

PITCH ENERGY CORPORATION

IBLA 2004-185

Decided July 26, 2006

Appeal from a decision of the Deputy State Director, New Mexico State Office, Bureau of Land Management (BLM), affirming a decision of the Carlsbad Field Office, BLM, requiring a record title holder of an oil and gas lease to either produce or plug and abandon wells. SDR 2004-07 (NMLC-069041).

Affirmed.

1. Oil and Gas Leases: Generally--Oil and Gas Leases: Assignments and Transfers

BLM may properly look to record title holders of Federal oil and gas leases for performance of obligations to submit plans for production from or plugging and abandonment of wells.

APPEARANCES: James E. Haas, Esq., Artesia, New Mexico, for appellant; Dale Pontius, Esq., Office of the Field Solicitor, Santa Fe, New Mexico, for the Bureau of Land Management.

OPINION BY ADMINISTRATIVE JUDGE PRICE

Pitch Energy Corporation (Pitch) has appealed from a March 4, 2004, decision of the Deputy State Director, Minerals and Lands, New Mexico, Bureau of Land Management (BLM), affirming on State Director Review (SDR) a December 17, 2003, decision of the Carlsbad Field Office (CFO), New Mexico, BLM, which required Pitch, as the lessee of record under Federal noncompetitive oil and gas lease NMLC-069041, to either produce or plug and abandon four oil and gas wells on leased lands. While upholding CFO's decision, the Deputy State Director approved Pitch's request for a 90-day extension of time to permit the New Mexico Energy, Minerals and Natural Resources Department, Oil Conservation Division (OCD), to pursue its plans to plug and abandon the wells. By order dated May 24, 2004, the Board granted Pitch's petition for a stay pending an adjudication of the merits of its appeal.

The four wells at issue here are the Welch A Nos. 1 through 4, situated on 238.90 acres of public land, described as Lots 1 through 3 and the S $\frac{1}{2}$ NE $\frac{1}{4}$ and SE $\frac{1}{4}$ NW $\frac{1}{4}$ sec. 4, T. 19 S., R. 31 E., New Mexico Principal Meridian, Eddy County, New Mexico. Lease NMLC-069041 was issued to Dwight Allison, effective May 1, 1951, for a term of 10 years and so long thereafter as oil or gas was produced in paying quantities, pursuant to section 17 of the Mineral Leasing Act of 1920 (MLA), as amended, 30 U.S.C. § 226 (2000).^{1/} Later, 100% of the record title interest in the lease was assigned by Allison to Western Oil Fields, Inc. (Western), by instrument dated April 29, 1955. Western subsequently became Summit Energy Corporation (Summit). Summit assigned 100% of the record title to Bulldog Energy Corporation (Bulldog), effective April 1, 1989. Pitch acquired 100% of the record title by assignment approved by BLM, effective February 1, 1993. (SOR, Ex. 8.)

Southwest Royalties, Inc. (Royalties), with a post office box address in Midland, Texas, became sublessee as a result of obtaining 100% of the operating rights to the lease by transfer approved by BLM, effective June 1, 1991. (SOR, Ex. 4.) Royalties posted performance bond SW-NM 1765 on August 2, 1991. (SOR, Ex. 1, Serial Register Page dated Dec. 19, 2003, at 2.) According to a notation on that Serial Register Page, at some point the bond was replaced with a nationwide bond, serialized as NM-1936. Id.; see also Pitch's Amended Request for SDR, Ex. 10. The record does not disclose any information regarding the notation or the circumstances that gave rise to it.

Royalties transferred 100% of the operating rights to Southwest Reserves, Inc., at an address on Crescent Court in Dallas, Texas, by transfer approved by BLM, effective September 1, 1991. (SOR, Ex. 5.) Under the regulations, Southwest Reserves, as the owner of 100% of the operating rights and sublessee (or the lessee or operator) should have posted a bond or other financial guaranty. 43 CFR 3104.1(a), 3104.2. In the alternative, with the surety's consent, Southwest Reserves could have been named a co-principal on Royalties' bond if the bond did not contain consent to do so. 43 CFR 3106.6-1. In 1991 and 1992, Southwest Reserves received partial assignments of operating rights in, among others, the Welch A lease from the surface down to a depth of 4,500 feet, and bills of sale of all rights in any operating agreements, easements, rights-of-way, contracts, the wells, equipment, and other personal property and fixtures on the lease.

