AMOCO PRODUCTION CO.

IBLA 98-86 Decided August 31, 1998

Appeal from a decision of the Acting Associate Director for Policy and Management Improvement, Minerals Management Service, affirming assessment of compensatory royalty. MMS-92-0311-O&G.

Decision Set Aside, Demand Letter Vacated and Case Remanded.

1. Administrative Authority: Generally--Appeals: Jurisdiction--Board of Land Appeals--Judicial Review--Oil and Gas Leases: Royalties: Generally

   A statute establishing time limitations for commencement of judicial actions for damages on behalf of the United States does not limit administrative proceedings within the Department of the Interior.

2. Administrative Procedure: Administrative Review--Appeals--Res Judicata--Rules of Practice: Appeals: Generally--Rules of Practice: Appeals

   Where the BLM has rendered a final decision not appealed by an oil and gas lessee because the lessee properly believed the decision required MMS, in implementing the BLM decision, to use the 8.03-percent drainage factor accepted by BLM to calculate compensatory royalty, the doctrine of administrative finality will not shield MMS' compensatory royalty calculation from administrative review.

3. Oil and Gas Leases: Compensatory Royalty--Oil and Gas Leases: Drainage

   An MMS demand letter implementing a BLM decision requiring an oil and gas lessee to pay compensatory royalty for drainage resulting from an adjacent well will be vacated and the case remanded to MMS with instructions, where MMS' failed to use the 8.03-percent drainage factor as agreed between lessee and BLM, to calculate the step-scale royalty rate for the drained lease.

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APPEARANCES: Charles L. Kaiser, Esq., and Ezekiel J. Williams, Esq., Davis, Graham & Stubbs LLP, Denver, Colorado, and Robert G. Leo, Jr., Esq., Amoco Production Company, Denver, Colorado, for Appellant; Geoffrey Heath, Esq., 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 TERRY

Amoco Production Company (Amoco or Appellant) has appealed from a May 5, 1997, Decision of the Acting Associate Director for Policy and Management Improvement (PMI), Minerals Management Service (MMS), that affirmed a July 13, 1992, Order issued by the Royalty Management Program (RMP) of MMS. The July 13, 1992, RMP Order demanded payment of $49,789.86 in compensatory royalties for Federal Lease No. O64-064912-0 (subject lease). The compensatory royalty assessment was based on Amoco's failure to compensate the lessor for oil drainage occurring from the subject lease. While conducting an audit of the subject lease in accordance with section 205 of the Federal Oil and Gas Royalty Management Act of 1982, 30 U.S.C. § 1735 (1994), the State of Wyoming determined that Amoco underpaid royalties in the amount listed above for the period June 1, 1960, through December 31, 1988.

As a brief history, Amoco is the lessee of Federal Lease No. 064-074533-0 as well as the subject lease. Lease No. 064-074533-0 contains the West Wertz No. 1, the offending well. Amoco paid royalty on production from the offending well at the established royalty rate of 12-1/2 percent for Lease No. 064-074533-0. However, the subject lease (Federal Lease No. 064-064912-0) has a step-scale royalty rate. When the step-scale royalty rate was recomputed using the Bureau of Land Management (BLM) well count and production data, it exceeded the 12-1/2 percent rate upon which royalties had been remitted for production from the West Wertz No. 1 well. Consequently, compensatory royalties were computed for the subject lease based on: (1) the difference between a royalty rate of 12-1/2 percent and the recomputed step scale royalty rate, (2) the amount and value of the production from the offending well, and (3) the drainage factor. A drainage factor of 8.03 percent for the subject lease was submitted by Amoco on July 16, 1986, and accepted by BLM on September 3, 1986. (Decision at 1-2.)

March 13, 1990, BLM Letter-Decision

On March 13, 1990, BLM advised Appellant by Letter-Decision "that Federal Oil and Gas Lease No. 064-064912-0 was subject to potential drainage by the West Wertz No. 1, SWNW, Section 1, T. 26 N., R. 90 W." The Letter-Decision further states:

> Subsequently, Amoco and BLM reached agreement that drainage is and was occurring. By letter dated July 16, 1986, Amoco submitted, for approval, a drainage factor of 8.03%. This was accepted by BLM on September 3, 1986.

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> Since both parties agree that drainage has [been] and is occurring, compensatory royalty is being assessed. The compensatory royalty assessment is effective June 1, 1960, which is the first date of production for the West Wertz No. 1. This compensatory royalty assessment will utilize the agreed upon 8.03% drainage factor. A copy of our report is enclosed.

(Mar. 13, 1990, Letter-Decision, paras. 2-3.) The Letter-Decision further states: "As appropriate, this matter will be referred to Minerals Management Service at a future date for the computation and issuance of a bill for compensatory royalty due." (Mar. 13, 1990, Letter-Decision, para. 3.) Appellant did not appeal this Decision.

