This volume of Decisions of the Department of the Interior covers the period from January 1 to December 31, 1990. It includes the most important administrative decisions and legal opinions that were rendered by officials of the Department during this period.

During the period covered by this volume, the following officials served with me as my principal advisors: Mr. Frank A. Bracken as Under Secretary; Ms. Constance B. Harriman, Ms. Stella A. Guerra, Messrs. Eddie F. Brown, Lou Gallegos, David C. O’Neal, and John M. Sayre as Assistant Secretaries of the Interior; Mr. Thomas L. Sansonetti as Solicitor; and Mr. James L. Byrnes as Director, Office of Hearings and Appeals.

This volume will be cited within the Department of the Interior as “97 I.D.”

Manuel Lujan, Jr.
Secretary of the Interior
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ERRATA:

On page 30, line 6, the correct spelling should be "appropriative."
On page 43, line 18, the X's denote a blank space.
On page 56, line 5, the word should be "projects."
On page 103, line 5, there should be a blank space before the period. The correct cite should read "90-1 BCA ¶ 22.412.)"
On page 258, second line from bottom of footnote 10, the "4" should be eliminated.
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NOTE—The abbreviations used in this title refer to the following publications: "B.L.P." to Brainard's Legal Precedents in Land and Mining Cases, Vols. 1 and 2; "C.L.L." to Copp's Public Land Laws, 1875 edition, 1 volume; 1882 edition, 2 volumes; 1890 edition, 2 volumes; "C.L.O." to Copp's Land Owner, Vols. 1-18; "L. and R." to records of the former Division of Lands and Railroads; "L.D." to Decisions of the Department of the Interior, Vols. 1-52; and "I.D." to Decisions of the Department of the Interior, Vols. 53 to current volume. —Editor.
Appeal from an August 13, 1987, decision of the Acting Director, Minerals Management Service, that the total production from the lease should be used when calculating the average daily production rate, which is used to determine the applicable royalty rate. MMS-86-0202-O&G and MMS-86-0307-O&G.

Affirmed as modified.

1. Oil and Gas Leases: Royalties: Generally—Regulations: Interpretation—Statutory Construction: Administrative Construction

It is within the authority of the Department to interpret its own regulations, and its interpretation should be given great deference. Normally an interpretive ruling stating the accounting procedures to be used for royalty calculation may be given retroactive effect. However, when it appears from the record that: (1) for several years the lessee had applied an accounting procedure which conformed with a reasonable interpretation of the applicable regulations when calculating the royalty due for oil produced and removed from the lease; (2) the Department had accepted lessee's royalty accounting procedure for several years before issuing an interpretive ruling that required a different accounting procedure; (3) the new procedure was an abrupt departure from a well-established practice, and not an attempt to fill a void in an unsettled area of the law; and (4) the prejudice to the lessee affected by retroactive application of the new interpretation substantially out-weighs the statutory interest and purposes sought to be protected, then the new MMS accounting procedure should be applied prospectively.


OPINION BY ADMINISTRATIVE JUDGE MULLEN

INTERIOR BOARD OF LAND APPEALS

Sun Exploration and Production Company (Sun) has appealed from an August 13, 1987, decision of the Acting Director, Minerals Management Service (MMS), that Sun had failed to properly apply the sliding-scale royalty provisions of its lease when determining the
royalty rate applicable to oil production during the period from January 1977 through January 1983 (MMS-86-0202-O&G and MMS-86-0307-O&G).

The record does not contain a copy of the lease 80-020997, and we do not know when it was initially issued. The lease was renewed with an effective date of February 1, 1978, and a copy of that renewal is in the case file. For the purposes of this decision, the term “lease” shall mean the February 1, 1978, lease renewal.\(^1\) Section 2, paragraph (d)(1) of the lease requires the lessee to “pay rentals and royalties in amount or value of production removed or sold from the leased lands as set forth in the rental and royalty schedule attached to and made a part hereof” (Lease at 2).

The attachment referred to in paragraph (d)(1) is Schedule D. This Schedule calls for a “sliding scale” royalty rate which is based upon the average daily production volume per well in the month the royalty accrues. The portion of Schedule D applicable to this case provides:

(2) For all oil produced of less than 30° Baume:

- On that portion of the average production per well not exceeding 20 barrels per day for the calendar month ........................................... 122%  
- On that portion of the average production per well of more than 20 barrels and not more than 50 barrels per day for the calendar month ........................................... 14%  
- On that portion of the average production per well of more than 50 barrels and not more than 100 barrels per day for the calendar month ........................................... 16%  
- On that portion of the average production per well of more than 100 barrels and not more than 200 barrels per day for the calendar month ........................................... 20%  
- On that portion of the average production per well of more than 200 barrels per day for the calendar month ........................................... 25%  

The MMS decision followed a review of Sun’s royalty payments for production from lease 80-020997 during the period from January 1, 1977, through January 31, 1983. This review was conducted by the State of California pursuant to section 205 of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), 30 U.S.C. § 1735 (1982). The State concluded that Sun’s failure to apply the correct royalty rates resulted in underpayment and delivery of less than the required amount of royalty-in-kind oil. The basis for the State’s contention was that Sun had improperly excluded oil used on the lease when calculating the average daily production for the purpose of determining the royalty rate.

By letter dated March 21, 1986, the Royalty Compliance Division, MMS, ordered Sun to pay $222,331 in underpaid royalties. This amount was stated to be the additional amount due as a result of applying the royalty at a higher rate to the sales volume.\(^2\) Sun appealed from this

---

\(^1\) We note that the period under review commenced prior to the renewal of the lease. If the previous lease terms differ materially from those contained in the Feb. 1, 1978, renewal, this decision may not be applicable to the royalties under the previous lease document. Neither party to this appeal raised this issue and we are presuming that the terms are unchanged.

\(^2\) The State had applied a royalty at the higher rate and had calculated the royalty based on gross production without deducting the fuel Sun had used on the lease.
determination (MMS-86-0202-O&G). By letter dated April 21, 1986, MMS ordered Sun to pay an additional $76,410, after determining that Sun had also applied the incorrect royalty rate when calculating the royalty-in-kind payment. Sun also filed a timely appeal of this determination (MMS-86-0307-O&G).

In his August 13, 1987, decision, the Acting Director, MMS, found the basis for the State's calculations to be incorrect, noting Sun's argument that the State's method imposed a royalty on the oil used on the lease by including oil not subject to a royalty to produce a higher royalty rate. After noting Sun's arguments that the phrase "average production per well" has always been interpreted as referring solely to "production subject to royalty," and that in its 1970 and 1979 correspondence the Department implicitly agreed to Sun's method of calculating royalties, the Director found that the United States is not estopped from asserting prerogatives granted by regulatory authority and that its rights may not be waived by past administrative practice. He then stated his opinion that neither the method advanced by the State nor the method advanced by Sun fairly implements the sliding-scale royalty provisions of the lease. Based on his finding that "the object of the sliding scale rate provisions to spread royalties over the total produced volumes is best served by allocating the lease use volumes proportionately to each production category calculated for a month," he found that, for the period in question, Sun had improperly calculated the average daily production by not including the oil consumed in lease operations. He then found that this failure resulted in Sun's misapplication of the sliding-scale royalty rates to the oil sold and its failure to deliver the total volumes of royalty-in-kind oil due. He then directed MMS to assign lease use volumes to each royalty rate category proportionately and recalculate the royalties due based on the reassignment of the total volume of oil used on the lease to each category. Sun appealed from this decision.

In its statement of reasons (SOR) on appeal, Sun contends that, under the Mineral Leasing Act, royalties are to be based on sales volumes rather than total production, and MMS failed to establish statutory authority for its method of calculating sliding-scale royalties. Sun correctly notes that the issue of assessing royalties on that portion of the oil sold, rather than the total production, is well settled and cites Federal court and Board cases in support of this limitation. Sun contends that the Acting Director erred when finding the manner of determining the royalty rate set out in his decision does not impose a royalty on exempt lease fuel and conflicts with MMS regulations.

According to Sun, the courts, this Board, and MMS regulations and forms construe the word "production" to include only royalty bearing production, and the Director has misconstrued the plain meaning of the MMS regulations. Sun contends that the MMS decision "conveniently fails to discuss a single regulation that supports [its]
newly devised methodology. The Director instead purports to find authority for his action in certain terms of the [lease] itself * * * * * * (SOR at 14). Sun cites the Board’s holding in *Amoco Production Co.*, 45 IBLA 16 (1980), in support of its contention that a provision of the lease which purports to negate the express language of the Mineral Leasing Act, as amended, and the oil and gas operating regulations is a nullity. Sun further contends that the following portion of the *Amoco* decision directly supports its contention:

Section 17 of the Mineral Leasing Act, as amended, 30 U.S.C. § 226(b) (1976), provides that royalty due the United States shall be computed at the rate fixed in the lease on the amount or value of production removed or sold from the lease. The words “removed or sold from the lease” were added after the word “production” in the 1946 amendment to the Act, August 8, 1946, 60 Stat. 951, giving thereby persuasive evidence that the Congress intended to ensure that royalty would be due only on oil and gas removed from the leasehold, not on the total oil and gas produced from the well. The operating regulations in 30 CFR 221.44 specifically state this exception.

* -- * : * * * : * * *

The Oil and Gas Operating Regulations in 30 CFR Part 221 were issued pursuant to the authority granted the Secretary by the Mineral Leasing Act, 30 U.S.C. § 189 (1976). The Secretary, therefore, must abide by and follow these regulations in administering oil and gas leases issued under the Act. As above quoted, section 221.44 provides that gas used for production purposes is excepted from royalty due the United States. We think it is error by the Geological Survey in this instance to seek payment of royalty for such gas, contrary to the statute and regulations, notwithstanding the language in section 5 of the Unit Agreement.

45 IBLA at 20. Finally, Sun contends that the method of determining the royalty rate is arbitrary and capricious. Sun advances three lines of reasoning in support of this argument. The first is that, contrary to the intent of the regulations, the method imposed penalizes operators who must use lease fuel for production, because this non-income generating oil must be included in the calculation of the royalty rate. According to Sun, this results in the lessee paying more royalty on less profit than would be the case for an operator not having a lease-fuel-consuming operation. The second is that MMS’ interpretation is discriminatory because, under this interpretation, a lessee using lease fuel is always subject to a higher royalty rate than one who does not. The third is that when lease fuel volumes equal or exceed lease-sales volumes a higher royalty rate would always be imposed, none of the royalty bearing production would be subject to the lower rate, and the objective of giving preferential treatment to marginally productive leases would be vitiated.

The Department filed an answer to Sun’s SOR. MMS contends that its method of royalty calculation complies with both the lease and the regulations. MMS states that:

Schedule D of the lease states that royalty will be calculated based on the “average production per well.” 30 C.F.R. § 206.104 (formerly set forth in similar form at 30 C.F.R. § 221.49) also states that sliding scale royalties “are based on the average daily production per well * * * * * * The average daily production per well for a lease is computed on the basis of * * * * the gross production from the leasehold.” [Italics added.]

Additionally, 30 C.F.R. § 206.104(i)(2) states: “The average production per well per day is
determined by dividing the total production of the leasehold by the number of wells. See also 30 C.F.R. § 206.104(i)(1).

(Answer at 3). According to MMS, use of qualifiers such as “gross” and “total” in the regulations cited above would be superfluous unless it was possible to confuse gross or total production with “net” production; i.e., production that has been reduced (netted) by some amount. It is MMS’ position that the use of the qualifiers in the regulatory language clearly refers to an amount that would include oil consumed on lease.

The answer also addresses Sun’s contention that Amoco Production Co., supra, is applicable by noting that the Amoco case did not interpret the sliding-scale royalty provision of a Federal oil and gas lease. It further contends that its interpretation of the lease is consistent with the Amoco decision, noting that, although total production is used when determining the average daily production, the royalty amount is determined by applying the applicable royalty to the oil removed or sold from the lease.

Citing Marathon Oil Co. v. Andrus, 452 F.Supp. 548 (D. Wyo. 1978) (which had also been used as authority for Sun’s arguments), MMS noted a statement made on page 551 of that opinion that:

Prior to the issuance of the NTL-4 Notice, the practice of the United States Department of the Interior had been that, in determining the amount of production to which royalty rates will be applied, no royalty is payable on oil or gas unavoidably lost, used in lease or producing operations on the leasehold premises, or beneficially used for purposes of production on the leasehold.

MMS argues that this quote makes it clear that “production” includes all of the oil produced and the royalty is collected only on that portion of the production removed or sold from the lease.

In its final response to Sun’s arguments MMS states that its application of the formula does not automatically impose a second-tier royalty rate on any production legally subject to a royalty obligation, and submits two examples of how the royalty would be calculated using the formula each advances as being correct.

[1] The issue before us can be more readily understood when viewed in the light of an example of the royalty calculations which would be made using the method advanced by Sun and that advanced by MMS. As a starting point we will set out the relevant text of 30 CFR 206.104 (1987), which was applicable at the time of the production:

Royalty rates on oil; sliding- and step-scale leases (public land only).

Sliding- and step-scale royalties are based on the average daily production per well. The Supervisor shall specify which wells on a leasehold are commercially productive, including in that category all wells, whether produced or not, for which the annual value of permissible production would be greater than the estimated reasonable annual lifting cost, but only wells which yield a commercial volume of production during at least part of the month shall be considered in ascertaining the average daily production per well. The average daily production per well for a lease is computed on the basis of a 28-, 29-, 30-
30-, or 31-day month (as the case may be), the number of wells on the leasehold counted as producing, and the gross production from the leasehold.

The following assumptions will be made in this example: (1) the month for which the royalty is to be calculated contains 30 days; (2) the lease contains 10 wells; (3) the total production from the wells was 15,000 barrels (bbl) of oil; (4) 4,500 bbls of oil were used on the lease; and (5) the oil was sold at $20/bbl.

We will now apply the regulation to the assumptions, first using the method urged by Sun, and then using the method urged by MMS:

Sun's calculation:

1. Average daily production per well:
\[
\frac{15,000 \text{ bbl} - 4,500 \text{ bbl}}{30 \text{ days} \times 10 \text{ wells}} = 3 \text{ bbl/well/day}
\]

2. Royalty at the various rates:

   A. At the 12\%\% royalty rate:
   \[
   20 \text{ bbl/day/well} \times 10 \text{ wells} \times 30 \text{ days} = 6,000 \text{ bbl.}
   \]
   \[
   6,000 \text{ bbl} \times $20/\text{bbl} \times 12\%\% = $15,000.00
   \]

   B. At the 14\%\% royalty rate:
   \[
   15 \text{ bbl/day/well} \times 10 \text{ wells} \times 30 \text{ days} = 4,500 \text{ bbl.}
   \]
   \[
   4,500 \text{ bbl} \times $20/\text{bbl} \times 14\%\% = $12,857.14
   \]

3. Total royalty due:
\[
$15,000.00 + $12,857.14 = $27,857.14
\]

MMS's calculation:

1. Average daily production per well:
\[
\frac{15,000 \text{ bbl}}{30 \text{ days} \times 10 \text{ wells}} = 50 \text{ bbl/well/day}
\]

2. Portion of oil consumed in production:
\[
\frac{4,500 \text{ bbl}}{15,000 \text{ bbl}} = 30\%
\]

3. Royalty at the various rates:

   A. At the 12\%\% royalty rate:
   
   i) total production:
   \[
   20 \text{ bbl/day/well} \times 10 \text{ wells} \times 30 \text{ days} = 6,000 \text{ bbl.}
   \]
   
   ii) production upon which royalty is assessed:
   \[
   6,000 \text{ bbl} - (6,000 \times 30\%) = 4,200 \text{ bbl}
   \]
   
   iii) royalty due:
   \[
   4,200 \text{ bbl} \times $20/\text{bbl} \times 12\%\% = $10,500
   \]

   B. At the 14\%\% royalty rate:
   
   i) Total production:
   \[
   30 \text{ bbl/day/well} \times 10 \text{ wells} \times 30 \text{ days} = 9,000 \text{ bbl.}
   \]
   
   ii) production upon which royalty is assessed:
   \[
   9,000 \text{ bbl} - (9,000 \times 30\%) = 6,300 \text{ bbl}
   \]
   
   iii) royalty due:
   \[
   6,300 \text{ bbl} \times $20/\text{bbl} \times 14\%\% = $18,000
   \]

4. Total royalty due:
\[
$10,500.00 + 18,000.00 = $28,500.
\]
As can be seen from the examples, the divergence of accounting procedures comes from Sun's deduction of the oil consumed on the lease prior to calculating the average daily production from the lease and MMS' calculation of the average daily production based on total production and subsequent pro-rata deduction of that portion consumed to each barrel of oil subsequently sold or removed. Sun argues that its method recognizes that there should be no royalty imposed on oil used on the lease and, therefore, the royalty calculation should be made as if the oil used on the lease had never been produced. On the other hand, MMS argues the same amount of oil is used to produce each barrel of oil subject to the 12-1/2 percent royalty as is used to produce the oil subject to the 14-2/7 percent royalty, and the pro-rata application of consumed oil recognizes this fact.

Both sides have cited a number of cases in support of their respective positions. However, we find none of these cases to be directly in point regarding the accounting procedure to be used when applying a sliding-scale or a step-scale royalty, when a portion of the oil produced had been used on the lease. To this extent this appears to be a case of first impression.

As noted above, in Amoco, supra, the Board stated that section 17 of the Mineral Leasing Act, as amended, 30 U.S.C. § 226(b) (1982), provides that royalty due the United States shall be computed at the rate fixed in the lease on the amount or value of production removed or sold from the lease. Both accounting procedures satisfy this requirement. The royalty is computed at the rate fixed in the lease, and is assessed against the amount or value of the production removed or sold from the lease. As can be seen from the examples, the amount of oil subject to a royalty is the same in each case (Sun: 6,000 bbl + 4,500 bbl = 10,500 bbl, and MMS: 4,200 bbl + 6,300 bbl = 10,500 bbl).

Neither accounting method assesses a royalty on the oil consumed during the process of production.

The initial question before us is whether a reasonable interpretation of the applicable regulations would allow the imposition of the MMS accounting procedure when determining the royalty for the oil sold or removed. Therefore, we will first examine the appropriate regulations to determine if they contain language which would permit the use of the MMS accounting method.

The regulation at 30 CFR 206.104 states that sliding-scale royalties “are based on the average daily production per well * * * . The average daily production per well for a lease is computed on the basis of * * * the gross production from the leasehold.” MMS focuses on the term “gross” with the conclusion that the average daily production calculation should include oil used on the lease. The MMS interpretation also complies with 30 CFR 206.104(i)(2), which states: “The average production per well per day is determined by dividing the total production of the leasehold by * * * the number of wells
* * *." See also 30 CFR 206.104(i)(1). The term "total production," as used in the regulations, can reasonably be interpreted to mean the total production from the wells before deducting the oil used on the lease. Thus, the regulations are subject to the interpretation advanced by MMS.