^{1/} The Welch A Nos. 1 and 3 ceased production in the 1980s. The Welch A No. 4 has produced only 29 barrels of oil since 1990, and the Welch A No. 2 has never produced. (Statement of Reasons (SOR) at 3-4.)

In 1991 and 1992, under the name of Southwest Reserves, Charles Langston, president, executed a number of partial assignments and assignments of fractional interests and, in one case, an undivided interest, in the operating rights in the Welch A lease from the surface down to a depth of 4,500 feet to both individuals and companies. Those transactions also transferred rights in any operating agreements, easements, rights-of-way, contracts, the wells, equipment, and other personal property and fixtures on the lease. (See various assignments submitted as Ex. 19 to Pitch's Jan. 13, 2004, Amended Request for SDR.)^{2/} Most of the partial assignments contained a paragraph pursuant to which Southwest Reserves' assignees agreed to properly plug and abandon lease wells in accordance with applicable Federal and State regulatory agencies or "agencies having jurisdiction," and agreed to indemnify and hold Southwest Reserves harmless "from and against all losses, costs, claim and expenses arising out of or in any way connected with Assignee's failure to so perform up through his [percentage interest] ownership, and in accordance with the Provisions of Said Operating Agreement." Id.

On April 30, 1993, CFO received a sundry notice from Royalties dated February 21, 1991, notifying BLM of a change in operators from Royalties to SWR Operating Company (SWR), at the Dallas address of Southwest Reserves, effective January 1, 1991. Compare SOR, Ex. 5 with Ex. 9. BLM appeared to treat both entities as under Langston's control. See June 20 and July 1, 2002, Letters of Deputy State Director, BLM, to Langston (SOR, Exs. 16 and 17, respectively; see also SOR, Exs. 10-13). Nothing in the record shows that either Southwest Reserves or SWR provided a bond for the lease, but it appears that BLM believed that Royalties' statewide bond, NM-1936, covered their activities.

On May 10, 2001, CFO issued a decision requiring SWR to return the wells to production or plug and abandon them. (Amended Request for SDR, Ex. 11.) That decision was addressed to Langston at an address on McKinney Avenue in Dallas. SWR did not respond. On September 5, 2001, and October 2, 2001, CFO issued Incidents of Noncompliance (INCs) for failure to comply with written orders to SWR to Langston at the McKinney Avenue address. (Amended Request for SDR, Exs. 12, 13.) SWR did not respond. On November 5, 2001, CFO issued a Notice of Proposed Penalties with respect to the INCs. (Amended Request for SDR, Ex. 14.) That Notice

^{2/} We cannot determine whether the assignments and partial assignments submitted as Ex. 19 to Pitch's Amended Request for SDR constitute the entire record of transfers of operating rights in the lease down to a depth of 4,500 feet or not. Consequently, we make no effort to reconcile the transfers of interests to this depth, which together appear to exceed 100%, noting only that none of the instruments bears a BLM receipt stamp.

was sent via certified mail. Again, however, SWR failed to respond. See Amended Request for SDR, Ex. 15 at 1.

On December 10, 2001, BLM issued its decision requiring Pitch Energy, the lessee of record, to return the wells to production or plug and abandon them. In addition, BLM advised of applicable daily penalty amounts if the violations continued unabated. Citing the definitions of *lessee* and *operator*, 43 CFR 3160.0-5, and the lack of a response from SWR, BLM directed Pitch to produce the wells or plug and abandon them. (Amended Request for SDR, Ex. 15.) In a letter from Marbob Energy Corporation (Marbob) on Pitch Energy's behalf, received by BLM on December 12, 2001, Marbob responded with a request that the decision be stayed until after OCD completed proceedings to issue an order requiring SWR to either return the wells to production or plug and abandon them. In that (Amended Request for SDR, Ex. 16.) ^{3/} Marbob also asserted its belief that allowing OCD to conclude its actions would result in an outcome that would be

the most successful with the least amount of potential legal challenge. We have concerns that we believe we have no legal ability to be able to produce the wells. Likewise, we are concerned that if we went out and plugged these wells that we could be subjecting ourselves to litigation by the current operator.