July 13, 1992, RMP Demand Letter

On July 13, 1992, the RMP issued a Demand Letter to Appellant in the amount of $49,789.86. This Demand Letter addressed the volumes and the values used to compute MMS royalties on compensatory royalty obligations for the drained lease, Federal Lease No. O64-064912-0. The Demand Letter stated, in pertinent part:

> On July 16, 1986, Amoco submitted to the District Manager of the Rawlins District Office, Bureau of Land Management (BLM) a drainage factor of 8.03 percent. This factor was accepted by BLM on September 3, 1986. The offending well is the West Wertz No. 1 located on Federal Lease No. 064-074533-0 with a 12.5 percent royalty rate. Amoco was the lessee and paid Federal royalty at a rate of 12.5 percent on production from the offending well. Federal Lease No. 064-064912-0 has a step-scale royalty rate. This step-scale royalty rate was recomputed using BLM's well count and well production data that included the offending well. The compensatory royalties due are based on two items. First, the difference between the recomputed step-scale rate and the 12.5 percent rate was applied to the drainage factor and the production from the offending well. Second, the difference from the recomputed step-scale rate, and the original lease step-scale rate was applied to the original production from Federal Lease No. 064-064912-0.

(July 13, 1992, Demand Letter at 1.)

In its Statement of Reasons (SOR) on appeal of the 1992 Demand Letter to MMS, Amoco argued that while compensatory royalties are intended to place the Government lessor in the same position as if the lessee had drilled an offset well to recover the drained production, the RMP Demand Letter is attempting to obtain an unauthorized benefit beyond any economic loss actually suffered. (1992 SOR at 2-3.) In the 1992 SOR, Amoco further stated:

> The amount of compensatory royalties due is the difference between the royalties that would have been paid had an offset well been drilled and the royalties actually paid. In the

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> present case, the MMS' calculations ignore these fundamental principles and have no valid factual or legal basis.
>
> Pursuant to the terms of the West Wertz Lease Amoco has paid a 12.5 percent royalty on production from that lease, including production from the West Wertz No. 1 Well. Therefore, additional royalties are due on the 8.03 percent of West Wertz No. 1 Well production which is attributable to the Lease only if a royalty rate higher than 12.5 percent would have applied to production from the Lease in the event Amoco had drilled an offset well on the Lease to recover the 8.03 percent production. To determine what royalty rate would have applied to Lease production had an offset well been drilled, 8.03 percent of the monthly production from the West Wertz No. 1 Well would be added to the actual production from the Lease and divided by the number of wells on the Lease that would have been necessary to recover that production (i.e., the number of existing wells plus one offset well). That number would represent the average per well production from the Lease if an offset well had been drilled. That average Lease production value would then be compared to the step-scale royalty rate table under the Lease to determine the applicable royalty rate for each month.
>
> The MMS did not do this. Instead, without any explanation, the MMS added the <u>total</u> monthly production from the West Wertz No. 1 Well (not just the 8.03 percent attributable to the Lease) and the actual production from the Lease, divided that value by the number of wells located on the Lease plus the West Wertz No. 1 Well, and then used that number to determine the step-scale royalty rate under the Lease.

(1992 SOR at 3-4.) Amoco further stated that there is no valid reason for MMS' use of 100 percent of the production from the West Wertz No. 1 well to calculate the step-scale royalty rate for production on the adjacent lease and MMS has provided no justifiable rationale. (1992 SOR at 4.) Appellant further argued in its appeal of the 1992 Demand Order that MMS' erroneous methodology unjustifiably inflates the step-scale royalty rate far beyond the rate that would have applied to lease production in the event Amoco had drilled an offset well to recover the 8.03 percent of West Wertz No. 1 well production being drained. (1992 SOR at 4-5.) Appellant's calculations demonstrated that rather than owing additional royalties on the Lease, Amoco actually overpaid royalties by 5,398.07 barrels, thereby placing the Department of the Interior in a significantly better position than it would be if an offset well had been drilled. (1992 SOR at 5.)

In its SOR before the Board, Amoco argues that MMS does not dispute that it erroneously used 100 percent of the production from the West Wertz No. 1 well to determine the step scale royalty rate for lease production, vice the 8.03-percent production rate Appellant had agreed to with BLM. (SOR at 5.) Appellant states again that compensatory royalties are

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intended to place the Government lessor in the same position as if the lessee had drilled an off-set well to recover the drained production, but are not intended to give the Government a benefit beyond the actual economic loss actually suffered. Id., citing Nola Grace Ptasynski, 63 IBLA 240, 252 (1982). Appellant claims the amount of compensatory royalties due is the difference between the royalties that would have been paid had an offset well been drilled and the royalties actually paid. Id., citing Benson-Montin-Greer Drilling Corp., 123 IBLA 341, 352 (1992).