The August 13, 1987, decision is a statement of the Department’s accounting policy applicable to calculating royalties due under the regulation, and is within the language and purpose of the Act. It is, of course, within the authority of the Department to interpret its own regulations, and its interpretation should be given great deference. Udall v. Tallman, 380 U.S. 1, 16 (1965). This being the case, the policy of prorating oil used on the lease among the various applicable royalty rates, as stated in the August 13, 1987, decision, is neither arbitrary nor capricious, if applied to all lessees falling within this category.4

Throughout the briefs filed with this Board, Sun has couched the August 13, 1987, MMS royalty-rate determination as “new methodology.” At no place in the case file, the MMS decisions, or pleadings MMS has filed with this Board is there any indication that the methodology set out in the August 13, 1987, decision is an application of a longstanding accounting procedure. Rather, MMS addresses the issue in terms of its authority to enforce a public right or protect a public interest, which “is not ‘lost by acquiescence of its officers or by their laches, neglect of duty, failure to act, or delays in performance of their duties.’ Otay Mining Co., 62 IBLA 166, 168 (1982)” (Answer at 6).

We have no quarrel with the notion that MMS is not forever bound by its prior interpretation of a statute or regulation, even though that interpretation has been applied for a long time. If MMS determines that a different construction should be given, it is within MMS’ prerogative to apply the new construction, so long as it is "adequately explicated." See, e.g., NLRB v. Weingarten, Inc., 420 U.S. 251, 265-67 (1975); Brennan v. Gilles & Cotting, Inc., 504 F.2d 1255, 1264-66 (4th Cir. 1974). Our inquiry does not end here, however.

When MMS finds that a prior interpretation of its regulations was based upon a mistake of law it is entitled to retroactively correct that interpretation. However, it must clearly set forth and identify the mistake of law in sufficient detail to show that the departure from the prior administrative position is not arbitrary or capricious. See, e.g., Squaw Transit Co. v. United States, 574 F.2d 492 (10th Cir. 1978); FTC v. Crowther, 430 F.2d 514 (D.C. Cir. 1970); Issac & Katherine Bonaparte v. Commissioner of Indian Affairs, 9 IBIA 115, 122 (1981). When MMS departs from a prior administrative position and seeks to apply its new position retroactively, it is not enough to state that it has the right to do so. A mere showing that the new interpretation is within the meaning of the law is not sufficient to meet that burden of

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4 A parallel is suggested. The step-scale royalty is similar to the graduated-scale income tax, and the IRS approach to the deduction of business expenses is similar to the Sun royalty approach. If the IRS adopted the MMS approach, taxpayers now deducting business expense would be subject to increased tax liability.
clearly setting forth and identifying the mistake of law. If the prior interpretation is also within the meaning of the law, no mistake is established.\(^5\)

We will examine the appropriate regulations to determine if the regulatory language would also permit the use of the accounting method applied by Sun. As previously noted, 30 CFR 206.104 states that sliding-scale royalties "are based on the average daily production per well * * *. The average daily production per well for a lease is computed on the basis of * * * the gross production from the leasehold." Sun's interpretation focuses on the phrase "from the leasehold," which Sun interprets to mean removed or sold. Under this interpretation, the term "gross" would be synonymous with the term "sum of" and refer to all producing wells. Likewise, the term "total production" in the phrase "average production per well per day is determined by dividing the total production of the leasehold by * * * the number of wells * * *" in 30 CFR 206.104(i)(2) can be interpreted to mean the total production subject to a royalty. Thus, these regulations are also subject to the interpretation advanced by Sun.

Sun's interpretation conforms with the Geological Survey Conservation Division Manual (GS Manual). Part 647 of the GS Manual addresses issues of accounting. Chapter 13 of that part is entitled "Variable Royalty Rate and Well Count." Part 647, Chapter 13.3 provides: "In calculating a royalty rate, production and sales are generally considered to be the same thing, with the sales figures being used to calculate all royalty rates even though the word "production" may be used in this chapter."\(^6\) GS Manual, Part 647.13.3A (Release No. 26, July 5, 1974). When Part 647.13.3A is applied, the oil used on the lease is not sold, it need not be reported, and the accounting method advanced by Sun is clearly applicable.

After examining the provisions of Part 647.13 of the GS Manual, which was specifically written to provide "guidance and procedures for reviewing variable royalty rate * * * leases to ensure that royalties are properly computed,"\(^7\) it is our opinion that the GS Manual clearly "specified that a particular method of valuation adopted by a lessee [i.e., Sun] is adequate." Supron Energy Corp., 46 IBLA 181, 191 (1980), appeal filed sub nom. Supron Energy Corp. v. Hodel, Civ No. 80-0463 JB (D.N.M., June 18, 1980). There is also no question that Survey was applying this interpretation before, during, and after the period in question. When the lease was renewed, Schedule D (quoted above)

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\(^5\) When the decision fails to clearly set forth and identify the mistake of law in sufficient detail, it is proper for this Board to assume that the prior practice was also within the ambit of the statutes and regulations. All else appearing regular, administrative officials are presumed to have properly discharged their duties. H.S. Rademacher, 58 IBLA 152, 88 ID. 873 (1980), and cases cited therein.

\(^6\) The use of the term "production" in Chapter 13 parallels the language found in 43 CFR 221.49 (7 FR 4122 (June 2, 1942)). This statement is thus an interpretation of that regulation.

\(^7\) GS Manual, sec. 647.13.1.
became applicable as provided by Exhibit 3, Part 647.13.2G, of the GS Manual.

We now will consider whether Sun had relied upon MMS' acceptance of the accounting procedure used by Sun when calculating the royalty due on the oil production removed or sold from the lease. Sun calculated the royalty due on the basis set forth in the example above during the entire period in question, and states that it did so in reliance upon its belief that the Department had accepted Sun's method of calculating royalties in the 1970 and 1979 correspondence.

On February 4, 1970, the Regional Oil and Gas Supervisor for the Pacific Region of the Geological Survey (Survey) wrote the Accounting Supervisor of Sun in Tulsa concerning Sun's January 1969 Report of Sales and Royalty for this lease. At the time Survey's figures for the amount subject to royalty were lower than Sun's:

We began making inquiries into the matter, and through a phone call to your Mr. J. T. Gibson we learned that this oil (Code 50) was used on the lease. We contacted Mr. J. R. Hinkle, District Engineer in your Newhall, California, office, and by letter of September 26 he informed us that the oil was "consumed in firing the lease heater treater facilities only."

Early in October our District Engineer visited the Maxwell lease and confirmed that the oil was used on the lease for "royalty free" purposes. After obtaining all the facts, we realized that Sun-DX had paid royalty on lease oil for which royalty was not required.

Although your oil purchase statements continue to show Code 50 entries, we have not included them in our royalty calculations since we began to take our royalty in kind. In this regard, we suggest that you discontinue showing these items on your oil purchase statements. Since the oil is used on the lease and is not subject to royalty, you do not need to report the oil. If convenient, please make the change effective with your January 1970 statement. [Italics added.]

This letter confirms the Department's acceptance of the interpretation advanced by Sun, as it would be necessary to report the quantity of oil used on the lease under the interpretation set out in the August 13, 1987, decision. We believe that this correspondence and Sun's subsequent royalty reports, which conformed with the described procedure, are ample evidence that Sun relied upon the assurances that the oil should be accounted for in the manner outlined in the GS Manual. Indeed, there is nothing in the record reflecting any reservation about the aspect of Sun's royalty accounting now in question until the California audit.

MMS argues that the United States is not estopped from asserting prerogatives granted by regulatory authority. However, this is not a matter of estoppel. Rather, MMS has stated a new policy, which amended the Department's previous policy regarding the accounting procedure to be used for calculating a sliding-scale or step-scale royalty when a portion of the production is used on the lease. Having determined that both accounting procedures are within the scope of the regulation, we must now determine whether the accounting procedure set out in the August 13, 1987, decision can be retroactively applied to the oil produced during the audit period.
This case, like all cases of first impression, has a retroactive effect. See S.E.C. v. Chenery Corp., 332 U.S. 194, 203 (1947). In Runnells v. Andrus, 484 F.Supp. 1234 (D.C. Utah 1980), the court addressed whether an interpretive ruling by the Department would be given retroactive effect, and applied the balancing test set out in Retail, Wholesale & Department Store Union v. NLRB, 466 F.2d 380, 390 (D.C. Cir. 1972). We believe that the application of this test weighs in favor of Sun. There is no question that when MMS adopted the new accounting procedure in its decision, that decision was an abrupt departure from a well-established practice, and not an attempt to fill a void in an unsettled area of the law. The facts clearly demonstrate that Sun relied upon the prior interpretation during the entire audit period. The newly adopted accounting procedure clearly imposes an additional royalty burden on Sun. In Runnells, the court found that the prejudice to the plaintiffs substantially outweighed the statutory interest and purposes sought to be protected, and held that the rule announced below should be applied prospectively. Runnells v. Andrus, supra at 1240. The same rationale applies in this case. We therefore find that MMS has the authority to impose the accounting procedure for calculating royalties set out in the August 13, 1987, decision, but that this accounting procedure should be applied prospectively.8

In light of our findings, appellant's request for a hearing is denied. Accordingly, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision of the Acting Director, Minerals Management Service, is affirmed as modified.

R. W. MULLEN
Administrative Judge

I CONCUR:

WILL A. IRWIN
Administrative Judge

Appeal from a decision of the Director, Minerals Management Service, affirming assessment of additional royalty and late payment charges. MMS-85-0326-OCS and MMS-86-0096-OCS.

Affirmed in part, set aside in part, and remanded.

8 In reaching this conclusion we need not address whether the provisions of 28 U.S.C. § 2415 (1982), are applicable to a portion of the royalties MMS had found to be due and owing.
1. Federal Oil and Gas Royalty Management Act: Royalties—Oil and Gas Leases: Royalties: Payments—Outer Continental Shelf Lands Act: Oil and Gas Leases

A royalty payor who has been assigned the duty to make royalty payments for production from an oil and gas lease on behalf of co-lessees and who has notified MMS of acceptance of this responsibility by filing a payor information form may be held liable for royalties due under the terms of the lease.

2. Federal Oil and Gas Royalty Management Act: Royalties—Oil and Gas Leases: Royalties: Generally—Outer Continental Shelf Lands Act: Oil and Gas Leases

A decision issued to the payor after audit regarding valuation of natural gas produced from certain leases asserting the gas sold was not priced in accordance with the statutory ceiling price may be set aside and remanded where the record fails to indicate the affected lessees were apprised of the basis of the revised valuation and afforded an opportunity to respond as required by the lease terms.

3. Federal Oil and Gas Royalty Management Act: Royalties—Oil and Gas Leases: Royalties: Generally—Outer Continental Shelf Lands Act: Refunds

In the context of an appeal from a decision of MMS after audit assessing additional royalty on production from an oil and gas lease, the issue is what, if any, additional royalty is due and owing to the lessor. The Board adheres to its holding in Shell Oil Co., 52 IBLA 74 (1981), and Mobil Oil Corp., 65 IBLA 295 (1982), that where an audit is made of royalty payments for an oil and gas lease, underpayments disclosed by the audit are properly offset by royalty overpayments on the same lease revealed within the period of the audit.


OPINION BY ADMINISTRATIVE JUDGE GRANT

INTERIOR BOARD OF LAND APPEALS

Forest Oil Corp. (Forest) has brought this appeal from a decision of the Director, Minerals Management Service (MMS), dated January 30, 1987. In that decision, the Director affirmed the assessment of additional royalties and late payment charges on production from offshore oil and gas leases.

This case arose from an MMS audit of Forest's royalty payments on production from Federal oil and gas leases from January 1977 through December 1983. The scope of the audit included payments made by Forest in its own behalf as lessee and on behalf of other working interest owners as operator and agent. In a November 8, 1985, letter responding to appellant's comments on the February 1985 draft audit report, the Associate Director of the Royalty Management Program (RMP) confirmed the intent of MMS to hold appellant responsible for additional royalty payments due from other working interest owners as
well as the intent to require payment of royalties which were the subject of alleged unauthorized recoupments. Forest appealed this decision to the Director, MMS, where the case was docketed as MMS-85-0326-OCS.

Subsequently, as a result of the audit, the Lakewood Regional Compliance Office, RMP, MMS, billed Forest for additional royalties and late payment charges in the amount of $2,868,517.88 in an undated demand letter.¹ This demand for payment was appealed to the MMS Director under docket number MMS-86-0096-OCS.

In upholding the assessment of $2,595,925.71 in challenged offshore royalties and late payment charges,² the Director addressed two major issues. The first question is whether additional royalty is due because Forest improperly recouped royalty overpayments on offshore leases by entering an offsetting credit on subsequent monthly reports in violation of refund procedures mandated by section 10 of the Outer Continental Shelf Lands Act (OCSLA), 43 U.S.C. § 1339 (1982).³ The second issue is whether MMS may hold the payor of an offshore oil and gas lease responsible for payment of royalties attributable to the other working interest owners.

With respect to the recoupment of the royalty overpayments on subsequent monthly reports, the Director held that recoupment of an overpayment on an Outer Continental Shelf (OCS) lease through entries to Form MMS-2014 is barred in the absence of prior approval from MMS. The decision contended that a fully documented refund request must be filed in conformity with the requirements of section 10 within 2 years of the overpayment. The Director distinguished the decision in Shell Oil Co., 52 IBLA 74 (1981), upholding the offsetting of underpayments against overpayments discovered during the audit

¹ The only copy of the demand letter appearing in the file is attached to Forest's appeal to the Director. Although the letter is undated, Forest states that it received the demand letter on Jan. 14, 1986.
² The Director's decision indicated that of the $2,744,159.57 assessed for offshore leases, Forest paid $148,233.96 and appealed the balance of $2,595,925.71 (Director's Decision at 2). The assessment was itemized in the Director's decision as follows:

<table>
<thead>
<tr>
<th>Audit Report Finding</th>
<th>Description</th>
<th>Amount Appealed</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.a)</td>
<td>Disallowed Overpayment and Duplicate Payments</td>
<td>$1,273,254.73</td>
</tr>
<tr>
<td>1.b)</td>
<td>Incorrect Pricing</td>
<td>208,595.47</td>
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<tr>
<td>1.c)</td>
<td>Unreported Sales</td>
<td>81,901.19</td>
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<tr>
<td>1.d)</td>
<td>Incorrect Volumes</td>
<td>162,459.56</td>
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<tr>
<td>1.f)</td>
<td>Incorrect Value</td>
<td>20,851.93</td>
</tr>
<tr>
<td>6.a)</td>
<td>Late Payment Charge Analysis—Detailed Review</td>
<td>798,015.36</td>
</tr>
<tr>
<td>6.b)</td>
<td>Late Payment Charge Analysis—Estimated Gas</td>
<td>49,847.37</td>
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<tr>
<td></td>
<td></td>
<td>$2,595,925.71</td>
</tr>
</tbody>
</table>

³ Sec. 10(a) of OCSLA provides in pertinent part:

"When it appears to the satisfaction of the Secretary that any person has made a payment to the United States in connection with any lease under this subchapter in excess of the amount he was lawfully required to pay, such excess shall be repaid without interest to such person or his legal representative, if a request for repayment of such excess is filed with the Secretary within two years after making of the payment ***," 43 U.S.C. § 1339(a) (1982).
period where the audit was conducted more than 2 years after the date of the overpayments on the ground that the "2-year period had not run at the time Forest discovered the alleged overpayments" (Decision at 5). The Director found that the 2-year limit under section 10 applies to credits, including recoupments.

Regarding the contention of Forest that it should not be responsible for that portion of the royalty underpayments attributable to the interest of other lessees, the Director found that co-lessees are joint venturers and, as such, are properly held jointly and severally liable for the royalty obligation. The Director also held Forest was responsible as an agent for the other lessees in view of its completion of an MMS payor information form (PIF) and assumption of the duties of royalty payor. The Director noted that Forest was the designated operator of the Eugene Island Block 292 Unit and had fractional interests in unit leases. In support of his decision, the Director noted the obligation of Forest under section 8 of the Unit Agreement to pay all royalty on production of unitized substances for the leases to which the production was allocated. Hence, the Director concluded Forest had a contractual obligation to report and pay royalties on behalf of the other lessees.

Several major issues are raised in the statement of reasons for appeal filed by Forest. The first question is whether the royalty payor is liable for the royalty deficiencies of other lessees. Another critical issue raised is whether overpayments recouped by "adjustments" taken on Form MMS-2014 without prior approval for the purpose of reconciling royalty payments with actual production figures are properly recognized as an offset to underpayments of royalty disclosed by an audit. A related question is whether a recoupment taken on Form MMS-2014 without prior approval for the purpose of reconciling royalty payments with actual production may be considered as an application for refund of overpayments when such adjustments are taken on a lease-by-lease basis within the 2-year limitation period. Finally, appellant contends royalties are not properly based on the relevant Natural Gas Policy Act (NGPA) category ceiling price without regard to other factors.

Forest argues that there is no statutory support in either OCSLA or the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), 30 U.S.C. §§ 1701-1757 (1982), for holding the royalty "payor" liable for the royalty share of other working-interest owners where the other lessees have marketed their own gas and computed the royalties due on that gas. Appellant also asserts that it is not legally responsible for the royalty payments of the other lessees based on its status as "operator," apart from its role as "payor." Forest contends that the
Designation of Operator Form 9-1123 authorizes the operator to act as the agent of the lessee, but by its express terms neither constitutes an assignment of an interest in the lease nor relieves the lessee from liability for compliance with the terms of the lease. Further, appellant argues that holding the payor liable for the royalty underpayments of other lessees in circumstances such as these will cause lessees to refuse to assume the role of single payor for several lessees. Hence, Forest contends the principle of administrative convenience is not served by automatically holding the payor liable.

With regard to the issue of offsets or recoupments taken on Form MMS-2014, Forest contends the recoupments are not an attempt to subvert the refund procedures under OCSLA, but, rather, are adjustments to royalty payments consistent with the Board’s decision in Shell Oil Co., supra. Forest asserts that the fact that the overpayments were discovered within 2 years, in time for filing a refund application under OCSLA, does not distinguish this case from Shell because the adjusting underpayments were made within 2 years of the overpayment in both cases and the subsequent audits revealed only that the Department had not accepted the use of the adjustment procedures. Appellant contends there is no viable distinction between offset and recoupment in this context. In the alternative, Forest argues that it has already applied for refund of royalty overpayments through the adjustments claimed on Form MMS-2014 which detailed in writing the lessee, the amount of any overpayment offset, and the lease to which the offset was applicable. Forest asserts these recoupments were filed within 2 years of the overpayment, thus qualifying for consideration as timely applications for a refund.