(Amended Request for SDR, Ex. 16 at 2.)

On June 20, 2002, BLM notified SWR of the status of the enforcement action. After a recitation of events, the letter erroneously demanded civil penalties in the amount of \$300,250.00, calculated at 60 days x \$500.00/day plus \$250.00 for the initial assessment. A Bill for Collection in the amount of \$300,250.00 was enclosed. (Amended Request for SDR, Ex. 17.) By letter to SWR dated July 1, 2002, BLM corrected its calculations, instead demanding \$30,000.00 (60 days x \$500.00/day = \$30,000.00) and enclosing a Bill for Collection in the corrected amount. (Amended Request for SDR, Ex. 18.)

On December 6, 2002, following a hearing at which SWR did not appear, OCD issued order no. R-11871 to SWR in case no. 12965, in which it concluded that SWR

^{3/} The letter represented the relationship between Marbob and Pitch Energy as follows: "Marbob Energy Corporation, on behalf of Pitch Energy Corporation, is responding to your request regarding the plugging of the above-described wells. We recognize that since Pitch owns an interest in the deep rights in this lease and since we are lessee of record, our interest is at risk."

was the current owner and operator of 15 wells in Eddy County, including the four Welch wells, none of which had been produced or used for injection or other beneficial purposes for more than a year. One well on the list had been properly plugged and abandoned, so that 14 wells were at issue before OCD. Noting the potential for waste, violations of correlative rights, and contamination of various resources and OCD's numerous attempts to contact SWR and have the wells brought into compliance, SWR was directed to plug and abandon the wells on or before January 15, 2003, failing in which OCD would take such action as was necessary to do so, proceed against any bond held by BLM, and recover any costs incurred from the operator. SWR evidently did not respond to OCD's order.

By letter dated December 17, 2003, BLM ordered Pitch, as lessee of record, to take over operations of the four Welch A wells and either return them to producing status, use them for beneficial purposes, or plug and abandon them. Pitch Energy requested SDR.

On appeal to the State Director, Pitch asserted that, although it is the lessee of record, it had never been the operator or owned an operating interest. It noted that there had been "a number of prior bonded operators who have operated the wells at issue" and attributed the present situation to CFO's "erroneous determination of bond coverage." (Amended Request for SDR at 2.)^{4/} Additionally, characterizing its connection to the wells to be "tenuous at best," Pitch claimed that BLM's order to produce or plug and abandon the wells placed it in jeopardy from the owners and assignees of operating interests. Pitch therefore argued that it "should not be required to act as a guarantor for the errors and omissions of the BLM." Id.

In his March 9, 2004, decision, the Deputy State Director affirmed CFO's December 2003 decision requiring Pitch to either produce or plug and abandon the wells, explaining as follows:

It is true that the BLM requires the operator(s) of a lease to perform actions necessary to bring wells and facilities into compliance. However, if we cannot obtain compliance from the operators, we will require the holders of Record Title as the party ultimately responsible for the work. Under the regulations at 43 CFR 3106.7-6(a), the holders of record title interest "...assume the responsibility to plug and abandon all wells which are no longer capable of producing."

^{4/} "Page 2" of the Amended Request for SDR is actually the third page of the document.

(SDR Decision at 2, 3.) The Deputy State Director afforded Pitch a 90-day extension of time to comply with CFO's December 17, 2003, decision, in view of the fact that CFO had confirmed Pitch's report that the wells "do not present an immediate hazard"^{5/} and that OCD had decided that it would plug and abandon the wells if SWR failed to do so.^{6/} *Id.* at 2. In addition, while noting that CFO could extend that time period, the Deputy State Director informed Pitch that "[i]f the plugging program is significantly delayed, the CFO may require Pitch to demonstrate, through mechanical integrity tests, that the wells do not pose a hazard." *Id.* at 3. The Deputy State Director stated that Pitch bore the ultimate responsibility for plugging and abandoning the wells if OCD's plans changed, and noted that, in addition, Pitch is responsible for "ensuring that the surface is satisfactorily reclaimed and revegetated," as provided by 43 CFR 3162.3-4(c). *Id.*