Second, Amoco claims that the doctrine of administrative finality "does not bar Appellant from challenging the MMS' erroneous determination of the step-scale royalty rate." (SOR at 8.) In the May 5, 1997, MMS Decision, the Acting Associate Director had claimed that Amoco waived its right to challenge the use of 100 percent of the West Wertz No. 1 well production to calculate the step-scale royalty rate for lease production because BLM made that determination in its March 13, 1990, Decision and Amoco failed to appeal. Appellant claims that the one page BLM Decision states just to the contrary because it clearly provides that "compensatory royalty is being assessed" and "[t]his compensatory royalty assessment will utilize the agreed upon 8.03% drainage factor." (SOR, Exhibit 1, at 1.)

Finally, Appellant argues that the MMS claim for royalties over a 32-year period is barred by the 6-year statute of limitations at 28 U.S.C. § 2415 (1994). Appellant claims that MMS' ruling conflicts with the plain language of 28 U.S.C. § 2415(a) (1994) and the 10th Circuit's opinion in Phillips Petroleum Corp. v. Lujan, 4 F.3d 858 (10th Cir. 1993).

In its Answer, after briefly restating this Board's position with respect to 28 U.S.C. § 2415 (1994), MMS focuses on the argument that the doctrine of administrative finality bars Amoco's appeal. MMS argues that BLM's drainage report attached to its 1990 Decision "stated in the text, formula and attached tables that the royalty rate was based on all of the production from WW No. 1. The detailed report specified that BLM calculated the royalty rate using 100 percent of the production from WW No. 1." (Answer at 5.) MMS further urges: "BLM could not have been clearer that it was using all of the production, not 8.03 percent of the production, to determine the royalty rate. * * * Amoco's argument is merely counsel's after the fact rationalization of Amoco's failure to appeal in 1990 and it must be rejected." Id.

[1] As an initial matter, we reject Amoco's contention that these proceedings are barred by the 6-year statute of limitations at 28 U.S.C. § 2415 (1994). That section, which governs the time for commencing judicial actions brought by the United States, provides in part:

> Subject to the provisions of section 2416 of this title, and except as otherwise provided by Congress, every action for money damages brought by the United States or an officer or agency thereof which is founded upon any contract express or implied in law or fact, shall be barred unless the complaint

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> is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings required by contract or by law, whichever is later * * *.

28 U.S.C. § 2415(a) (1994).

This Board has held in numerous decisions that statutes of limitation apply to judicial enforcement of administrative actions, but not to the underlying administrative actions. See Texaco Exploration & Production, Inc., 140 IBLA 282, 284 (1997); Anadarko Petroleum Corp., 122 IBLA 141, 147 (1992); Marathon Oil Co., 119 IBLA 345, 352 (1991); Mobil Exploration & Producing U.S., Inc., 119 IBLA 76, 81, 98 I.D. 207, 210 (1991); Alaska Statebank, 111 IBLA 300, 311 (1989). We stated in Alaska Statebank, supra, that a Departmental proceeding requiring payments which accrued more than 6 years before the proceeding began "is not an action for money damages brought by the United States, but rather is an administrative action not subject to the statute of limitations." Id. at 311; see Texaco, Inc., 138 IBLA 202, 204 (1997); Phillips Petroleum Co. v. Johnson, 22 F.3d 616 (5th Cir. 1994).

While MMS may be prevented by 28 U.S.C. § 2415(a) (1994) from obtaining judicial relief on a claim for royalties where the obligation to pay arose more than 6 years prior to the filing of the claim with a court, an administrative claim for royalties is not precluded by that statute even where more than 6 years have elapsed since the obligation to pay the royalty arose. Amoco Production Co., 123 IBLA 278, 281 (1992); Mobil Exploration & Producing U.S., Inc., supra, at 81, 98 I.D. 210. We find therefore that 28 U.S.C. § 2415(a) (1994) did not bar MMS in this case from requiring Amoco to pay additional royalties that became due more than 6 years before payment was claimed, absent some other recognizable bar to enforcement.

MMS has argued that the Board should dismiss this appeal because the doctrine of administrative finality precludes Amoco from raising the issue of the disparity between the 8.03-percent drainage factor agreed to by BLM and Amoco in 1986, and the 100 percent of production actually used by BLM in its 1990 Drainage Report attached to the March 13, 1990, Decision, and implemented by MMS in computing the MMS royalty compensation Demand Letter in 1992. By not timely appealing the March 13, 1990, Decision, MMS contends, Amoco is now precluded from raising the use of the 100 percent of production in this appeal. (Answer at 4-6.)