Finally, appellant challenges the assertion in the audit report of the right to calculate royalty on the NGPA ceiling price without regard to the price received by the lessee under arm’s-length sales contracts. Forest asserts that royalty is ordinarily calculated on the basis of the price received by the lessee in the absence of special circumstances, which do not exist in this case.

In answer to Forest’s statement of reasons for appeal, MMS contends before the Board that appellant’s recoupment of royalty overpayments by taking offsets on subsequently filed monthly reports (Form MMS-2014) without MMS approval violated section 10 of OCSLA, 43 U.S.C. § 1339 (1982), governing refunds of overpayments. MMS contends that Forest is not entitled to claim offsets for the overpayments involved because, unlike the situation in Shell Oil Co., supra, the overpayments were discovered within 2 years when an application for refund was still an available remedy.5 MMS argues that the recognition of offsets for

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5 Thus, MMS disagrees with appellant’s understanding of the factual context of the Shell case and asserts that the lessee in Shell was not aware of the overpayment until the audit when the underpayment was disclosed, well after the lapse of time in which to file a refund request.
underpayments and overpayments within the audit period which have been disclosed by an audit conducted after the close of the period for filing a refund request "does not authorize unilateral credit adjustments for recoupments."

Regarding the liability of Forest for the royalty obligation of other lessees, MMS notes that appellant was the operator for the leases at issue and cites the portion of the unit agreement in the file, cited in the Director's decision, providing that royalty shall be paid by the unit operator. MMS asserts that this responsibility for royalty payment qualifies Forest as a "lessee" under the definition in section 3 of FOGRMA, 30 U.S.C. § 1702(7) (1982), embracing persons assigned the obligation to make royalty payments under the lease. In further support of its conclusion, MMS has cited several Federal court opinions involving Department of Energy crude oil pricing regulations and Federal Power Commission regulations where the operator was held responsible without resort to all of the different lessees. Further, MMS argues that appellant assumed the responsibility to make royalty payments for the other lessees when it filed a PIF with MMS and was assigned a payor code number, thus assuming the status of a payor.

With respect to appellant's assertion of error regarding the assessment of royalty on the basis of the NGPA ceiling price without regard to the price received by the lessee in arm's-length sales, MMS contends Forest is precluded from raising this argument before the Board by the failure to raise the issue before the Director. MMS further asserts that Forest paid its share of the assessment relating to this issue, citing an MMS Field Report dated May 19, 1986, for docket number MMS-86-0096-OCS.6 In any event, MMS argues that royalty valuation is not necessarily limited to the actual proceeds received and that the regulated price is a relevant factor under the royalty valuation regulation. Finally, MMS contends Forest is responsible for the late payment charges in connection with the additional royalties assessed.

[1] The issue of the liability of the royalty payor for the share of royalty due on production attributable to the interests of other lessees is a matter of first impression before this Board. The lessee, as the owner of the working interest in production, is liable to the lessor under the terms of the lease contract for the royalty on oil and gas produced.7 The same is true of any approved assignee of a record title interest in the lease. It appears from the record that appellant shared a working interest in each of the leases with other lessees and, further, that appellant had assumed the responsibility of making royalty

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6 A search of the record submitted to the Board has failed to disclose a copy of the cited document. Even if it is assumed that Forest has paid its share of this item of the royalty assessment, the asserted liability of Forest for the share of the other lessees would preclude dismissal of this issue for mootness.

7 Further, a lessee may designate an operator to act for the lessee in matters relating to lease operations, but this does not relieve the lessee of liability for royalty due on production in the event of default by the operator. Jerry Chambers Exploration Co., 107 IBLA 161 (1989).
payments for the co-lessees pursuant to the unit agreement.\(^8\) Offshore oil and gas unit agreements are generally required to conform to a model unit agreement. 30 CFR 250.192(b); 250.193(a). Under the terms of the model unit agreement, the operator is required to pay production royalties. 30 CFR 250.194. In order to fulfill this responsibility for making the royalty payments, appellant filed a PIF with MMS. Thus, the question is whether appellant’s assumption of the status of royalty payor is sufficient to impart liability for royalty due on behalf of other working interest owners.

In resolving this issue we find certain statutory provisions relevant. Under section 3 of FOGRMA, the term “lessee” is defined to include “any person to whom the United States, an Indian tribe, or an Indian allottee, issues a lease, or any person who has been assigned an obligation to make royalty or other payments required by the lease.” 30 U.S.C. § 1702(7) (1982) (italics added).\(^9\) Section 102 of FOGRMA provides that:

A lessee—(1) who is required to make any royalty or other payment under a lease * * * shall make such payments in the time and manner as may be specified by the Secretary; and (2) shall notify the Secretary, in the time and manner as may be specified by the Secretary, of any assignment the lessee may have made of the obligation to make any royalty or other payment under a lease * * *.

30 U.S.C. § 1712(a) (1982). The implementing regulation provides that MMS must be notified within 30 days when the lessee or revenue payor assigns any responsibility for payment to any other entity. 30 CFR 218.52(a).

MMS utilizes the PIF for this purpose: “The PIF is used to transmit lease and payor information to the Minerals Management Service (MMS). * * * MMS uses the PIF information to establish and maintain the lease and payor accounts required for monthly Report of Sales and Royalty Remittance (Form MMS-2014) reporting.” 1 MMS, Royalty Management Program, Oil and Gas Payor Handbook § 2.3 (1987).

Regarding those events which require filing a PIF, MMS has provided:

A PIF must be filed for each Federal or Indian lease on which royalties * * * are paid to the AFS [Auditing and Financial System]. The payor is required to submit a PIF to establish or revise royalty and rental payment responsibility. Generally, an initial or revised PIF is required when physical, contractual, and operational events occur or conditions are revised regarding a lease, its subdivisions, or its payment responsibilities.

An initial PIF is required to establish reporting and paying responsibilities and a revised PIF is required when data change on any PIF.

Id. at § 2.4.

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\(^{8}\) A copy of the Eugene Island Block 292 Unit Agreement, approved by the Department May 4, 1966, appears in the case file. The agreement provides at sec. 4 that “Forest Oil Corporation is hereby designated as Unit Operator, and * * * agrees and consents to accept the duties and obligations of Unit Operator, for the discovery, development and production of Unitized Substances * * *.” Further, sec. 8 of the Unit Agreement regarding royalties on unitized substances produced from the leases provides that “royalty shall be paid by the Unit Operator.”

\(^{9}\) One of the express purposes of FOGRMA was “to clarify, reaffirm, expand, and define the responsibilities and obligations of lessees, operators, and other persons involved in transportation or sale of oil and gas from the * * * Outer Continental Shelf.” 30 U.S.C. § 1701(b) (1982).
Although appellant is the agent of the co-lessees for purposes of payment of royalty due on their share of production, we find it inappropriate in the circumstances to allow appellant to deny liability on the ground it is merely an agent for the working interest owners. As unit operator it signed the agreement as a principal. Indeed, the unit operator is in a unique position to know what is produced from a lease and what is delivered for sale as this is its responsibility. Notwithstanding appellant’s lack of knowledge of the terms under which production was marketed by the co-lessees, it has access to other information critical to determining the amount of royalty due. Thus, we find that appellant as unit operator and payor was assigned and accepted the responsibility of making royalty payments for its co-lessees and notified the Department of this fact both in submitting the unit agreement and in filing the appropriate PIF. In this context, we must affirm the liability of the operator/payor for the royalty on the share of production attributable to the other working interests. Although this conclusion is strengthened by cited provisions of FOGRMA and regulations and procedures implementing this Act, we find this result to be consistent with the obligations assumed by the unit operator acting as payor prior to FOGRMA.\[^2\]

[2] With respect to the issue of liability for additional royalty on the basis that certain gas sold was not priced in accordance with the NGPA ceiling price, we note that this issue was not addressed by the Director’s decision. We are unable to accept the contention of MMS on appeal that appellant waived this issue on the ground it was not raised before the Director. The issue of liability for incorrectly priced gas is raised in appellant’s November 22, 1985, appeal letter addressed to the Director, MMS, in MMS-85-0326-OCS. One element of appellant’s argument regarding liability for royalty owed by co-lessees is the lack of information it had with respect to the sale price obtained by co-lessees who marketed their own share of the production. Indeed, where MMS elects to hold the payor liable, the adequacy of notice to the lessees of the valuation of production for royalty purposes becomes an issue. Section 2(d) of the OCS leases in the record provides that:

(2) It is expressly agreed that the Secretary may establish reasonable minimum values for purposes of computing royalty on products obtained from this lease, due consideration being given to the highest price paid for a part or for a majority of production of like quality in the same field, or area, to the price received by the lessee, to posted prices, and to other relevant matters. Each such determination shall be made only after due notice to the lessee and a reasonable opportunity has been afforded the lessee to be heard. [Italics added.]\[^11\]

\[^10\] The legislative history of FOGRMA indicates that the Act was not perceived to grant "the Secretary new authority to designate a 'principal payor' i.e., a single payor legally obligated to make payment for any royalty obligation on a lease." Rather, "The Committee is allowing the Secretary the discretion to determine under existing authority of law which person (i.e., lessee, interest holder, operator, etc.) is responsible for making royalty payments to the United States." H.R. Rep. No. 859, 97th Cong., 2nd Sess. 28, reprinted in 1982 U.S. Code Cong. & Admin. News 4268, 4282.

\[^11\] In this regard, section 14 of the Eugene Island Block 292 Unit Agreement provides that the Unit Operator shall, "after notice to other parties affected, have the right to appear for and on behalf of any and all interests affected hereby before the Department of the Interior, and to appeal from orders issued under the regulations of said Department * * * provided, however, that any interested party shall also have the right * * * to be heard in any such proceeding." See 30 CFR 250.194 (model unit agreement).
It is not clear from the record that MMS notified the lessees other than appellant of the royalty valuation determination made in the audit. Hence, we set aside and remand the Director's decision to the extent it affirmed the royalty assessment on the basis of incorrect pricing to allow appellant and the other lessees to respond to the findings regarding valuation of production.

[3] With respect to the overpayments of royalty which were the subject of the subsequent alleged unauthorized recoupments taken by appellant on Form MMS-2014, we believe the precedents established in Mobil Oil Corp., 65 IBLA 295 (1982), and Shell Oil Co., supra, are relevant. In the lead case, Shell Oil Co., we dealt with the question of whether, in the circumstances of an audit of royalty payments on a lease account, overpayments disclosed in the audit may be allowed as an offset to underpayments disclosed in the audit notwithstanding the fact that the audit was conducted more than 2 years after the overpayment so that a refund would be barred by the terms of section 10 of OCSLA. The Board answered the question in the affirmative:

Had Shell initiated a request in 1979 for a refund of its November 1974 overpayment, we believe Survey [10] would have been correct in denying such request as untimely. In Phillips Petroleum Co., 39 IBLA 393 (1979), we so held. Where, however, Survey undertakes to audit a producer some 4 years after the payments at issue have been made, we hold that a sense of fundamental fairness requires Survey to recognize both a producer's underpayments and overpayments of royalty. We believe Survey should have properly offset Shell's underpayment by the amount of its overpayment. We do not believe that the 2-year period of limitations was established to give Survey a procedural advantage in computing royalty payments.

52 IBLA at 78. This precedent was further developed in Mobil Oil Corp., supra.

In the Mobil case the asserted overpayments which appellant sought to offset were discovered by the lessee rather than by Survey in the audit. The Board found this distinction immaterial: "The question then, is not whether the statute bars refunds or credits, but whether—assuming overpayments occurred—Survey should have recognized and offset these in the same audit period in which it discovered and assessed underpayment." 65 IBLA at 304. The Board answered this question in the affirmative and remanded the case to allow Survey to determine the extent of any allowable offsets. The scope of our holding was defined further by the concurring opinion wherein we recognized the past practice of permitting offsets and declined to invalidate this past practice:

It is true that, in the past, Survey has permitted the off-setting of overpayments in one month by deductions from subsequent payments in future months. Our decision herein does not invalidate this practice. It does, however, properly limit it to the 2-year period

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mandated by 43 U.S.C. § 1339(a) (1976). In other words, where a lessee made royalty payments for any month in excess of that required by law, the excess may be deducted from future royalty payments provided that the excess payment occurred within 2 years of the future payment. Where, however, an excess payment has not been discovered within this 2-year period, such payment may not be recouped by diminution of future payments owing from production in the lease. Indeed, allowance of such deduction would be directly contrary to the 2-year limitation on refunds which Congress has expressly imposed. [Italics in original; footnote omitted.]

65 IBLA at 305-06 (Burski, A.J., concurring). Subsequently, MMS issued the Oil and Gas Payor Handbook referred to previously. Effective August 1, 1983, the Handbook was amended to specifically provide that a “payor cannot recoup an overpayment on an OCS lease through entries to Form MMS-2014 without receiving prior approval from MMS.” Payor Handbook Addendum No. 4, page 3 of 5 (July 1983); see 2 MMS, Royalty Management Program, Oil and Gas Payor Handbook § 4.4.2 (1986). In the absence of an MMS audit, the Board has upheld MMS decisions applying this provision to disallow recoupments of overpayments on Form MMS-2014 without prior authorization. E.g., Mesa Petroleum Co., 107 IBLA 184 (1989); Kerr-McGee Corp., 103 IBLA 338 (1988). However, the appeal in this case is filed from a decision after audit refusing to consider the overpayments which were the subject of the recoupments as an offset to underpayments disclosed by the audit rather than from a decision disallowing an unauthorized recoupment. In the context of the appeal of the audit the issue is what, if any, additional royalty is due the lessor. Accordingly, we find it necessary to set aside and remand the Director's decision for further consideration of those overpayments which may offset the underpayments at issue.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision of the Director, Minerals Management Service, is affirmed in part, set aside in part, and remanded for further action pursuant to this decision.

C. Randall Grant, Jr.  
Administrative Judge

I concur:

Gail M. Frazier  
Administrative Judge

13 The concurring opinion also found that offsetting can only be allowed within the context of a single lease. 65 IBLA at 306. This finding has been upheld by the Board in subsequent cases. E.g., Mobil Oil Exploration & Producing, S.E., 104 IBLA 399, 401 (1988).

14 Indeed almost the entire audit period preceded the August 1983 effective date of the Handbook change. The prior practice, as noted in the Mobil concurring opinion, was to allow recoupment.

15 In this regard, the present case is distinguishable from those involving an assessment for erroneous reporting or a civil penalty for failure to properly pay royalty when due.
Judicial Review: Generally—Water and Water Rights: Reclamation Projects: Filings by United States

When it becomes necessary to protect the water supply of a Federal reclamation project, the United States is obligated and entitled to make filings in general stream adjudications on behalf of project water rights to which the United States holds legal title.

The United States is not obligated to make water rights filings or present evidence of beneficial use on behalf of individual water users. In addition, when the United States files in general stream adjudications in states that do not distinguish between storage rights and rights to receive water, it has no evidentiary burden to carry for the individual water users. However, by making the filings of reclamation project water rights held in its name, the United States protects its interest in the project water rights, and the project water users are afforded the opportunity to protect their water rights, based on their ability to establish beneficial use of water.

To: Secretary

From: Solicitor

Subject: Filing of Claims for Water Rights in General Stream Adjudications

We have been requested to address the question of what obligations, if any, the United States has to file water right claims on behalf of reclamation project water users in state court general stream adjudications. Several such adjudications have been initiated in various western states to adjudicate the water rights of water users on both major and minor river systems. The United States has been joined as a party to these adjudications pursuant to the provisions of the McCarran Amendment, 43 U.S.C. § 666 (1982). In virtually all of these adjudications, the United States holds title to water rights obtained under state law pursuant to the Reclamation Act of 1902, as amended, 43 U.S.C. § 372, 383.

We conclude that while the United States is obligated and certainly entitled to make filings in general stream adjudications on behalf of project water rights to which the United States holds legal title, we find no mandate in the statutes or case law that would require the United States to make filings or present evidence of beneficial use on behalf of individual water users.

We begin our discussion with an overview of water rights generally and specifically with respect to reclamation projects. We then outline

*Not in chronological order.
the nature of project water rights and finish with a discussion of what obligations rest upon the United States with respect to these rights.

I. Water Rights in General

The right of western states to regulate the allocation and use of non-navigable waters flowing within their boundaries has been recognized by the Supreme Court. See, e.g., California Oregon Power Co. v. Beaver Portland Cement Co., 295 U.S. 142 (1935); California v. United States, 438 U.S. 645 (1978). Because most of the western lands acquired by the United States through purchase and treaty were arid, there developed a system for allocating rights to the use of water which is known as the prior appropriation doctrine.¹

Although procedural differences exist, there are basic elements common to all appropriation systems employed in the western states. First, water traditionally had to be diverted from the natural flow and applied to a beneficial use, such as irrigation.² States use the concept of beneficial use to measure the extent of the right acquired under the prior appropriation doctrine; one is entitled to receive only that amount of water that is actually put to a use that is recognized as “beneficial” by the state.

Second, the first person using the water has the better right to it, i.e., first in time, first in right. Because the amount of water actually available for beneficial use will naturally vary from year-to-year, the priority principle dictates that when there is not enough water to satisfy all rights, cutbacks must be made starting with the most junior (recent) rights and proceeding in inverse chronological order through those with earlier priorities toward those which are most senior (oldest). Under this system, the full extent of any prior right must be satisfied before any water may be used by those holding junior rights.

Appropriate water rights can also be associated with the right to store water. With the development of water distribution systems, discussed below, came also the advent of reservoir storage capacity. By using upstream reservoirs, spring runoffs could be captured and stored for late-season use when unregulated flows were low, and carried over from years of high runoff to mitigate deficiencies of years with low rainfall.

Three methods have developed in the West to integrate into the prior appropriation system rights to store water.³ In a majority of states, a unitary permitting procedure exists whereby one obtains a water right; no distinction is made between water rights granted to divert direct flow and those that incorporate the right to store water for later delivery. In these states, when a distributor seeks to develop facilities

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¹ For a complete description of the appropriate water rights system, see 1 Clark, Waters and Water Rights 74-175 (1967), and 1 Hutchins, Water Rights Laws in the Nineteen Western States (1971) (hereinafter Hutchins).
² Some states recognize instream beneficial uses not requiring a diversion.
³ For an extensive discussion of storage rights, see Hutchins at 348-65.
to store water for delivery, the application will describe the location and capacity of the proposed storage facilities, periods of impounding and release from storage and the beneficial uses to which the water will be put. As approved, this information is then incorporated into the final permit, which is issued by the state in the name of the distributor.