On appeal, Pitch argues that pursuant to 43 CFR 3162.3-4, the operator bears the responsibility for plugging and abandoning wells. (SOR at 8.) Pitch contends that it has no responsibility to plug and abandon the wells, because it has never been an operating rights owner; moreover, such activity could place it "in jeopardy of legal liability for monetary damages" to the operating rights owners. (SOR at 7, 9.) Pitch points out that BLM did not require SWR to post a bond, and posits that the bond secured by Royalties is still active.^{7/} (SOR at 4-5.) Royalties is the last operating rights owner to hold a surety bond and is still the operator of record, Pitch argues, because SWR's failure to post a bond renders it "unable to serve as operator of the wells pursuant to 43 CFR 3106.6-1." (SOR at 7-8.) Moreover, Pitch maintains that the obligation to produce or plug and abandon the wells accrued before the approval date of the assignment of record title to Pitch and the assignment of operating rights to SWR, as the wells were incapable of producing oil and gas in paying quantities at the time Royalties became the owner of operating rights. (SOR at 8-9.) For the foregoing reasons, Pitch argues that Royalties is the proper party to plug and abandon the wells.

^{5/} BLM noted that three of the wells had "minor leaks to the surface," but that "[s]ome delay in well plugging should not have an adverse effect on surface resources." (SDR Decision at 2.)

^{6/} OCD's Jan. 15 deadline had clearly passed by the time of CFO's December 2003 order and the Deputy State Director's March 2004 decision. However, OCD had not yet taken action, although the decision noted that OCD had identified the Welch A wells "for plugging this year." (SDR Decision at 2.)

^{7/} Exs. 6 and 7 to Pitch's SOR are bond abstracts prepared by BLM documenting the status of statewide oil and gas bonds secured by Royalties. As of Dec. 18, 2003, Royalties was bonded in the amount of \$25,000 by BLM Bond No. NM-1936.

BLM responds that, since our May 24, 2004, order, it has been informed that OCD has in fact plugged the four Welch A wells. (Answer at 1.) However, BLM states, “issues remain with respect to potential surface reclamation”; therefore, the appeal is not moot. Id. BLM argues that the issues on appeal are controlled by the Board’s decision in Petroleum, Inc., 161 IBLA 194 (2004), aff’d sub nom. Monahan v. United States Department of the Interior, No. 04-CV-205-J (D. Wyo. May 17, 2005), appeal filed No. 05-8068 (10th Cir. July 22, 2005). BLM correctly notes that our decision in Petroleum, Inc. rejected arguments that record title owners are insulated from the requirement to plug and abandon well sites (Answer at 1-3), and that prior operators are solely responsible for producing or plugging and abandoning well sites (Answer at 3-4). BLM also requested that the Board “request a status report from the parties * * * to determine whether there are outstanding environmental issues” warranting the lifting of the stay order. Id. at 5.

[1] We begin with section 2(j) of Lease 069041, issued May 1, 1951, which was assigned to Pitch effective February 1, 1993. The lease states, in pertinent part, that the lessee agrees

to plug properly and effectively all wells before abandoning the same; to carry out at expense of the lessee all reasonable orders of the lessor relative to the matters in this paragraph, and * * * on failure of the lessee so to do the lessor shall have the right to enter on the property and to accomplish the purpose of such orders at the lessee’s cost[.]

A lessee may relinquish all rights under a lease and be relieved of its obligations. 30 U.S.C. § 187 (2000) (“The lessee may, in the discretion of the Secretary of the Interior, be permitted at any time to make written relinquishment of all rights under such a lease, and upon acceptance thereof be thereby relieved of all future obligations under said lease, and may with like consent surrender any legal subdivisions of the area included within the lease.”). However, section 5 of the lease specifies that, even if the lease is surrendered or terminated, the lessee remains “subject to the continued obligation of the lessee and his surety to * * * place all wells on the land to be relinquished in condition for suspension or abandonment in accordance with the regulations and the terms of the lease[.]” Section 2(m) recognizes and generally provides for the filing and effective dates of instruments transferring assignments of oil and gas lease or interests therein, including record title, working or royalty interests, operating agreements, and subleases, but that section does not relieve a record title owner of its rights and responsibilities under the lease as long as it retains record title. Thus, the assigned lease commits Pitch to produce or plug and abandon wells on the leasehold, and to perform any attendant responsibilities, including reclamation, if called upon by BLM to do so.