The one page March 13, 1990, BLM Decision clearly states, however: "This compensatory royalty assessment will utilize the agreed upon 8.03% drainage factor." Furthermore, nowhere in the 1990 Decision did BLM state that it would use 100 percent of production in its calculations. In fact, one document in the official file provided the Board by MMS clearly explains that BLM changed the agreed-upon rates after issuing the

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1990 Decision. In a memorandum from Jeff Braunschweig, Wyoming Royalty Auditor to Scott Ellis, PMI/Appeals, dated September 20, 1995, Braunschweig states, in pertinent part:

> I'm sending the BLM decision letter to Amoco and other correspondence that I have. It appears that the royalty rates were part of the BLM decision (attachment 2) but BLM revised those rates from a SICD [State and Indian Compliance Department] (long after the BLM decision) and Amoco did not know that the BLM was revising the rates until they received the Demand Letter from MMS.

[2, 3] The doctrine of administrative finality—the administrative counterpart of the principle of res judicata—generally precludes reconsideration of a decision of an agency official when a party, or his predecessor in interest, had an opportunity to obtain review within the Department and no appeal was taken, or an appeal was taken and the decision was affirmed. Thermal Energy Co., 135 IBLA 291, 306 (1996); Edward N. O'Leary, 132 IBLA 337, 343 (1995). The doctrine applies only where the later proceedings involve the same subject matter, the same parties, and the same issues. Heirs of Herculano Montoya, 137 IBLA 142, 146 (1996); Beard Oil Co., 117 IBLA 54, 57 (1990); Frederick J. Schlichter, 54 IBLA 61, 63 (1981). Administrative finality, however, does not bar an appeal of a decision where the later appeal involved a "wholly separate issue." Frederick J. Schlichter, supra, at 63.

The issue of the application of the utilization of 100 percent of the production of the offending well was not even raised in the March 13, 1990, BLM Decision. Rather, it was raised in ambiguous language within the attached Drainage Report, although no specific mention of the utilization of 100 percent of production from the offending well exists in the 1990 Drainage Report used by MMS to compute the compensatory royalty assessment in the 1992 Demand Letter appealed by Amoco. The 1995 memorandum cited above reflects that the royalty rate in the Demand Letter was actually determined sometime after the 1990 Decision and Drainage Report. Even if the doctrine were technically applicable, as a matter of equity and to prevent the violation of basic rights, we could not apply it to this case. As this Board has stated:

> This rule is not absolute, because decisions by administration officials, as well as those of this Board, are made exercising authority delegated by the Secretary of the Interior. The Secretary, and those exercising his authority, may review a matter previously decided and correct or reverse an erroneous decision. See Gibbs Exploration Co. v. Udall, 315 F.2d 37, 40 (D.C. Cir. 1963).

Turner Brothers, Inc. v. OSMRE, 102 IBLA 111, 121 (1988). The Secretary of the Interior "is not estopped by the principles of res judicata or finality of administrative action from correcting or reversing an erroneous decision

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by his subordinates or predecessors in interest." Ideal Basic Industries, Inc. v. Morton, 542 F.2d 1364, 1368 (9th Cir. 1976). "It necessarily follows that this Board, in exercising the Secretary's review authority, is not required to accept as precedent erroneous decisions made by the Secretary's subordinates." Pathfinder Mines Corp., 70 IBLA 264, 278, 90 I.D. 10, 18 (1983), aff'd, Pathfinder Mines Corp. v. Clark, 620 F. Supp. 336 (D. Ariz. 1985), aff'd, Pathfinder Mines Corp. v. Hodel, 811 F.2d 1288 (9th Cir. 1987). In our view, since BLM committed the Department to applying a 8.03-percent drainage factor in its calculations of the compensatory royalty assessment, and so stated in the March 13, 1990, Decision, that would constitute a compelling legal reason to review a subsequent MMS Decision applying a wholly different drainage factor based upon an ambiguous Drainage Report at odds with BLM's prior commitment.

In this case, Amoco was deprived of its opportunity to challenge the revision contained in the 1992 Demand Letter. Amoco was entitled to a decision notifying it of the revision and the justification for the MMS change.

We therefore set aside the May 5, 1997, Decision. We vacate and remand to MMS the compensatory royalty assessment issued in the 1992 Demand Letter using 100 percent of production of the West Wertz No. 1 well, vice 8.03 percent of production as agreed between lessee and BLM. We direct BLM to provide Amoco with a new decision which includes its rationale for any revisions in the calculation of the compensatory royalty assessment other than as set forth in its March 13, 1990, Decision. Appellant, of course, retains the right of State Director Review and of appeal of this subsequent decision to this Board.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 C.F.R. § 4.1, the Decision appealed from is set aside, the 1992 Demand Letter is vacated, and the case is remanded to MMS for further action consistent herewith.

James P. Terry
Administrative Judge

I concur:

Gail M. Frazier
Administrative Judge

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