An important aspect of this type of storage right is the fact that, unlike the dual permitting systems described below, there is generally no separate formal record of ownership issued by the state to the water users putting the water received from the storage facilities to beneficial use. Rather, the single "paper" right issued by the state is exclusively with the distributor. Because it is these water users and not the distributor who actually put the water to a beneficial use as required by state law, various court cases and in some instances state legislative actions have recognized that the water users are entitled to a perpetual right to receive the amount put to beneficial use; this right is in addition to any contractual rights the water users have with the distributor who holds legal title to the state water right. In states employing this system, the Federal Government holds several such water rights which are issued in the name of the United States and do not separately indicate any interest in the water right in the individual water users.

A smaller group of states provide for separate but complimentary procedures. To obtain storage rights, the distributor receives what is called a "primary permit" which is subject to the general requirements for appropriation except that it is exempted from specifically stating to what beneficial use the water will be put. One who wishes to apply to receive and put to beneficial use the water so stored files an application for a "secondary permit." This application presents evidence that an agreement has been entered into with the reservoir owner for a permanent interest in receiving water stored in the reservoir. Once water has actually been put to a beneficial use, the holder of the secondary permit submits evidence to that effect. The final certificate of appropriation refers to both the conveyance of water to the lands described in the secondary permit and the reservoir described in the primary permit. See, e.g., Wyo. Stat. § 41-3-303; Wyo. State Engineering Reg. Part I, Ch. 3, Sec. 3 (1974).

Finally, Colorado water law has recognized appropriations of two classes: (1) one for diversion of water for immediate application to a particular beneficial use, and (2) the other for storage of water to be used subsequently. Colorado courts have held that an appropriation of water for one of these functions was not an appropriation for the other. City & County of Denver v. Northern Colorado Water Cons. Dist., 130 Colo. 375, 276 P.2d 992 (1954).
II. Water Right Granted Under State Law to the United States Pursuant to Section 8 of the Reclamation Act

A. History of the Water Rights Obtained by Water Distributors

Using rudimentary diversion systems, the earliest settlers in the West appropriated water to irrigate the lowlands immediately adjacent to rivers and streams. However, it soon became apparent that while sufficient water existed to put more lands under cultivation, significant capital expenditures would be necessary to bring water to irrigable nonriparian land. To the extent it was able, private enterprise in the late 19th century became involved in the form of land and water companies or canal companies, whereby private developers would purchase arid lands and construct the diversion, storage, and transportation facilities necessary to irrigate them. Once water was ready for delivery, the company would divide the land and sell to farmers who would then contract with the company to have water delivered for irrigation.

States initially recognized the company as the appropriator of the water and the owner of the water right, “since the appropriation of water for sale or rental was recognized [as a beneficial use] by the laws of the time.” Trelease, Reclamation Water Rights, 32 Rocky Mountain Law Review 464, 475 (1960). Under this arrangement, the farmer was seen as having only a contractual right to receive water, and the water delivery company often had complete control over water delivery. Id.

To alleviate abuses which arose under the water delivery company scheme, such as when a company would threaten cutoff of water supply to obtain higher payments, corrective legislation and court decisions in the various western states gave to the water user “[a] form of a state water right, a property right independent of and superior to the contract right he had from the company.” Id. at 476. States continued, however, to recognize in the company the right to protect rights to the water it delivered against outside interests. Accordingly, once the states undertook to protect the water user's interest, “[t]he upshot . . . was that in most states, in external relationships between the project and other claimants to the water, the distributor was regarded as 'the proprietor of the appropriation,’ but internally, between the distributor and the consumer, the consumer had property rights that the courts would protect from arbitrary action by the distributor.” Id.

B. Obtaining Reclamation Project Water Rights

Although private capital and to some extent state-sponsored water delivery projects partially met the demand for irrigation, it became apparent that there was a role for the Federal Government in this effort. “With the passage of the Reclamation Act of 1902, 32 Stat. 388, the Federal Government was designated to play a more prominent role in the development of the West. That Act directed the Secretary of the Interior to withdraw from public entry arid lands in specified Western
States, reclaim the lands through irrigation projects, and then to restore the lands to entry pursuant to the homestead laws and certain conditions imposed by the Act itself.” *Nevada v. United States*, 463 U.S. 110, 115 (1983).

In *Nevada v. United States*, the Supreme Court observed that “Congress in its wisdom, when it enacted the Reclamation Act of 1902, required the Secretary of the Interior to assume substantial obligations with respect to the reclamation of arid lands in the western part of the United States.” 463 U.S. at 1281, and specifically noted that Congress had imposed “upon the United States . . . a duty to obtain water rights for reclamation projects . . .” 463 U.S. at 142. Such rights are obtained pursuant to state law, as required by section 8 of the 1902 Reclamation Act. *See California v. United States*, 438 U.S. 664 (1978). Section 8 provides:

Nothing in this act shall be construed as affecting or intended to affect or to in any way interfere with the laws of any State or Territory relating to the control, appropriation, use, or distribution of water used in irrigation, or any vested right acquired thereunder, and the Secretary of the Interior, in carrying out the provisions of this act, shall proceed in conformity with such laws, and nothing herein shall in any way affect any right of any State or of the Federal Government or of any landowner, appropriator, or user of water in, to or from an interstate stream or the waters thereof: *Provided*, That the right to the use of water acquired under the provisions of this act shall be appurtenant to the land irrigated and beneficial use shall be the basis, the measure, and the limit of the right.


Pursuant to the mandate of section 8, the Bureau has customarily obtained water rights for reclamation projects by making application to the appropriate state agency which in turn would generally grant a single water right for the entire project in the name of the United States. The Bureau, upon completion of the project works, would then deliver water to users for beneficial use within the project boundaries.

C. Water Users’ Interest in the Project Water Right

The Supreme Court has determined that for water rights obtained by the Bureau in the name of the United States, the water user who puts the project water to beneficial use obtains a vested property interest in the water right. In the initial Supreme Court case to address the nature of the water rights obtained by water users in connection with reclamation projects, *Ickes v. Fox*, 300 U.S. 82 (1936), the Court had before it a dispute between the Federal Government and a water users’ association supplied by the Yakima Project in Washington. These two parties had initially agreed that the Bureau would deliver 4.84-acre feet-per-irrigable-acre in exchange for repayment of specified project.

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4 The Bureau also obtained water rights from those who had appropriated water for use on lands that ultimately were included within project boundaries prior to authorization of the project. In some instances, project water rights are not held in the name of the United States.
construction, operation, and maintenance costs, with the United States holding liens on the water users' land and water rights to the extent of those repayment obligations. 300 U.S. at 89-91. The agreed-upon amount of water had been delivered to the water users for more than two decades when the Secretary of the Interior unilaterally issued an order limiting the water users' rights to 3-acre feet-per-acre with a rental charge for any additional water.

Arguing that they had historically put to beneficial use the 4.84-acre feet of water they had initially contracted to receive, the water users claimed they owned vested water rights in that amount of water and brought suit to restrain enforcement of the Secretarial order. 300 U.S. at 91-92. The United States argued that it had, in compliance with section 8, properly appropriated the project water rights pursuant to Washington law and therefore owned the water it diverted, stored, and distributed for the project. The water users, the United States asserted, had "no property rights in the water from its use, but merely their contract rights against the distributor." 300 U.S. at 84.

In oft-quoted language, the Supreme Court rejected the Government's arguments:

Although the government diverted, stored and distributed the water, the contention of petitioner that thereby ownership of the water or water-rights became vested in the United States is not well founded. Appropriation was made not for the use of the government, but, under the Reclamation Act, for the use of the land owners; and by the terms of the law and of the contract already referred to, the water-rights became the property of the land owners, wholly distinct from the property right of the government in the irrigation works. The government was and remained simply a carrier and distributor of the water with the right to receive the sums stipulated in the contracts as reimbursement for the cost of construction and annual charges for operation and maintenance of the works. As security therefor, it was provided that the government should have a lien thereto—a provision which in itself imports that the water-rights belong to another than the lienor, that is to say, to the landowner.

300 U.S. at 94-95 (citations omitted).

Since Ickes v. Fox, the principle that the proprietary interest in the project water right is in the project water users who put the water to beneficial use has been reaffirmed by the Supreme Court on two occasions. In Nebraska v. Wyoming, 325 U.S. 589 (1945), the Court, after quoting the passage from Ickes v. Fox quoted above, found that individual landowners who had put the project water to beneficial use, thereby "perfectiong" the water right obtained by the United States, had "become the appropriators of the water rights, the United States being the storer and the carrier." 325 U.S. at 615.

Finally, in Nevada v. United States, supra, the Supreme Court addressed Government arguments that water decreed to the United States for the Newlands reclamation project in Nevada could be reallocated to an Indian reservation. The Court, after quoting from Ickes v. Fox and Nebraska v. Wyoming, stated:
In the light of these cases, we conclude that the Government is completely mistaken if it believes that the water rights confirmed to it by the Orr Ditch decree in 1944 for use in irrigating lands within the Newlands Reclamation Project were like so many bushels of wheat, to be bartered, sold, or shifted about as the Government might see fit. Once these lands were acquired by settlers in the Project, the Government’s “ownership” of the water rights was most nominal; the beneficial interest in the rights confirmed to the Government resided in the owners of the land within the Project to which these water rights became appurtenant upon the application of Project water to the land.

463 U.S. at 126.

With the issuance of *Nevada v. United States*, the Supreme Court, conclusively reaffirmed the concept that beneficial ownership of a reclamation project water right is in the water users who put the water to beneficial use.\(^5\)

D. Government’s Interest in Project Water Rights

At first glance, the pronouncements of the Supreme Court in *Ickes* and *Nebraska* would appear to indicate that upon application by water users of project waters to beneficial uses, all interests incident to the water right flow to the project water users. However, as pointed out in *Nebraska v. United States*, these cases “discuss[] the beneficial ownership of water rights in irrigation projects built pursuant to the Reclamation Act.” 463 U.S. at 123. *Nevada* likewise clarifies that where project water rights are obtained by and remain in the name of the United States, the Federal Government retains legal title. Id. at 128. This point is important because the Court in *Nevada* speaks of “obligations that necessarily devolve upon [the United States] from having mere title to water rights . . .” Id. at 127. We next address some of the implications of holding legal title to project water rights.

III. Obligations of the United States With Respect to Project Water Rights

A. Obligation to Obtain and Protect Project Water

In *Nevada v. United States, supra*, the Supreme Court emphasized that “Congress in its wisdom, when it enacted the Reclamation Act of 1902, required the Secretary of the Interior to assume substantial obligations with respect to the reclamation of arid lands in the western part of the United States.” Id. at 128. We have been asked to determine whether the obligations alluded to by the Supreme Court in the above statement extend to filing of water rights claims on behalf of project water users in state general stream adjudications.

First, it appears clear that the Court in *Nevada* was referring to the obligation of this Department to obtain necessary water rights for authorized projects pursuant to section 8. The Court, in reviewing the dual responsibilities that Congress placed upon the Secretary to

\(^5\) However, none of the cases discussed herein should be read to restrict the right of the Secretary to enforce Federal reclamation or other applicable law with respect to project water users.
represent Indian interests and also obtain project water rights, stated: "... Congress has imposed upon the United States in addition to its duty to represent Indian tribes, a duty to obtain water rights for reclamation projects ..." Id. at 143. See also id. at 128. ("The Government does not 'compromise' its obligation to one interest that Congress obliges it to represent by the mere fact that it simultaneously performs another task for another interest that Congress has obligated it by statute to do.")

Beyond the obligation to obtain water, we also find support in Nevada for the proposition that the United States is obligated at least to do what is necessary to preserve, maintain, protect, or have confirmed project water rights that are held in the name of the United States. While less explicit than the obligation to obtain initially the water right, we believe the Court's further discussion of the United States' general obligations to deliver water to the beneficial owners of project water rights indicates this result. In Nevada, the Court specifically held that the Government could not reallocate project water in a manner that would impair its obligation as legal titleholder to deliver project water to project beneficiaries; it did not have occasion to also address the question of whether there is an affirmative duty to act to protect the right to that water. We believe, however, that the filing of project water rights by the United States in a general stream adjudication is the necessary means by which the United States must protect the ability of the project to deliver or store water, and thereby meet the mandatory obligation as enunciated by the Supreme Court to maintain appropriate deliveries of water to beneficial owners.

The Federal Government opened its brief in Nevada by stating: "The court of appeals has simply permitted a reallocation of the water decreed in Orr Ditch to a single party—the United States—from reclamation uses to a Reservation use with an earlier priority." Brief for United States at 21, as quoted in Nevada v. United States, supra at 121. In rejecting the Government's position, the Court pointed out that the argument that water decreed to the United States in the Orr Ditch decree for project purposes could be reallocated away from those purposes "seems wholly to ignore ... the obligations that necessarily devolve upon [the United States] from having mere title to water rights for the Newlands Project, when the beneficial ownership of these water rights resides elsewhere." 463 U.S. at 127. Thus, in attempting to reallocate water away from the project, the Federal Government was ignoring and failing to meet its obligation, as titleholder of the project water right, to maintain the project water supply in the amount which had previously been decreed to the project and to which the water users had acquired the beneficial ownership.

Commencing with the Court's holding that the United States as legal titleholder has a responsibility to maintain project water supplies, we believe it follows that the United States would further be obligated to
take any steps necessary to protect its ability to meet that responsibility. Turning to the issue of what filings should be made in general stream adjudications, the question then becomes, in those cases where the United States is legal titleholder to a project water right, what actions is the United States obligated to take in the adjudication to protect its ability to deliver water to the beneficial owners. Given that the purpose of a general stream adjudication is to determine and correlate all existing water rights within the adjudicated drainage basin, we note that there is perhaps no other context in which it is more important that the United States take those steps necessary to protect the full scope of the project’s water right, including the filing of claims held in the name of the United States.

We also point out that in cases decided before and after Ickes v. Fox, supra, courts have recognized that the United States, as distributor and as holder of legal title, has an interest in protecting project water rights for the benefit of the project as a whole. Thus, regardless of whether an obligation to file on project water rights can be found to exist, the Government clearly is entitled to make such filings.

Addressing the right to protect project water interests, the Supreme Court in Ide v. United States, 263 U.S. 497 (1924), reviewed arguments of non-project landowners that they, and not the Bureau, were entitled to project runoff. The Court found for the Government, stating:

In disposing of the lands in small parcels, the [United States] invests each purchaser with a right to have enough water supplied from the project canals to irrigate his land, but it does not give up all control over the water or do more than pass to the purchaser a right to use the water so far as may be necessary in properly cultivating his land. Beyond this all rights incident to the appropriation are retained by the [United States].

Id. at 506 (italics added).

Other instances in which the right to protect project water interests has been asserted include United States v. Humboldt Lovelock Irrigation Light & Power Co., 97 F.2d 38 (9th Cir. 1938), where the Ninth Circuit found that the United States could sue to enjoin upstream nonproject irrigators from diverting water to which the Bureau had obtained a prior right from the State of Nevada, and Hudspeth County Conservation & Reclamation Dist. v. Robbins, 213 F.2d 425 (5th Cir. 1954), where the Fifth Circuit Court of Appeals held that because of its responsibilities to project water users, the United States was a necessary party to a suit brought against the Bureau officials by nonproject landowners who received project water under “Warren Act” contracts.

In United States v. Tilley, 124 F.2d 850 (8th Cir. 1942), the Eighth Circuit Court of Appeals spoke generally of the right of the distributor to protect project water interests. It concluded that this right “has never rested upon the premise that the United States was the actual
owner of the waters appropriated and diverted” since in Nebraska as elsewhere the landowner who puts the water to beneficial use holds the vested right to receive the water. 124 F.2d at 861. Rather, the court, in language summarizing the nature of the United States’ interest in project water rights, observed:

[T]he owner of the irrigation project or canal . . . has an interest in such appropriative rights, by virtue of the fact that the statute permits him to make the appropriation and diversion, that the maintenance of such appropriative rights is necessary in accomplishing the purpose of the project or canal, and that the law imposes certain duties and obligations upon him in the carriage, distribution, and conservation of the diverted waters. This interest clearly is such as to entitle him to take any necessary steps to protect the scope of the right conferred by the state appropriation statutes, not merely in representatively securing and protecting the full measure of beneficial use for the land owners under the project or canal, but also in effectuating the object of the project or canal as an enterprise.

Id. (Italics added.)

None of the cases discussed above held that the rights of the United States to protect project water rights stemmed from any beneficial interest in the water rights. Rather, they clearly recognized in the United States as distributor and legal titleholder of the appropriative right an interest in protecting project water rights for the benefit of the project.

In some situations, the United States is also entitled as a lien holder to assert claims for project water rights in general stream adjudications. The United States is considered as having a lien upon the water rights within a reclamation project to ensure repayment of the project’s construction, operation, and maintenance costs. In Ickes v. Fox, supra, the Supreme Court made express reference to the lien interest: “The government . . . [has] the right to receive the sums stipulated in the contracts as reimbursement for the cost of construction and annual charges for operation and maintenance of the works. As security therefor, it was provided that the government should have a lien upon the lands and the water rights appurtenant thereto . . .” 300 U.S. at 95.

Finally, the United States may have certain contractual obligations to defend a reclamation project’s water supply. Each contract may vary as to the extent of the obligation. Often at a minimum the contract will provide the United States with discretion to take action either independently or in cooperation with the contracting district as deemed necessary to protect the water supply. See, e.g., Repayment Contract between the United States and the A&B Irrigation District, Idaho, dated February 9, 1962.

B. Obligation to File on Behalf of Water Users

We now turn to the question of whether the United States is obligated to file in a general stream adjudication claims on behalf of the individual project water users who, as the Supreme Court has held, have the equitable ownership interest in the water right. We
distinguish here between protecting the project water as a block and protecting individual rights to water.

In all general stream adjudications, the state has the option and generally will require the evidence be produced which shows that the water received by the water user is being put to a beneficial use within the definitions of state law. Therefore, given that the Supreme Court has clearly stated that it is the water user who has beneficial ownership of the water, we believe that it would therefore be incumbent upon the water user to meet the necessary evidentiary requirements imposed by the state, as this aspect of the appropriative water right rests exclusively with the water user. We find nothing in the statutes or case law which would obligate the United States to meet these evidentiary requirements.