The assignment of operating rights under a Federal oil and gas lease has long been distinguished from the assignment of record title to the lease. Cross Creek Corp., 131 IBLA 32, 36 (1994), citing Harry L. Bigbee, 2 IBLA 23, 25, 27 (1971).^{8/} Departmental regulations differentiate between the two, stating that “[a] transfer of operating rights is * * * a subsidiary arrangement between the lessee (sublessor) and the sublessee * * * [and does not] affect the relationship imposed by a lease between the lessee(s) and the United States.” 43 CFR 3100.0-5(e). The assignee of full title to a Federal oil and gas lease, upon approval of the assignment to him, becomes the Government’s lessee and is responsible for compliance with the lease terms and any regulations affecting the lease. Marlin Oil Corporation, 158 IBLA 362, 367 (2003); Ralph G. Abbott, 115 IBLA 343, 346 (1990). While the designated operator and operating rights owner have primary responsibility for plugging wells, the ultimate responsibility remains with the record title owner of the lease. 43 CFR 3100.0-5(a), (d), (j); 43 CFR 3106.7-6(b); Marlin Oil Corporation, 158 IBLA at 367; Ralph G. Abbot, 115 IBLA at 346; see also Stanco Petroleum, Inc., 143 IBLA 86, 88 (1998). Accordingly, it is immaterial whether Pitch ever served as operator or owned any operating rights in the lease.

Pitch maintains that the obligation to produce or plug and abandon the wells accrued before the approval date of the assignment of record title to Pitch, and that Pitch therefore is not responsible for obligations relative to abandonment of the wells. However, 43 CFR 3106.7-6 draws no such distinction and provides, in pertinent part, as follows:

If I acquire a lease by an assignment or transfer, what obligations do I agree to assume?

(a) If you acquire record title interest in a Federal lease, you agree to comply with the terms of the original lease during your lease tenure. You assume the responsibility to plug and abandon all wells which are no longer capable of producing, reclaim the lease site, and remedy all environmental problems in existence and that a purchaser exercising reasonable diligence should have known at the time.

^{8/} “[A]ny oil and gas lease issued under the authority of this chapter may be assigned or subleased, as to all or part of the acreage included therein, subject to final approval by the Secretary and as to either a divided or undivided interest therein.” 30 U.S.C. § 187a (2000). Generally, an assignment is a transfer or making over to another of the whole of any property held by a lessee; a sublease is a transfer or making over to another of a partial interest held by a lessee. See Black’s Law Dictionary, (Revised 4th Ed. 1968) 153.

These requirements are consistent with the language of Lease NMLC-069041 noted above,^{2/} and with the case law cited herein as well.

The remainder of Pitch's arguments are directed at whether Royalties is the proper party to plug and abandon the wells and complete reclamation on the lease. BLM's acceptance of a bond from a sublessee does not relieve the record title holder of its obligation to comply with the terms of its lease or limit that obligation in any way. Likewise, BLM's failure to secure a bond from a sublessee does not relieve the record title holder of its obligation to perform under the terms of its lease. BLM properly held Pitch, the record title holder, responsible for producing or plugging and abandoning the Welch A wells, and for reclamation of the lease site.

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 and the request to lift the stay is denied as moot.^{10/}

T. Britt Price
Administrative Judge

I concur:

James F. Roberts
Administrative Judge

^{2/} Pitch's lease was issued "subject to the terms and provisions of the [MLA], as amended, * * * and to all reasonable regulations of the Secretary of the Interior now or hereafter in force when not inconsistent with any express and specific provisions herein, which are made a part hereof." (Initial paragraph of Lease NMLC-069041 at 1.) The applicable regulatory language in effect prior to Jan. 10, 2001, is not to the contrary.

^{10/} BLM had requested that the Board reconsider its May 24, 2004, order granting a stay of BLM's decision pending adjudication of the appeal.