerce, but actual sales in interstate commerce. Thus, if a producer did not commence actual delivery of the gas until after Nov. 8, 1978, it was not "dedicated to interstate commerce" and the NGA rate did not apply. Instead, the higher section 109(a)(2) price applied.

Thus, the higher section 109(a)(2) price applied to OCS natural gas which, if sold, would be required to be sold in interstate commerce under the terms of any contract (that is, gas which was "committed to interstate commerce") on Nov. 8, 1978, but actual delivery of which did not commence until after that date (that is, gas which was "not yet dedicated to interstate commerce within the meaning of the NGA"). Id. at 381.

reasonably have been received had Cities acted prudently to receive approval to charge the higher rate for all of its qualifying leases.

[2] Although Cities billed TGPC on August 12, 1983, Cities did not actually receive payment from TGPC until December 30, 1983, apparently because of a disagreement between the parties as to the amount owed. Appellant maintains that it should not be assessed interest charges during this period because of Cities' good faith efforts to collect the price differential from TGPC. Any delay in payment, it argues, was not Cities' fault, so that collection of late payment charges would be inconsistent with the intent and purpose of FOGRMA and MMS' contemporaneous interpretation of 30 CFR 218.54. In support of this argument, appellant notes that, in response to one comment at the time of the promulgation of this regulation, MMS agreed that "[i]f a late payment or underpayment is not the fault [of] the lessee in the judgment of MMS, assessment of interest will be waived" (Appellant's Suppl. SOR at 17).

As a general rule, a lessee cannot avoid the responsibility of timely payment to the Government because of difficulties in obtaining payments from the purchaser. Dugan Production Corp., 107 IBLA 91, 94 (1989). Neither Congress nor MMS intended that interest should be deferred pending resolution of a dispute between the lessee and the purchaser. Cities Service Oil & Gas Corp., 104 IBLA 291, 295 (1988). In the absence of a showing that there was a genuine dispute between the lessee and purchaser directly affecting the lessee's legal entitlement to receive additional monies for the sale of gas, we are not persuaded to extend the due date for payment of royalty on those monies. There is no reasonable doubt here that, following FERC's amendment of its certificate, the purchaser was legally required to pay Cities the difference between the section 104 and section 109 prices retroactive to the date of first production. Although TGPC evidently initially asserted that the terms of its contract with Cities barred collection of additional monies, TGPC eventually capitulated and paid not only the additional monies to Cities, but also late payment charges dating back to its receipt of Cities' initial bill (Cities' Suppl. SOR to the Dir., MMS, Att. 2 at 4-5). In these circumstances, we are not persuaded that Cities' obligation to pay late payment charges arose only after it received the additional monies from TGPC. See Cities Service Oil & Gas Corp., supra at 295 n.3.

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

---

David L. Hughes  
Administrative Judge

I concur:

---

Gail M. Frazier

Administrative Judge