Thus, when the United States does file in the adjudication for the full project water right held in the name of the United States and that right is confirmed, and when the water users meet the state’s evidentiary obligations, the water users’ beneficial rights to project water will be protected. Exactly how this will occur in a particular adjudication will depend on the type of storage rights systems used in the state initiating the adjudication. For example, in a state such as Wyoming which uses the primary/secondary storage permit system, it would be incumbent upon the United States to file on the primary (storage) permit it holds in its name. This filing will permit the storage right previously decreed to the United States to be reaffirmed in the adjudication, thereby protecting the Government’s ability to maintain delivery of project water. In turn, those holding secondary permits would be responsible to file on the secondary permit and to provide the evidence necessary to show water received is put to beneficial use.6

In other states where no distinction is made in the appropriative permit between rights to storage and rights to receive water, and where the United States was the original applicant and received in its name the project water right, the project water user has no formal record of ownership. Conceivably, then, the only project water right which can be filed in this situation is the one enumerated in the appropriative permits, licenses or decrees issued by the state and held in the name of the United States.7

When the United States files in a general stream adjudication in states that do not distinguish between storage rights and rights to receive water, it has no evidentiary burden to carry for the individual water

6 In those situations in which the United States also holds the secondary permit in its name, the United States should file on the secondary permit and those entitled to receive the water would meet the evidentiary obligations.

7 Some project water rights held in the name of the Federal Government may be legally recognized “notice” water rights obtained by meeting appropriative requirements in states before implementation of a permitting or licensing procedure. In these cases it would be the record of notice or commencement of use that would be filed in the adjudication.
users. However, by making the filings, the United States protects its interest in the project water rights, and the project water users—who have a beneficial interest in the water—will be afforded the opportunity to protect their rights, based on their ability to establish beneficial use of water. Generally, there will be a long history of water delivery based on contracts with the water user to which the water user can point as his entitlement. Thus, when he produces evidence to show that the full extent of the water received from the project is put to beneficial use, he will be able to preserve his beneficial interest in the project water right held and asserted by the United States.

In other words, while the United States is not obligated to “file on behalf of” project water users, by filing to protect the Federal reclamation project water rights, the same objective is achieved on behalf of the individual water users. Finally, our conclusions with regard to obligations to water users should not be read to mean that the Bureau cannot work with the State, the districts, and the actual water users to develop methods to present such evidence that best meets the respective needs of all parties.

IV. Conclusion

In the recent Nevada v. United States decision, the Supreme Court reaffirmed that the beneficial ownership of reclamation project water rights is in the water user who puts the water to beneficial use, and that, when the United States retains legal title to project water rights, the Government is obligated to protect project water supplies. We therefore conclude from this and other court decisions that when it is necessary to protect the supply, the United States is obligated and entitled to make filings in general stream adjudications on behalf of project water rights to which the United States holds legal title. We have also concluded that the United States is not obligated to make filings or present evidence of beneficial use on behalf of individual water users.

RALPH W. TARR
Solicitor

AUTHORITY TO PROVIDE WATER TO STILLWATER WILDLIFE MANAGEMENT AREA*

M-36967

July 10, 1989

Secretary of the Interior

* We further point out that, while not obligated to meet evidentiary requirements to show beneficial use, the United States, just as it is entitled to file on project water rights to protect project interests, is entitled to meet those requirements, if it finds that such action is in the best interest of the project’s water rights that it do so. As noted in U.S. v. Tilley, supra, the distributor is entitled to take “any necessary steps to protect the scope of the right conferred by the state appropriation statutes . . .” 124 F.2d at 861.

* Not in chronological order.
Where the Secretary proposes to use water developed by the Bureau of Reclamation for irrigation and wildlife purposes without specific legislative directives, the Secretary must answer two questions: (1) does the Secretary, through the Fish and Wildlife Service, have authority to acquire Project water rights and use them for fish and wildlife purposes at Stillwater; and, (2) if the answer to the first question is in the affirmative, does the Secretary, through the Bureau of Reclamation, have authority to transport water so acquired through Project facilities to Stillwater Wildlife Management Area.


Water and Water Rights: State Laws

Neither the decrees governing the water rights involved, nor provisions of state law provide an inherent bar to the acquisition by the Secretary of water rights for use at Stillwater for wildlife purposes; however, the State Engineer may find factual reasons for disapproving an individual change of use or change of place of use application.

To: Secretary

From: Solicitor

Subject: Authority to Provide Water to Stillwater Wildlife Management Area

This responds to your inquiry concerning the authority of the Secretary to acquire water rights for fish and wildlife purposes and transport the water through Bureau of Reclamation (Reclamation) facilities within the Newlands and Washoe Reclamation Projects (Project) to Stillwater Wildlife Management Area (Stillwater). Your inquiry relates to a proposal by the Nevada Waterfowl Ass’n to donate water rights to the U.S. Fish and Wildlife Service (Fish and Wildlife Service) for use on Stillwater. In addition, the Appropriations Act for Fiscal Year 1989 requires the Fish and Wildlife Service to acquire water rights for use at Stillwater. In addition, the Appropriations Act for Fiscal Year 1989 requires the Fish and Wildlife Service to acquire water rights for use at Stillwater. Pub. L. No. 100-446, 102 Stat. 1778 (1988).

Two specific questions are raised by the proposal and the legislation: (1) does the Secretary, through the Fish and Wildlife Service, have authority to acquire Project water rights and use them for fish and wildlife purposes at Stillwater; and, (2) if the answer to the first

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1 An application has been made to the Nevada State Engineer to transfer those rights to the Fish & Wildlife Service and the Nevada Dept. of Wildlife. The application identifies the Fish & Wildlife Service and the Nevada Dept. of Wildlife as the applicant, although the Fish & Wildlife Service has not been asked to join in the application. The Dept. of the Interior has petitioned the State Engineer to intervene in the proceeding as an unaligned party. The State Engineer has not yet ruled on this petition. For the purposes of this memorandum, we have assumed that if the Fish & Wildlife Service acquires an interest in water rights, it will acquire an undivided interest in those rights.
question is in the affirmative, does the Secretary, through the Bureau of Reclamation, have authority to transport water so acquired through Project facilities to Stillwater. We conclude that the Secretary does have ample authority to acquire Project water rights for fish and wildlife purposes at Stillwater and to transport water so acquired through Project facilities to Stillwater.

BACKGROUND

At the time of creation of the Newlands Reclamation Project, the Secretary of the Interior's only enabling legislation with regard to the construction of reclamation projects consisted of the 1902 Reclamation Act (Reclamation Act). Act of June 17, 1902, 32 Stat. 388. That Act has been since supplemented and amended numerous times. The Reclamation Act did not authorize any particular project, but, rather, generally authorized the Secretary to undertake reclamation efforts. In response to that authority, the Secretary directed the Geological Survey to initiate the Newlands Project only a few days after enactment of the Reclamation Act. The Newlands Project proposal is set forth in a memorandum from the Director of the Geological Survey to the Secretary dated March 7, 1903. United States Department of the Interior, Bureau of Reclamation Project Feasibilities and Authorizations, 10-11, 14-15 (1957).

As initially conceived, the Newlands Project would have irrigated 140,000 acres of land, with a second phase adding approximately 100,000 acres. Id. The lands withdrawn and reserved totaled 232,800 acres. Id. The lands withdrawn and reserved totaled 232,800 acres. U.S. Department of the Interior, Operating Criteria and Procedures for the Newlands Project, Record of Decision 2 (April 15, 1988) (OCAP ROD). The Omnibus Adjustment Act of May 25, 1926, reduced the size of the Newlands Project by approximately 97,000 acres.

The Newlands Project receives water from two rivers, the Truckee and the Carson. The water rights for those rivers were adjudicated in United States v. Orr Water Ditch Co., Equity A-3 (D. Nev., 1944) (Orr Ditch); and United States v. Alpine Land and Reservoir Co., 503 F.Supp. 877 (D. Nev. 1980), aff'd, 697 F.2d 851 (9th Cir. 1983) (Alpine). The decrees do not apportion water rights to particular parcels of land; rather, the decrees recognize that the Secretary holds legal title to the block of water rights, under which the Department provides irrigation water to up to 232,800 acres of land. Orr Ditch at 10; Alpine, 503 F.Supp. at 879. The Secretary contracted with individual project farmers for delivery of water from the Newlands Project until signing an operations contract with the Truckee Carson Irrigation District (TCID) in 1926. After this contract was signed,
TCID contracted directly with project farmers for delivery of water to them. These individual contracts identify water rights to particular parcels of land within the Project.

An agreement among TCID, the Nevada State Board of Fish and Game Commissioners (currently Nevada Department of Wildlife), and the Fish and Wildlife Service established Stillwater Wildlife Management Area in November 1948 (Attachment A) on Newlands Project withdrawn lands. The so-called "tri-party agreement" established the management area for a 50-year term, which will terminate in 1998, unless renewed. The agreement provides that the management area is to be administered by the Fish and Wildlife Service but Stillwater continues as Reclamation withdrawn lands.* Memorandum from Acting Associate Solicitor, Conservation and Wildlife Division, to Assistant Secretary for Fish, Wildlife and Parks, dated August 17, 1973, regarding Stillwater Wildlife Management Area, Bureau of Sport Fisheries and Wildlife (Attachment B). The land included in Stillwater serves as a drainage area for the Project and as habitat for waterfowl, migratory birds, and bald eagles.

In 1956, Congress authorized another project in the same area as the Newlands Project. The Washoe Project (Washoe) supplemented and became integrated with the existing Newlands Project. 70 Stat. 775-76, 43 U.S.C. § 614; see also, H.R. Doc. No. 184, 84th Cong., 1st Sess. 3 (1955). Although the Washoe Project made water available to additional lands, the area designated to receive benefits from the Washoe Project includes all of the areas designated to receive water from the Newlands Project. H.R. Doc. No. 184, supra at 1. The Washoe Project was designed to develop water supplies to meet additional water needs in the area of the Newlands Project by conserving excess runoff in project reservoirs, and by saving water previously lost to evaporation and transpiration. In addition, Congress authorized the Washoe Project for fish and wildlife purposes. 70 Stat. 775, 43 U.S.C. § 614.

Operation of the Newlands Project has raised many issues that have led to considerable litigation. Two areas of contention have been how to efficiently manage project water and who owns the water rights. Competition for water from the Project is keen. Water diverted to the users in TCID does not reach Pyramid Lake, home to the cui-ui, an endangered species, and the Lahontan cutthroat trout, a threatened species, and the Pyramid Lake Paiute Tribe of Indians (Tribe). Conversely, water flowing to Pyramid Lake does not reach TCID, the

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* A portion of Stillwater was set aside as Fallon National Wildlife Refuge in Exec. Order No. 5606 (1931). Creation of the Fallon National Wildlife Refuge changed the legal status of those lands. Fallon National Wildlife Refuge lands have been removed from the Newlands Project, and are reserved for another purpose. By contrast, the Stillwater Wildlife Management Area, which includes that area administratively designated by the Fish and Wildlife Service as Stillwater National Wildlife Refuge, remains project lands.
Fallon Indians, and Stillwater. In order to meet all of its obligations, the Department focused on efforts to make the use of the Project's water more efficient by promulgating operating criteria and procedures for the project.

The Department adopted regulations setting out operating criteria and procedures for the Newlands Project in 1967. These were challenged in *Pyramid Lake Paiute Tribe of Indians v. Morton*, 354 F.Supp. 252 (D.D.C. 1973). The court in *Morton* examined the Department's management regulations in light of the three major factors that the court maintained should control Secretarial action at the Newlands Project: (1) the Secretary's contract with the irrigation district, (2) applicable court decrees, and (3) trust responsibilities to the Pyramid Lake Tribe. The court found the operating criteria and procedures then in effect to be defective and set out its own criteria and procedures, which it ordered the Secretary to adopt.

In 1973, in an attempt to properly allocate Project water, the United States instituted a suit against all users of Truckee River water, asserting that the *Orr Ditch* decree determined only the reservation Indians' rights to irrigation water, and claiming an additional reserved right for water to maintain and preserve Pyramid Lake and maintain the lower Truckee as a natural spawning ground. In *Nevada v. United States*, 463 U.S. 110 (1983), the Supreme Court held that res judicata barred the United States from asserting this claim. Further, the court held that reallocating Project water to the reservation would not be merely an internal shift by the United States of its own water because the beneficial interest in the Government's water right for the reclamation project resided in the owners of the land irrigated by the project. Therefore, the Court placed substantial restrictions on the ability of the United States to meet its obligations by reallocating Project water:

> We conclude that the government is completely mistaken if it believes that the water rights confirmed to it by the *Orr Ditch* decree in 1944 were like so many bushels of wheat, to be bartered, sold or shifted about as the Government might see fit. Once these lands were acquired by settlers in the Project, the Government's "ownership" of the water rights was at most nominal; the beneficial interest in the rights confirmed to the Government resided in the owners of the land within the Project to which these water rights became appurtenant upon the application of Project water to the land.

463 U.S. at 126 (1983).

With this limitation as background, the Ninth Circuit in *TCID v. Secretary of Interior*, 742 F.2d 527 (9th Cir. 1984), reaffirmed the authority of the Department to establish operating criteria for TCID. See also *Orr Ditch*, supra. Following the decision in *TCID v. Secretary of Interior*, supra, Interior annually promulgated interim operating criteria and procedures from 1985 until 1987. After undertaking a comprehensive review, with public participation and comment, on April 15, 1988, the Secretary issued, subject to court approval, the final operating criteria and procedures (OCAP) to govern use of Federal
facilities for delivery of irrigation water. The stated objective of the promulgation was to "ensure that maximum use is made of the Carson River and minimum use of the Truckee River for deliveries to meet decreed entitlements, in conformance with instructions from the Nevada Federal District Court." OCAP ROD at 3. By requiring water conservation measures and providing incentives and disincentives to TCID and water users to use water more efficiently, the Department intends through OCAP to supply the project with water to meet all valid water rights, and to do so in a manner that will comply with applicable court decrees; fulfill the Federal trust responsibility to the Pyramid Lake and Fallon Tribes; meet the requirements of the Endangered Species Act; and provide a "framework for local decisionmaking which can contribute to the protection of wetlands, recreation, economic and other regional values." OCAP at 3.

The OCAP are designed to reduce the amount of water diverted from the Truckee River to TCID, in order to increase flows to Pyramid Lake for the benefit of the Tribe and endangered species, while meeting obligations to deliver water to all holders of valid water rights. The water conservation measures and incentives and disincentives are designed to result in expected irrigation diversions from the Truckee River ranging from 343,855 acre-feet in 1988 to 320,480 acre-feet in 1992. OCAP at 27. Although approximately 73,800 water-righted acres could be irrigated in the project (OCAP at 27), the OCAP rely upon an assumption that less acreage will in fact be irrigated than the full water-righted total; the actually irrigated acreage estimates range from 61,630 in 1988 to 64,850 in 1992. OCAP at 28, Table 1 and related discussion. As the Record of Decision states, "OCAP are predicated on water being used on water-righted land in a manner similar to past operations. Compliance with OCAP will be measured based on facts which can be readily determined by the District and the Bureau."

Water conserved under OCAP would eventually reach both the Indian tribes and the endangered species without depriving the water users of their water rights. Water conserved through efficiency at the Project would not be diverted out of the Truckee River and would flow into Pyramid Lake. Water at Pyramid Lake benefits the Pyramid Lake Paiute Tribe, the Lahontan cutthroat trout, and the cui-ui.

One direct consequence of the OCAP, however, will be to reduce drainage of excess irrigation water to Stillwater. Absent another source of water for Stillwater, this reduced drainage will result in a loss of wetlands, and an attendant drop in wildlife areas. The OCAP do

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5 The final OCAP have been filed with the U.S. District Court for the District of Nevada in Pyramid Lake Paiute Tribe v. Lujan, Civil No. CV-R-85-197-BRT, and are pending before the court for approval. The final OCAP have not been published in the Federal Register.
not attempt to mitigate this impact because the area possesses no primary water rights for wildlife use. Instead, Stillwater receives Project runoff under an appropriative right and uses the water for wildlife purposes. Nev. State Eng. Permits Nos. 13345-51 (Oct. 26, 1987). Therefore, Stillwater has no right to rely on the continued availability of waste water from the Project. See Bowers v. Big Horn Canal Ass'n, 77 Wyo. 80, 307 P.2d 593 (1957).

In an effort to mitigate potential wetlands losses at Stillwater as a result of OCAP, both public and private assistance measures are being undertaken. Congress, through Pub. L. No. 100-446, directed the Fish and Wildlife Service to expend $1.2 million to lease or purchase water rights, subject to certain requirements, for the benefit of Stillwater:

[Of the funds provided to the United States Fish and Wildlife Service under the heading “Construction and Anadromous Fish in Public Law 100-71,” $1,200,000 shall be expended for the lease or purchase of water rights, from willing sellers, for the benefit of Stillwater Management Area, Nevada: [Provided] That the lease or purchase shall be carried out pursuant to this appropriation if and only if the Secretary receives certification from the State of Nevada that the transfer of water rights and associated change of use for the beneficial use of Stillwater Management Area is approved by the State of Nevada.

102 Stat. 1778. Private organizations are also making efforts to acquire water rights for donation to the management area.

DISCUSSION

A. Authority of the Secretary to Acquire Water Rights for Fish and Wildlife Purposes at Stillwater

The question of authority to acquire Project water rights for use for fish and wildlife purposes at Stillwater must be answered in two parts. First, does the Secretary have authority generally under Federal law to acquire water rights for fish and wildlife purposes? Second, does the Secretary have authority to use this Project water for fish and wildlife purposes at Stillwater? We believe the answer to both of these questions is in the affirmative.

1. Authority under Federal Law


In addition to those statutes, the Secretary must also take into consideration trust obligations to Indian tribes and the requirements of the Endangered Species Act before proceeding. It is our judgment that these requirements can be satisfied if the proposed acquisitions are consistent with the OCAP for the Project.
a. Trust Responsibilities

Any proposed water rights transfers must be consistent with the Secretary's fiduciary duty to the Pyramid Lake Paiute and Fallon Tribes. The primary question in the consideration of whether a proposed acquisition is consistent with that duty is whether the acquisition will adversely affect the operation of the OCAP. Consistency with the OCAP is of primary importance because the effectiveness of the OCAP in improving the efficiency of water deliveries to irrigation will permit water not needed for irrigation to go to Pyramid Lake for the benefit of tribal fisheries and endangered species, and to the Fallon Reservation.

In Pyramid Lake Paiute Tribe of Indians v. Morton, supra, the Pyramid Lake Tribe challenged transfers that would deliver more water to TCID than required by applicable court decrees and statutes. In agreeing with the Tribe, Judge Gesell stated that the water to go to Pyramid Lake was "all water not obligated by court decree or contract with the District." 354 F.Supp. at 256 (italics added). The Secretary was directed to develop operating criteria and procedures that would protect the Tribe's interest in minimizing diversions from the Truckee River and from Pyramid Lake. It is assumed that the water rights now proposed for transfer are those obligated by decree or contract. Further, from the available facts, there is no indication that the currently proposed transfers would otherwise violate Judge Gesell's judgment and order in Morton or operate against the effectiveness of the OCAP subsequently developed by the Department or the incentives on which the OCAP relies.

In summary, and as a general proposition, Morton itself does not appear to preclude the proposed transfers. Known facts do not indicate that the current proposal would increase consumptive use or cause greater diversions from the Truckee River in violation of the OCAP and the Secretary's trust responsibilities. However, before approving or accepting any specific acquisition of water rights or transportation of water, there should be confirmation that the proposed transfers will not impair the Department's ability to achieve the diversion objectives of the OCAP.

6 The Fallon Paiute Tribe differs from the Pyramid Lake Tribe in that the Fallon Indian Reservation is within the Project. In 1978, Congress enacted Pub. L. No. 95-337, 92 Stat. 455 (1978), charging the Secretary with the responsibility of developing irrigation on the Fallon Reservation. Accordingly, the water budget for OCAP includes present and projected irrigation needs of the Fallon Reservation. As long as the subject transfers will be consistent with that budget, they will not affect performance of the Secretary's duty to that Tribe.

7 Delivery of water to Stillwater will involve conveyance losses, and Reclamation must consider whether a transfer of the full water allotment to Stillwater will lessen the district's efficiency in delivery and use of water under the OCAP. If Federal action results in or contributes to diversions beyond that predicted from historical data and included in the OCAP water budget, the result will tend to defeat efforts by TCID and the farmers to minimize overall diversions, will detract from the rewards which TCID and the farmers can seek under the OCAP incentive system, and could even result in penalties being imposed on those parties under the OCAP. Such a result could bear on the sustainability of the OCAP now filed with the Nevada Federal District Court. One of the objections to the OCAP filed by TCID was that the OCAP could lead to TCID and the farmers being penalized for matters over which they have no control.
b. The Endangered Species Act

On November 24, 1987, the Fish and Wildlife Service issued an extensive biological opinion on a number of proposed, alternative long-term operating criteria for the Newlands Project. See Memorandum from Regional Director, Fish and Wildlife Service, Region 1, Portland, Oregon, to Regional Director, Bureau of Reclamation, Mid-Pacific Region, Sacramento, California, re Formal Section 7 Consultation for Reinitiation of Newlands Project Long-Term Operating Criteria and Procedures (File No. 1-5-86-F-81R) (Nov. 24, 1987) (November 1987 Biological Opinion).

That opinion concluded that the implementation of the preferred alternative in the Final Environmental Impact Statement (FEIS), which involved a total allowable diversion of 320,000 acre-feet over a 5-year phase-in period, is not likely to jeopardize the continued existence of the cui-ui or the bald eagle. See November 1987 Biological Opinion at 3.8

Later, after further fine-tuning of the long-term OCAP as a result of the post-FEIS public review and comment process, the Fish and Wildlife Service examined the revised OCAP, and in an updated biological opinion, issued on April 14, 1988,9 I concluded that they continued to meet the requirements of section 7(a)(2) of the ESA. We conclude that there is nothing to prevent the Department from again relying upon this biological opinion, assuming that the water rights being considered for acquisition and transportation are consistent with the OCAP water budget and that there is no new data that would require further analysis.

We also conclude that the proposed acquisition of water rights for the Stillwater wetlands would not violate the Secretary's general responsibility to conserve the cui-ui or the Lahontan cutthroat trout under section 7(a)(1) of the ESA. In fact it is important to note that the Department is not ignoring its conservation responsibilities for the cui-ui and the cutthroat trout. The Department is pursuing the conservation of these species by devoting the entire conservation yield of Stampede Reservoir for the benefit of these fish. Carson-Truckee Water Conservancy District v. Clark, 741 F.2d 257 (9th Cir. 1984), cert.

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8 The Fish & Wildlife Service's biological opinion also addressed whether the Department must reduce diversions of water from the Truckee River to avoid the impairment of cui-ui spawning activity and, therefore, avoid the alleged unlawful "taking" of the endangered fish. See 16 U.S.C. § 1538(a). The Fish & Wildlife Service examined the issue of whether cui-ui might be taken incidental to the implementation of the proposed long-term OCAP and concluded that no incidental taking would be anticipated. See November 1987 Biological Opinion at 17.

9 The biological opinions issued by the Fish & Wildlife Service under sec. 7 of the ESA are entitled to great deference by reviewing courts. See e.g., Roosevelt Campobello International Park Commission v. U.S. Environmental Protection Agency, 684 F.2d 1041 (1st Cir. 1982); H.R. Conf. Rep. No. 697, 96th Cong., 1st Sess. 12 (1979) (legislative history to the ESA Amendments of 1979). As noted in Village of False Pass v. Watt, 565 F.Supp. 1123 (D. Alaska 1983), aff'd, 735 F.2d 605 (9th Cir. 1984), "The biological opinion is accorded substantial weight as evidence of [the agency's] compliance with the Endangered Species Act." 565 F.Supp. at 1160. The Department relied upon the biological opinion of the Fish & Wildlife Service in determining that its long-term OCAP satisfied the requirements of sec. 7(a)(2) of the ESA.
denied, 470 U.S. 1083 (1985). Such discretionary action on the part of the Department satisfies the requirements of section 7(a)(1).

We therefore conclude that the Secretary possesses ample authority under Federal law to acquire water rights for fish and wildlife purposes for use at Stillwater.

2. Authority to Use Project Water

While there is ample authority for the Secretary to acquire water rights for fish and wildlife purposes under Federal law, we must still address the question of whether Project water in particular can be used for fish and wildlife purposes. Section 8 of the Reclamation Act of 1902 requires that “the Secretary of the Interior, in carrying out the provisions of [the Reclamation Act] shall proceed in conformity with [state laws relating to the control, appropriation, use, or distribution of water used in irrigation].” 43 U.S.C. §§ 372, 383; Nevada v. United States, supra; United States v. Alpine Land & Reservoir Co., 697 F.2d 851 (9th Cir. 1983). In California v. United States, 438 U.S. 645 (1978), the Supreme Court held that section 8 “requires the Secretary to comply with state law in the ‘control, appropriation, use, or distribution of water.’” Id. at 675. The Court proceeded to find that the Secretary should “follow state law in all respects not directly inconsistent with [Federal statutory] directives.” Id. at 678.

a. The Orr Ditch and Alpine Decrees

The decrees resulting from the original general stream adjudications constitute the initial determination of the Project’s rights under state law. The Orr Ditch decree provides that the Newlands Project water from the Truckee River may be used for:

[T]he irrigation of 232,800 acres of lands on the Newlands Project, for storage in the Lahontan Reservoir, for generating power, for supplying the inhabitants of cities and towns on the project and for domestic and other purposes and under such control, disposal and regulation as the [Secretary] may make or desire, provided that the amount of this water allowed or used for irrigation shall not exceed, after transportation loss and when applied to the land, 3.5 acre feet per acre for the bottom lands, nor 4.5 acre feet per acre for the bench lands under the Newlands Project. (Italics added.)

Orr Ditch at 10. Thus, under Orr Ditch, the Secretary would appear to have broad discretion with respect to changes in the place or type of use of Project water, subject to state procedural authority.

The Alpine decree does not specify to what uses the water rights may be put. The Alpine court, however, emphasized that “the United States . . . is required to conform to applicable Nevada law with respect to changing the place of diversion or place of use.” 503 F.Supp. at 884.10

10 Alpine did not address whether the United States must comply with Nevada procedures for a change in the type of use to which the water would be put. However, this conclusion is implicit from the discussion of the Alpine court. 503 F.Supp. at 884.

While the Orr Ditch decree would appear to give the Secretary broad discretion with respect to changes in the use of Project water under state law, we must examine further the state provisions applicable to changes in beneficial ownership and use. The proposed transfer of a water right from the Nevada Waterfowl Ass'n, and the proposed acquisition of water rights under Pub. L. No. 100-446, would result in conveyances of beneficial ownership of water rights from irrigators to the Fish and Wildlife Service. In addition to the change of beneficial ownership, the transactions would change the use of the water from irrigation to wildlife.\(^\text{11}\)

For water rights acquired under Pub. L. No. 100-446, the Act provides that the Secretary may not proceed with water rights acquisitions until the State of Nevada certifies that the transfer and change of beneficial use has been approved by the State of Nevada. 102 Stat. 1778.\(^\text{12}\) This requirement is consistent with the holding in Alpine requiring the United States to follow Nevada law in water transfers. On appeal in United States v. Alpine, the Ninth Circuit addressed whether the United States must follow Nevada law with respect to water rights transfers and changes of use for Newlands. The Ninth Circuit affirmed the trial court's decision that the United States had properly acquired water rights for the Project from private parties:

We agree with the district judge that "the conspicuous absence of transfer procedures, taken in conjunction with the clear general deference to state water law impels the conclusion that Congress intended transfers to be subject to state water law." [Citation omitted.]

697 F.2d at 858.\(^\text{13}\) Ultimately, then, the State Engineer's decision constitutes the determination of consistency with state law.


\(^{11}\) It is unclear whether the proposed transaction would constitute a change of place of use under state law because the state general stream adjudications did not identify the water rights to individual parcels of land within the project and the only such identification derives from actions taken by or on behalf or the Department of the Interior. The State Engineer has processed several previous applications for change of location of use within the Newlands Project. The United States has not challenged his jurisdiction to do so since the Alpine decision.

\(^{12}\) Pub. L. No. 100-446 provides:

That the lease or purchase shall be carried out pursuant to the statutory and procedural requirements of the laws of the State of Nevada, and the Secretary shall proceed with any such lease or purchase pursuant to this appropriation if and only if the Secretary receives certification from the State of Nevada that the transfer of water rights and associated change of use for the beneficial use of Stillwater Wildlife Management Area is approved by the State of Nevada.

102 Stat. 1778. Because the Appropriation Act requires Nevada's certification that any particular transfer is approved, contracts for the purchase or lease of water rights acquired with funds under Pub. L. No. 100-446 should be made contingent on the approval of the transfer application by the Nevada State Engineer.

\(^{13}\) It has been argued that the Ninth Circuit opinion suggests that the court believed that the Secretary has no authority to review the merits of a proposed transfer within the Project, and no opportunity to protect Federal interests in the Project, except before the State Engineer. See 697 F.2d at 858. Indeed, the Supreme Court held in California v. U.S., 438 U.S. 645 (1978), that state law will control the distribution of water rights to the extent that there is no preempting Federal directive. 438 U.S. at 678. However, under California v. U.S., the United States retains authority to review proposed transfers to ensure that no Federal directive preempts the proposed state action.
change of type of use would be virtually identical to the standards for a change in the place of use.\footnote{Provisions under both state and Federal law address changes in the place of use of a water right. Nev. Rev. Stat. § 533.040 provides: All water used in this state for beneficial purposes shall remain appurtenant to the place of use; provided: 1. That if for any reason it should at any time become impractical to use water beneficially or economically at the place to which it is appurtenant, the right may be severed from such place of use and simultaneously transferred and become appurtenant to other place or places or use. \ldots without losing priority of right. \ldots 2. That the provisions of this section shall not apply in cases of ditch or canal companies which have appropriated water for diversion and transmission to the lands of private persons at an annual charge. Nev. Rev. Stat. § 533.040 (1986). Thus, the ability to sever the water right from the appurtenant land under Nevada law will depend on determinations made by the Nevada State Engineer with respect to the question of whether it is impractical or uneconomical to use water at the place to which it is appurtenant. A separate provision appears in sec. 8 of the Reclamation Act of 1902, which provides that “the right to the use of water acquired under the provisions of this act shall be appurtenant to the land irrigated \ldots” 43 U.S.C. §§ 372, 383. However, because the water rights to be transferred here will continue to serve and become appurtenant to Project lands, as specified in the \textit{Orr Ditch} and \textit{Alpine} decrees, we believe that the provisions of sec. 8 will not preclude the use of water at Stillwater.}

Two separate sections, sections 1 and 3, provide guidance to the State Engineer in reviewing a change of use application. Section 1 reads in pertinent part:

\begin{quote}

(b) The proposed use or change, if within an irrigation district, does not adversely affect the cost of water for other holders of water rights in the district or lessen the district's efficiency in its delivery or use of water.
\end{quote}

Nev. Rev. Stat. § 533.370(1) (1986). This section provides three considerations important to the current situation: (1) that the new use of the water be a recognized beneficial use; (2) that the change does not adversely affect the remaining users' irrigation costs;\footnote{We will not address the question of the proper allocation of costs generated by a change of use or place of use until specific proposals concerning these allocations are made. We note only that some writers suggest that any use of project conveyance facilities should avoid the imposition of additional costs on users intended by Congress to be the primary beneficiaries of project water. See B. Driver, "The Effect of Reclamation Law on Voluntary Water Transfers," 38 Rocky Mt. Min. L. Inst., § 26.04[7] (1988); R. Roe-Collins, "Voluntary Conveyance of the Right to Receive a Water Supply from the United States Bureau of Reclamation," 13 Ecology L.Q. 773, 817 (1987).} and (3) that the change does not lessen the district's efficiency in delivery or use of water.

For many years, Nevada law did not specify whether the use of water for wildlife purposes constituted a beneficial use. Recently, in the Nevada Supreme Court case, \textit{Nevada v. Morros}, 104 Nev. XXX, 766 P.2d 263 (1988), the court recognized use of water for wildlife purposes as a beneficial use.

With respect to the cost of water and the district's efficiency in its delivery or use of water, Nevada law provides no guidance.\footnote{TCID has argued in the past that this provision precludes the State Engineer from approving a proposed transfer of water from Project to non-Project lands that would affect the cost of water for other holders of water rights in the district or lessen the district's efficiency in its delivery or use of water. \textit{In re Medlock, et al.}, Bankruptcy, Case No. 87-149 (July 17, 1987). We assume here that Project water will be transferred only to Project lands. We leave for another day the issue of the validity or transfers to non-project lands.} There is no case law guiding these provisions; these are factual determinations committed to the State Engineer.

Section 533.370(3) provides additional criteria under which the applications will be reviewed:
Where the transferee's proposed use or change conflicts with existing rights, or threatens to prove detrimental to the public interest, the state engineer shall reject the application and refuse to issue the permit asked for.

Nev. Rev. Stat. § 533.370(3) (1986). Therefore, the State Engineer must reject a transfer application if it harms existing appropriators or is "detrimental to the public interest." The public interest is nowhere defined, and research has not disclosed a reported Nevada case providing further guidance. However, Nevada v. Morros, supra, and the various Federal laws favoring protection of wildlife provide support for the proposition that the proposed transaction is not inconsistent with the public interest.

The question of harm to other appropriators remains to be determined as a factual matter by the State Engineer. Under the law of most western states, the right to change beneficial use or place of use may not be approved if it would harm other appropriators. See generally, Farmer's Highline Canal & Reservoir Co. v. City of Golden, 129 Colo. 575, 272 P.2d 629 (1954). Appropriators normally have vested rights in the continuation of stream conditions as they existed at the time of their respective appropriations. Id. Subsequent to such appropriations, they may successfully resist all proposed changes in points of diversion and use of water that in any way materially injure or adversely affect their rights. Id. In approving the proposed change of use of water, the State Engineer must ensure that no other appropriator's rights will be adversely affected.

Therefore, State law contains no legal bar to the acquisition by the Secretary of Project water rights for use at Stillwater for fish and wildlife purposes. However, uncertainty will remain until the State Engineer makes the factual determinations necessary for approval of a transfer or a change of use.

B. Authority of the Secretary to Use Project Facilities to Transport Water to Stillwater for Fish and Wildlife Purposes

Once water rights are acquired, the water must be transported to Stillwater.17 Because the Project provides the only existing delivery system for that water, Project facilities must be used if delivery of the water is to be timely and cost effective. Thus, the second question we address is the Secretary's authority to use Project facilities to transport acquired water to Stillwater for fish and wildlife purposes.

The question of authority to use Project facilities differs from the question of the use of the Project water rights. While the courts have been firm in holding that the United States must comply with state law in its use of water, they have consistently reaffirmed the

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17 Any consideration of environmental and trust responsibilities necessary for the use of Federal facilities for the proposed transfers will be subsumed within the consideration of those responsibilities with respect to the acquisition and application of water rights. We need not address whether such Federal responsibilities would be triggered if water rights acquired by some other party were to be transported through Federal facilities. Further, because Stillwater lies within the Project, we have not examined whether the use of Project facilities to deliver water outside Project boundaries would be permissible.
proposition that the United States retains ownership of and an interest in management of project facilities. In California v. United States, the Court quoted from Nebraska v. Wyoming, 325 U.S. 589 (1945), and Ickes v. Fox, 300 U.S. 82 (1937): "[T]he water-rights became the property of the land owners, wholly distinct from the property right of the government in the irrigation works." 438 U.S. at 677. In Nebraska v. Wyoming, the Court also noted that the United States retains a distinct "property right in the reservoirs, ditches or canals." 325 U.S. at 614.

In Pyramid Lake Paiute Tribe v. Morton, supra, the court recognized that the Secretary retains responsibility for the management of the Newlands Project even though beneficial ownership of the Project water lies with the landowners. Further, in TCID v. Secretary, supra, the Ninth Circuit affirmed the authority of the United States to terminate a water contract in order to assert management control over the Project. Given these considerations, the use of Project facilities to accomplish a proposed transaction must be reviewed for consistency with Federal law.

Federal law requires that the Department, through the Bureau of Reclamation, operate its water projects in a manner consistent with the projects' legislative authorities and in a manner consistent with any feasibility reports submitted to Congress at the time of the projects' authorizations. 85 I.D. 326 (July 31, 1978). However, when the project report and legislation authorizing the project are unclear, the Secretary has broad discretion to use the facilities or even modify the features of a project so long as those modifications are consistent with the legislative descriptions of the project. 85 I.D. 337 (May 1, 1978).

Because the Newlands Project was not authorized under a specific project authorization act, there was no statement of Congressional intent with regard to the specific purposes for the Newlands Project. The Reclamation Act neither expressly prohibits nor authorizes the use of Project water rights or facilities for fish and wildlife purposes, although the legislative history of the Act makes clear that Congress had an irrigation focus for reclamation projects at that time. The focus of the 1902 Act should not be read as perpetual, however, because later enactments have supplemented the authority of the Act.

Congress implicitly recognized fish and wildlife uses for the Newlands Project facilities when it authorized the Washoe Project in 1956. The authorized purposes for Washoe include supplementation of the water supply available to the Newlands Project and fish and wildlife purposes. 43 U.S.C. § 614. In fact, the Washoe legislation expressly provides funding for fish and wildlife purposes. 43 U.S.C. § 614c.

19 The Project feasibility report, like the legislative history, discusses the feasibility of the Project only for irrigation and domestic uses. Bureau of Reclamation Project Feasibilities & Authorizations 10-11, 14-15 (1957).
As discussed above, the project area for Washoe includes the entire Newlands Project. H.R. Doc. No. 184, supra at 1. Further, the legislative history of the Washoe legislation reflects Congress' intent that the Newlands and Washoe Projects be fully integrated. The "Plan of Development" portion of the Feasibility Report on the Washoe Project outlined the relationship between the Washoe and Newlands Projects:

The Washoe project would be integrated with the existing Truckee River storage and Newlands projects... The Washoe project would increase irrigation supplies... by an average of 72,000 acre-feet annually... In addition, during dry cycles, [The Washoe Project] would firm the existing supplies for... the Newlands project.

Id. at 3. Further, the feasibility study for Washoe contemplated that Lahontan Reservoir and other key facilities of the Newlands Project would be integrated with the new Washoe facilities in order to achieve the goals of the Washoe Project, including the fish and wildlife protective purposes. Id. at 3.

The Washoe Project legislative history also reflects Congress' intent that Washoe facilities be used to provide fish and wildlife benefits specifically at Stillwater. H.R. Doc. No. 184, supra at 15, 30, 79 and 143. In the Feasibility Report's discussion of fish and animal life, it is recognized that "the Stillwater wildlife management area offers protection to thousands of birds attracted each year to the Carson Sink area." Id. at 15. In addition, in a letter to the House Chairman commenting on the Washoe Project, the Secretary emphasized his responsibilities within Washoe for protecting fish and wildlife resources:

Moreover, the project area contains significant waterfowl habitat. The Federal Government has responsibilities for the welfare of migratory waterfowl under statutes enacted pursuant to international treaties with Great Britain and Mexico designed to provide for the welfare of these species. We therefore feel that provisions for development of fish and wildlife resources of the project area... is appropriate...


Washoe specifically added drains to carry water already transported through Newlands Project facilities into the management area. Therefore, Congress recognized that Newlands Project facilities would transport water to Stillwater and, thus, implicitly modified the authorization of the Newlands Project to include fish and wildlife purposes. Moreover, provision was specifically made for "adaptation[s] of Washoe] as are justified to best protect and enhance fish and wildlife values." H.R. Doc. No. 184, supra at 7. Pursuant to this ability to adapt the project plan for wildlife purposes, the Bureau of Reclamation proposed construction of facilities to improve the water supply for waterfowl habitat at Stillwater. U.S. Department of the Interior, Water and Power Resources Service Project Data 1291 (1981).
Proposals included enlarging the capacity of Stillwater Point Reservoir and construction of a Paiute Reservoir supply canal to take Newlands Project drain water to Paiute Reservoir. Id.

The Washoe legislation, then, is reasonably interpreted to provide general authority to use Newlands Project facilities for fish and wildlife purposes. Two further acts supplement that authority by providing additional tools for you to meet those purposes. Section 14 of the Reclamation Project Act of 1939 provides further authority to the Secretary to meet the fish and wildlife purposes of Washoe:

The Secretary is further authorized, for the purpose of orderly and economical construction or operation and maintenance of any project, to enter into such contracts for exchange or replacement of water, water rights, or electric energy, or for the adjustment of water rights, as in his judgment are necessary and in the interests of the United States and the project.

43 U.S.C. § 389 (italics added). Thus, in order to ensure orderly operation and maintenance of a project and to meet the needs of a project, the Secretary may by contract, adjust, exchange, or replace project water rights. This statute, then, would appear to provide the Secretary with the flexibility to adjust water rights by changing their place of use in order to meet the fish and wildlife purposes of the Washoe Project.

As we have discussed, the OCAP for the Newlands Project will reduce the drainage water available to Stillwater and may even render its appropriative right to waste water worthless. If the Secretary undertakes to mitigate such effects, we believe the Secretary may do so by means of a contract to replace or otherwise adjust water rights at Stillwater under section 14. Congress recognized that such adjustments might be necessary. In the Feasibility Report for Washoe, incorporated in the legislative history of its authorizing Act, the following discussion of water rights appears:

In order that the most economical use of the water for the entire project area may be effected, agreements would be required with the users of both Truckee and Carson River waters for modification of certain established water rights and for exchanges or water among the various users.

H.R. Doc. 184, supra at 7.

Section 14 has been used as a tool to mitigate adverse effects of projects in the past. In one instance, the Secretary “adjusted” water rights adversely affected by a project, by purchasing water rights outright. Dec. Comp. Gen. B-84264. In another, the Secretary replaced a water supply diverted by project operations by agreeing to supply water from the project. Memorandum from Associate Solicitor, Division of Water and Power, July 27, 1959.

In addition, a contract for the adjustment, replacement, or exchange of water rights would promote the interests of the United States, because Stillwater furthers several interests of the United States. The policy of the United States favors the protection of wetlands. Exec. Order No. 11990, 42 FR 26,961 (1977). Further, treaties with the Union of Soviet

In addition to the 1939 Act, the Water Project Recreation Act of 1965, 16 U.S.C. § 460l-18(a), provides the Secretary with additional authority to meet the fish and wildlife purposes of the Washoe Project. This Act permits the Secretary:

in conjunction with any reservoir heretofore constructed by him pursuant to the Federal reclamation laws or any reservoir which is otherwise under his control, except reservoirs within national wildlife refuges to investigate, plan, construct, operate and maintain, or otherwise provide for . . . fish and wildlife enhancement facilities, to acquire or otherwise make available such adjacent lands or interests therein as are necessary for . . . fish and wildlife use and to provide for public enjoyment of project lands, facilities and water areas in a manner coordinated with the other project purposes: Provided, That not more than $100,000 shall be available to carry out the provisions of this subsection at any one reservoir.

16 U.S.C. § 460l-18(a) (italics added). Stillwater constitutes a fish and wildlife enhancement area; its primary purpose is to provide habitat for waterfowl. It also provides a hunting area, an area or project lands set aside for public enjoyment. As such, this provision would permit the Secretary to operate and maintain existing Project facilities for wildlife purposes, or to acquire other interests for wildlife purposes. One limitation on such use is that these purposes must be coordinated with other Project purposes; another is that costs must be limited to $100,000 per reservoir. The cost limitation would not present a problem in this instance, however, because no new facilities would be necessary.

Our conclusion, then, is that the Secretary has sufficient authority to transport water to Stillwater for fish and wildlife purposes based upon the Washoe Project authorization, the Reclamation Project Act of 1939 and the Water Project Recreation Act.¹⁹

CONCLUSION

We conclude that the Secretary has sufficient authority to acquire water rights for fish and wildlife purposes and to transport the water for use at Stillwater Wildlife Management Area. This legal conclusion assumes that such acquisition and transportation is consistent with OCAP and does not interfere with the primary Project purpose of providing water for irrigation. In addition, the proposed use of the water at Stillwater must be reviewed by the Nevada State Engineer,

¹⁹ An argument could be made that the 1989 Appropriations Act, Pub. L. No. 100-446, which directs the Secretary, through the Fish & Wildlife Service, to acquire water rights for Stillwater supports our conclusion. Because the Act provides no authority for construction of delivery facilities, and no alternate method of delivery exists, and because the Act requires that the water be put to beneficial use in accordance with Nevada law, a reasonable inference may be drawn that Congress intended to authorize the Secretary to use Newlands Project facilities for the delivery of water to Stillwater. Sierra Club v. Andrus, 610 F.2d 581, 601 (9th Cir. 1979), rev’d on other grounds, 451 U.S. 287 (1981).
and he must approve it prior to completion of the transaction and delivery of the water.

RALPH W. TARR
Solicitor

"ADDITIONAL ROYALTY" UNDER SECTION 6(a)(9) OF THE OUTER CONTINENTAL SHELF LANDS ACT*

M-36968
August 31, 1989

Outer Continental Shelf Lands: Oil and Gas Leases—Oil and Gas Leases: Royalty: Payments

In calculating the additional royalty owed under sec. 6(a)(9) of the Outer Continental Shelf Lands Act, 43 U.S.C. § 1335(a)(9), the Department must use the tax rates in effect in Texas and Louisiana on Aug. 7, 1953.

To: Director, Minerals Management Service

From: Solicitor

Subject: “Additional Royalty” under Section 6(a)(9) of the Outer Continental Shelf Lands Act

Before the Outer Continental Shelf Lands Act (OCSLA) was enacted in 1953, Texas and Louisiana issued mineral leases for certain submerged lands off their coasts. In 1950 these lands were decreed to belong to the United States. United States v. Louisiana, 339 U.S. 699 (1950); United States v. Texas, 339 U.S. 707 (1950). Section 6 of the OCSLA created a procedure by which the lessees of the leases could have them maintained as Federal leases. Basically, under section 6 the terms of the original State-issued leases were left in force, provided the lessees satisfied the 11 conditions set out in section 6(a) of the Act, 43 U.S.C. § 1335(a)(1)-(11).

One of those conditions, section 6(a)(9), controls the issue your memorandum of July 28, 1989, to the Associate Solicitor for Energy and Resources asked this Office to address. Section 6(a)(9) requires the lessee to pay “as an additional royalty on the production from the lease... a sum of money equal to the amount of the severance, gross production, or occupation taxes which would have been payable on such production to the State issuing the lease under its laws as they existed on August 7, 1953.” 43 U.S.C. § 1335(a)(9). The issue is whether the tax rate to be used in determining the additional royalty is the rate in effect on August 7, 1953, or the current rate as the States may amend it from time-to-time.

Texas and Louisiana were the only States issuing leases which would later become subject to section 6. “Outer Continental Shelf,” Hearings before the Committee on Interior and Insular Affairs, United States Senate, on S. 1901, 83d Cong., 1st Sess. 709 (1953) (letter of former Solicitor General Perlman) [hereinafter 1953 Senate Hearings]. A

*Not in chronological order.

For the reasons explained below, I conclude that the applicable rate for determining additional royalty under section 6(a)(9) is the rate in effect on August 7, 1953.

Analysis

The language of section 6(a)(9) leaves no room for doubt on this question. The lessee’s duty is to pay a sum equal to the tax he would have paid under the State’s tax laws “as they existed on August 7, 1953.” For a lease originally issued by Louisiana, for example, under the severance tax law as it existed on August 7, 1953, the lessee would have paid three-tenths of one cent for each thousand cubic feet of natural gas produced. Today, under section 6(a)(9), the lessee owes “as an additional royalty” a “sum equal to” that amount for gas produced from the lease. The sum equal to that amount is plainly three-tenths of one cent, not seven cents.

The legislative history of section 6(a)(9) shows that Congress meant what it said. As reported out of committee in the House of Representatives on May 12, 1953, section 11(a) of the bill H.R. 5134 would have permitted holders of State-issued leases to exchange them for Federal leases if they agreed, among other things, to pay “a sum as additional royalty equal to any severance tax charged by an abutting State.” H.R. Rep. No. 413, 83d Cong., 1st Sess. 10 (1953). The bill

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1 When the offshore leases were issued, Texas law imposed a “gross production” tax on “the occupation of producing oil.” State v. Humphrey, 159 S.W.2d 162, 163-64 (Tex. Civ. App. 1941). Texas law distinguished an occupation tax from “a gross proceeds tax, a sales tax, [and] a transfer tax.” Id. at 164. The tax accrued “the moment oil is taken from the ground.” Id. See also Humble Oil & Refining Co. v. Calvert, 478 S.W.2d 926 (Tex. 1972), cert. denied, 409 U.S. 967 (1972).

2 In addition to its general severance tax, Louisiana law also imposed other taxes tied in some manner to the production of natural gas. It assessed “an excise, license or privilege tax” on those engaged in the gathering of natural gas of one cent per thousand cubic feet gathered. La. Rev. Stat. Ann. § 47:671 (West 1952). The Louisiana Supreme Court ruled that this tax violated the Louisiana Constitution’s limitations on taxes that may be imposed on oil and gas leases. Bel Oil Corp. v. Fontenot, 238 La. 1002, 117 So.2d 857 (1959). Louisiana law also assessed an “excise tax” to eliminate the “unjust enrichment” of producers who received a higher price for the royalty owner’s share of gas than the producer paid the royalty owner. La. Rev. Stat. Ann. § 47:692 (West 1952). The question of which taxes Congress intended to include within the phrase “severance, gross production, or occupation taxes” in sec. 6(a)(9) is beyond the scope of this opinion.
introduced in the Senate, S. 1901, had no comparable provision. 1953
Senate Hearings, at 1-6.

On May 26, 1953, the Department of Justice submitted to the Senate
committee a “comparison of S. 1901 and H.R. 5134, with comments and
Assistant Attorney General Rankin). The letter specifically addressed
the provision for additional royalty based on a State’s severance tax:

Section 11(a) provides that the exchange lease shall provide for payment to the United
States of the same rentals, royalties, and other payments as were provided for by the
original lease, plus an additional royalty equal to “any severance tax charged by an
abutting State.” The provision for additional royalty is important, as it prevents a
windfall to lessees through their being relieved of State severance taxes which
presumably were taken into consideration in fixing the terms of the original leases. . .
The provision does not specify whether the State tax referred to is to be that in effect
when the original lease was executed, when the exchange lease is issued, or as it may be
from time to time. This should be made specific; probably the date of the exchange lease
is the most desirable.

Id. at 34-35.

On June 8, 1953, Secretary of the Interior McKay wrote the committee
suggesting a series of amendments to the May 28 committee print of S.
1901. Id. at 26-31. His amendment to section 6(a)(9) proposed the
language Congress eventually enacted. Secretary McKay did not use
the date suggested by Assistant Attorney General Rankin. Instead of
specifying the tax in effect on the date the State lease became a
Federal lease, the Secretary proposed using the date the OCSLA took
effect. Id. at 30. In accepting this amendment, the committee report
noted:

When the lessees bid for leases, they do so in the knowledge that they would be subject
to State taxes on their operations. Therefore, in order to prevent the lessees from
receiving a ‘windfall’ through Federal administration of the area, an amount equal to
the state taxes is to be added to the royalty payments the lessees will make to the
United States.

Id. at 25. In short, the Eisenhower Administration and the Senate
Committee considered the possibility of using the tax rates as they
might change from time-to-time, but chose to use the rates in effect
when the OCSLA was enacted.

The Secretary’s amendment was discussed at some length on the floor
of the Senate on June 22, 1953. The debate did not focus with precision
on the issue before us now. But one part of the discussion clearly
suggested that Congress did not intend the additional royalty under
section 6(a)(9) to change whenever Texas or Louisiana amended their
tax laws. Senator Cordon, who presented the bill to the Senate on
behalf of the Committee on Interior and Insular Affairs, explained that
section 6(a)(9) would give the Treasury a royalty in addition to the
12½ percent royalty on the existing leases, and that the additional
royalty would be fixed at existing state tax rates:
The provisions for validation of leases do not become operative until, of course, the enactment of the bill. ... As of the time of enactment of the bill, there will thereafter be due nothing to the States; but there will continue to be due to the United States 121/2 percent royalty, plus, after enactment, the equivalent of the State severance, production, or use tax in effect at the time the lease was issued. There are various names for these State taxes, but in essence they are primarily severance taxes.

99 Cong. Rec. 6966 (1953) (Senator Cordon) (italics added). Nothing elsewhere in the debate on the bill suggested that Congress intended the additional royalty to increase or decrease as the States changed their tax laws.

Having considered the text and legislative history of the language directly at issue, we might end our inquiry here. But "the words of a statute must be read in their context and with a view to their place in the overall statutory scheme." Davis v. Michigan Dept. of Treasury, 109 S.Ct. 1500, 1504 (1989). It is therefore sometimes necessary to look beyond "the particular statutory language at issue" and consider "the language and design of the statute as a whole." K Mart Corp. v. Cartier, Inc., 108 S.Ct. 1811, 1817 (1988).

Here that broader look reinforces our conclusion. Elsewhere in the OCSLA, whenever Congress looked to State law to provide a rule of decision, it adopted only those State laws in effect on the date the OCSLA became law. The most prominent example was Congress' decision to adopt State laws as Federal law to supplement existing Federal law governing the OCS. 43 U.S.C.A. 1333(a)(2) (West 1964). In so doing, Congress adopted only those State laws "as of the effective date of this Act." Id. Congress did so at the insistence of the Eisenhower Administration. In the Administration's view, if Congress were to adopt State laws and amendments yet to be enacted, it would be unconstitutionally delegating its legislative power to the States. S. Rep. No. 411, at 33 (letter of Assistant Attorney General Rankin).

Similarly, it would have been considered an improper delegation of authority for Congress to leave the future amount of the additional royalty up to the legislatures of Texas and Louisiana.

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5 Senator Cordon was imprecise in identifying the relevant date as the date the leases were issued. The text before the Senate expressly made the relevant date the date the OCSLA took effect. 99 Cong. Rec. 6965 (1953). A few minutes later, Senator Cordon conceded that, concerning the details of the effective date of sec. 6(a)(9), "I am not too fully advised." 99 Cong. Rec. 6966 (1953).

4 Senator Cordon estimated that sec. 6(a)(9) would make the royalty rate in effect somewhere "between 18 and 19½ percent." 99 Cong. Rec. 6966 (1953). Senator Long estimated that "[t]hus far as Louisiana leases are concerned, that would amount to payments running to almost 20 percent, when the additional royalty is added." 99 Cong. Rec. 6966 (1953). These estimates both refer to the State tax rates in effect in 1953. For example, the Louisiana tax of 26 cents per barrel for high gravity oil was approximately 3 percent of the value of oil in 1953 which averaged $3.00 per barrel. Federal Offshore Statistics 60 (OCS Report MNS 84-0071) (using average for 1954). This 8 percent, added to the basic royalty of 12½ percent, approximates Senator Long's estimate of 20 percent. The 5.72 percent rate in Texas, added to the basic royalty, approximates Senator Cordon's estimate of 18 percent.

Another example of this policy in the OCSLA appears in sec. 6(b), 43 U.S.C. § 1335(b). That section permitted holders of State-issued leases to continue their leases "in accordance with . . . any extensions, renewals, or replacements . . . heretofore authorized by the laws of the State issuing such lease . . . ." Solicitor Armstrong construed that phrase to give assurance to the lessees that nothing shall be done to adversely affect their leases as to the term thereof or any extensions authorized in the lease or authorized by the laws of the State on the effective date of the act. I take this to mean that Congress intended that each such lease should continue according to its terms and the then existing laws of the State issuing it in the same manner and to the same extent as it would have done had it remained under the jurisdiction of the State, except as otherwise limited by the provisions of section 6 . . . .
As far as our review of this Department's published and unpublished decisions reveals, this interpretation of section 6(a)(9) has never previously been questioned. And it is plain from the decision in *Kerr-McGee Industries, Inc.*, 70 I.D. 464, 472 (1963), that the Department considered itself bound by the tax rates in effect in 1953. For in *Kerr-McGee* it applied the 1953 Louisiana rate for natural gas, three-tenths of a cent, to royalties to be paid during 1962 to 1967, even though Louisiana had increased its severance tax on gas to 2.3 cents per thousand cubic feet in 1958. La. Acts 1958, Ex. Sess., No. 2, §2.

The sole judicial opinion on this issue supports this interpretation. In *Ocean Drilling & Exploration Co. v. United States*, 600 F.2d 1343, 220 Ct.Cl. 395 (Ct.Cl. 1979), the issue was whether Ocean Drilling, when filing its tax return, had properly characterized payments to the United States under section 6(a)(9) as royalty or severance tax. Among several reasons why the court concluded the payments were royalty was that the amount was fixed without regard to what the Louisiana legislature might do in the future:

> The statute fixes the additional royalty as the amount of the severance taxes “which would have been payable on such production to the state issuing the lease under its laws as they existed on August 7, 1953.” The amount of the additional royalty to be paid to the United States would be the same even if, after August 7, 1953, the state of Louisiana had reduced its severance tax or even abolished it.

*Id.* at 1347, 220 Ct.Cl. at 402.

**Conclusion**

In calculating the additional royalty owed under section 6(a)(9), the Department must use the tax rates in effect in Texas and Louisiana on August 7, 1953. It has been suggested that this interpretation would permit holders of leases under section 6 to reap a windfall, because if their leases had remained under State jurisdiction, they would be subject to higher severance tax rates today. On this point, it should be noted that all leases maintained under section 6 were originally entered into before December 21, 1948. 43 U.S.C. § 1335(a)(2). The Federal Government has already benefitted under section 6(a)(9) from increases enacted in the Texas and Louisiana tax rates in 1948 and 1951, after the lessees obtained most of their leases. Tex. Acts 1951, 52nd Leg. p. 695, ch. 402 §§ I and III; La. Acts 1948, No. 10, §1.

Although one might argue that Congress could have specifically provided for a different result by tying section 6(a)(9) to State tax rates as they may change from time-to-time, the fact is it did not provide for any such sliding-scale royalty. Such a decision is not for this

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* Ocean Drilling argued the payments were for severance taxes. By characterizing the payments in this way, Ocean Drilling increased its depletion allowance, thus lowering its taxable income. 600 F.2d at 1345, 220 Ct. Ct. at 398-99.

MARTIN L. ALLDAY
Solicitor

PROPER DISBURSEMENT & CREDITING OF MINERAL LEASING REVENUES FROM RECLAMATION ACQUIRED LANDS*

M-36969 September 8, 1989

Act of June 17, 1902—Act of February 2, 1911—Act of May 9, 1938

The requirement of the Acquired Lands Act, 36 Stat. 895, that mineral leasing revenues be distributed "to the same funds or accounts and in the same manner as other receipts from the land affected by the lease" is most fully met for mineral revenues from acquired reclamation lands that have been charged to the reimbursable component of a project by the "credit to the project" disbursement formula. When revenues are generated from acquired lands which have not been charged to a project, a general credit to the Reclamation fund is appropriate. A credit to the annual obligations of the project is not appropriate for mineral leasing revenues from acquired lands because future use of the subsec. I annual credit method was cut off by the Hayden-O'Mahoney Amendment of 1938, 52 Stat. 322, except where such treatment was grandfathered in under that amendment.

Act of June 17, 1902

Credits created by the statutory disbursement of mineral leasing revenues to projects may be used to satisfy new construction obligations in the same manner that such credits were applied against past obligations.

To: Secretary

From: Solicitor

Subject: Proper Disbursement and Crediting of Mineral Leasing Revenues from Reclamation Acquired Lands

This responds to your request that we review the proper method of crediting mineral revenues which are derived from the leasing of Bureau of Reclamation project lands both before and after the construction repayment obligation has been settled.

BACKGROUND

Prior to 1902, Congress had sought the "reclamation" of the West by promoting private efforts at homesteading and irrigation. By the end

* Not in chronological order.

1 Congress carried out it, settlement and reclamation policy through such laws as the Homestead Act of 1862, 12 Stat. 392; 43 U.S.C. §§ 161-284 (repealed 1976) which allowed qualified claimants to enter upon up to 160 acres public domain lands and after complying with certain requirements such as filing, cultivation, residence and tenure, to
of the 1800's, it had become clear that further successful agricultural
development in the West would depend upon massive water projects
involving very large dams, reservoirs, and water delivery systems.
After prolonged consideration, Congress decided that these projects
should be undertaken by the Federal Government.

To accomplish this goal, Congress passed the Reclamation Act of 1902,
32 Stat. 388; 43 U.S.C. § 391 et seq. Sections 1 and 4 of that Act
provided for the creation of a revolving Reclamation fund that would
be used to finance water projects on a reimbursable basis with the
project’s users repaying the monies advanced under 10-year contracts.

Section 3 of the Act stated that public domain lands would be
withdrawn from the operation of the various entry statutes for the
purpose of 1) constructing irrigation works (dams, reservoirs and
canals) and 2) the creation of farms on the newly irrigable lands. Thus,
once an area had been determined as being suitable for an irrigation
project, the Secretary would withdraw from entry both the lands
needed for project works and the lands which could be irrigated from
those works and would then begin to dispose of the farmlands under
the restrictions of the Homestead Act. Under this scheme, there were
occasions where some lands were not immediately disposed of or which,
while serving project purposes, were also amenable to other, income-
producing uses as well such as grazing, timber harvesting or oil and
gas production. This situation resulted in the leasing of these
withdrawn, public domain lands (withdrawn lands) for those purposes
under applicable statutes.

1902 was a comparatively late date in the history of the disposal of
western lands and millions of acres of the best lands which were the
most suitable for irrigation had already been disposed of before the
Reclamation Act of 1902 was passed. In some circumstances, to make
the most efficient use of the irrigated areas and to fulfill project
purposes, the United States reacquired title to previously alienated
lands by purchase or other means and included those “acquired” lands
in Reclamation projects either as a contribution at no cost or on a
reimbursable basis. If lands were contributed on a reimbursable basis,
the costs paid by the United States to reacquire the lands were charged
to the construction obligation of the project which had to be repaid by
the water users. These acquired lands were also subject to leasing if
they were not disposed of but under a different set of authorities than
withdrawn lands.
The Reclamation program did not remain static. It soon became obvious that a 10-year repayment period was unrealistic and that the Reclamation fund as then constituted was insufficient to accomplish the task that had been set of large-scale irrigation in the West. Congress extended the repayment period for project, provided new sources of revenue for the Reclamation fund, allowed projects and irrigators to benefit from reclamation revenues and provided new purposes for reclamation projects in addition to irrigation. Throughout the history of reclamation, Congress has provided assistance for the financing and operation of these projects and then adjusted those incentives as times and economic conditions changed. Some individual projects were created that had their own project-specific entitlements and obligations.

As statutes proliferated over the years, there arose a labyrinthine array of congressional directives for distribution of different types of revenues generated from leases and other activities on reclamation lands. Reclamation lands generate an assortment of revenues from such activities as water sales, electrical power sales, land sales, leasing and grazing. Each of these revenues has at least one specific statute governing the method of revenue distribution which, depending upon the facts of each sale or lease, can be different for the same types of revenue.

These revenue disposition statutes do, however, break down into three main categories: 1) revenues which may be distributed as a general credit to the Reclamation fund; 2) revenues which may be distributed as a “back-end” credit to the reimbursable component of the project; and 3) revenues which may be distributed as a “front-end” credit to the annual obligations of the water users. Each type of crediting system is referred to within the act which employs it by statutory terms of art that the legislative histories show to have specific meaning. General credit statutes state that their subject are to be “paid” or “covered” into the Reclamation fund. Statutes mandating
back-end credits to the reimbursable accounts employ more, extensive language directing disbursal, for example, stating that the revenues are to be "covered into the reclamation fund and be placed to the credit of the project..." or simply "credited to the project..." The front-end credit appears in only one statute which provides that "the net profits from such sources may be used by the water users to be credited annually..." The implications of these statutory terms of art will be more fully developed below, as an understanding of the operation or each of these types of credits is essential for determining the proper distribution of mineral revenues from project lands.

We first examine the method of distribution involving a general credit to the Reclamation fund. When the revenues from Federal lands are collected, they are first placed in the Treasury. Within the Treasury are separate accounts to which are credited the various revenues assigned to them by law and appropriation. One of these accounts is the Reclamation fund. The first method of revenue distribution we consider consists of taking certain revenues and placing them as a general credit to this fund. That means the monies are not targeted to be spent on specific functions or projects but are available to be spent as directed by the laws governing the fund.

Congress provided for the first general credit revenue to the Reclamation fund when it passed the Reclamation Act in 1902. It provided in section 1, 43 U.S.C. § 391:

All monies received from the sale and disposal of public lands in [the sixteen western States]. . . shall be, and the same are hereby, reserved, set aside, and appropriated as a special fund in the Treasury to be known as the "reclamation fund," to be used in the examination and survey for and the construction and maintenance of irrigation works and storage, diversion, and development of waters for the reclamation of arid and semiarid lands in the States and Territories, and for the payment of all other expenditures provided for in this act.

These public lands, generally, had nothing to do with the Reclamation program and no costs for them had been charged to any projects; their sale was simply intended to provide funding for the Reclamation effort. Section 5 of the same Act, 43 U.S.C. § 392, extends this same crediting system to "all moneys received from entrymen or applicants for water users..."

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12 See e.g., 43 U.S.C. §§ 374, 526.
14 This entire background explanation, while generally accurate as far as it goes, is not intended as a definitive discourse on all aspects of Reclamation accounting. Since the passage of the 1939 Projects Act, 43 U.S.C. § 485, the cost of Reclamation projects has been divided among different purposes. Some of these purposes or functions are designated as non-reimbursable and some functions may produce revenues which are used to aid the repayment of other functions. This situation may result in further allocations of revenues once they have been credited to a project. A further complicating factor is that interest is charged on the construction debt of some project functions. When projects are in the M&I phase, the fact that the construction debt has been amortized with interest may require that revenue credits must be applied directly to principal in such a manner as to shorten the repayment period without affecting the yearly obligation of the water users. This crediting method will have the same effect as a back-end credit as intended by Congress in the relevant acts because the water user's annual payments will be unchanged.
rights . . .” Again, the purpose of these provisions was to get revenue into the Reclamation fund for use in building reclamation projects.

The revenues from public land sales were insufficient to provide for all of the needed projects, so Congress passed the Act of July 17, 1919, 41 Stat. 202; 43 U.S.C. § 394. That statute forms the basis for allocation of reclamation lease revenues by providing that the proceeds from leasing withdrawn or reserved reclamation lands are to go as a general credit to the Reclamation fund. The Act provides:

The proceeds heretofore or hereafter received from the lease, of any lands reserved or withdrawn under the reclamation law or from the sale of the products therefrom shall be covered into the reclamation fund; and where such lands are affected by a reservation or withdrawal under some other law, the proceeds from the lease of land and the sale of products therefrom shall likewise be covered into the reclamation fund in all cases where such lands are needed for the protection or operation of any reservoir or other works constructed under the reclamation law, and such lands shall be and remain under the jurisdiction of the Secretary of the Interior.

Note that this Act involves revenues from withdrawn lands that had been contributed at no cost to the projects by the United States and so the revenues were provided as a general credit to increase the size of the fund.

This pattern of supplying revenue to the Reclamation fund was chosen again in 1920 in both the Mineral Leasing Act of 1920 and the Federal Water Power Act of 1920, 41 Stat. 1063; 16 U.S.C. § 810. The Mineral Leasing Act is a very important general credit statute because it provided huge revenues from non-Reclamation lands to help finance the fund. (This Act will be discussed more fully at page 61.) These provisions augmented the fund with power and mineral revenues. This distribution system was retained when the Federal Water Power Act was amended as the Federal Power Act in 1935, 49 Stat. 845; 16 U.S.C. § 810. The general Reclamation fund credit was also adopted both as a general guide for revenues derived from nonreimbursable sources and as a specific method of crediting for a percentage of the royalties from the Naval petroleum reserves in the Hayden-O'Mahoney Amendment, 52 Stat. 322; 43 U.S.C. § 392a. The other two methods of revenue crediting are more detailed and involve directing funds to specific accounts within the Reclamation fund. Each Reclamation project has one of these accounts which is divided in turn into even more accounts which represent the various obligations of the project. One of the sub-accounts within the general project account is the debt incurred by the project for the money spent to construct the project. Because the construction component must be repaid, it is referred to as a reimbursable account. The construction

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16 The preceding selection of statutes requiring credit to the reclamation fund is not exhaustive but show a recurring pattern adopted by Congress over a period of years.

18 Many kinds of expenditures are included in this debt; costs of materials, construction costs, in some cases interest, in some cases the cost of any lands which had to be acquired for the creation of the project, and other costs.
PROPER DISBURSEMENT & CREDITING OF MINERAL LEASING REVENUES
FROM RECLAMATION ACQUIRED LANDS

September 8, 1989

obligation is amortized or broken down into fixed yearly payments, each payment due in chronological order.

The two additional crediting methods, back-end and front-end, both require that revenues be applied against the reimbursable construction obligation for the project. The main difference between the back-end credit to the reimbursable component of a project and the front-end credit to annual obligations of a project consists of the manner in which revenues are applied against the amortized installments of the reimbursable construction obligation. A front-end credit to annual obligations would go to satisfy the payment due currently. It also allows revenues in excess of the annual construction obligation to be applied against operation and maintenance or other water-user obligations).

A back-end credit, however, is applied against the last payment due and so reduces the total debt but without satisfying the current amount due. Thus, in the case of a back-end credit, if a project's construction repayment were amortized over twenty years, then the revenues received as a credit to the project would be applied against the obligation due on the back-end or twentieth year, and then on the nineteenth year, and so on until the obligation had been paid. As the water users would still be making their annual, or front-end, payments on the construction obligation, the net result would be an accelerated repayment of the project's construction cost. Because this back-end credit serves to pay off the project's construction cost without relieving the project users of their requirement to pay their annual obligations, the back-end credit is called a "credit to the project" in those laws that incorporate it.

Another feature of the credit to the project or back-end credit is that Congress seems to have allowed this method in only those cases where the cost of the lands or facilities that produced the revenues to be credited had been charged to the reimbursable construction debt of the project. The necessary link between reimbursements and a credit to the project will be more fully discussed at page 63.

The first apparent use of the back-end credit to the project formula occurred in 1911 when Congress provided an additional means of crediting reclamation revenues. The Act For the Sale of Surplus Acquired Lands of 1911, 36 Stat. 895, 43 U.S.C. § 374, states:

whenever in the opinion of the Secretary of the Interior any lands which have been acquired under the provisions of the . . . "reclamation act" or under the provisions of any act amendatory thereof or supplementary thereto . . . for any irrigation works . . . are not needed for the purposes for which they were acquired . . . said Secretary of the Interior may . . . sell the same . . . The moneys derived from the sale of such lands shall be covered into the reclamation fund and be placed to the credit of the project for which such lands have been acquired. (Italics added.)
This method was specified again in 1920 as the proper way to credit proceeds from the sale of water for miscellaneous purposes to the credit of the project that supplied the water in 41 Stat. 451; 43 U.S.C. § 521. Also in 1920, Congress enacted legislation requiring the proceeds from the sale of reclamation public domain lands that had been improved at the expense of the Reclamation fund to be credited to the project for which such lands had been withdrawn. 41 Stat. 605; 43 U.S.C. § 375.

A particularly noteworthy application of this accounting method is subsection J of the “Fact Finder’s Act” of 1924, 43 Stat. 703; 43 U.S.C. § 526. This subsection provides:

All moneys or profits as determined by the Secretary heretofore or hereafter derived from the sale or rental of surplus water under the Warren Act . . . or from the connection of a new project with an existing project shall be credited to the project or division of the project to which the construction cost has been charged. (Italics added.)

Subsection J is of particular interest because it spells out the rationale for crediting revenues to the project as stemming from the fact that the initial cost has been charged to the reimbursable construction component that must be repaid by the users.17

In 1930, Congress again used the back-end credit to the project formula when it specified that monies collected from defaulting contractors were to be credited to the project on whose behalf a contract was made. 46 Stat. 522; 43 U.S.C. § 401.18

The last statutory method of revenue crediting is a front-end credit to the water user’s annual obligations. In contrast to the credit to the project or back-end credit, the front-end credit merely relieves the water users from the necessity of making payments toward their annual obligations. Thus a front-end credit is not a credit to the project, but a credit to the water user and so this front-end water user credit is also referred to as an annual credit. This scheme is found only in subsection I of the Second Deficiency Appropriation Act for 1924 or Fact Finder’s Act (subsection I), which states:

Whenever the water users take over the care, operation, and maintenance of a project, or a division of a project, the total accumulated net profits, as determined by the Secretary, derived from the operation of project power plants, leasing of project grazing and farm lands, and the sale or use of town sites shall be credited to the construction charge of the project, or a division thereof, and thereafter the net profits from such sources may be used by the water users to be credited annually, first, on account of project construction charge, second, on account of project operation and maintenance charge, and third, as the water users may direct. No distribution to individual water users shall be made out of any such profits before all obligations to the Government shall have been fully paid.

17 Because under sec. 4 of the 1902 Act, the users had to repay essentially all costs attributable to the project, such language detailing the crediting of revenues to the project charged would be unnecessary. It was only necessary to say which revenues could be credited as the project was to be charged for everything. In the case of Subsec. J, where two different projects were to be connected, only the project that had been charged with the costs was to receive the revenues.

18 The above statutes do not constitute a complete list of the laws with a credit to the project formula but are sufficient to illustrate what the method is and, to an extent, how it works.
This is a straightforward statute allowing water users to receive credit on their annual obligations for certain specific project revenues from specific sources.

DISCUSSION

I. DISTRIBUTION OF MINERAL REVENUES

The first issue we address here is the proper distribution of mineral leasing revenues from project lands. You have asked that, in addressing this issue, we include an analysis of proper distribution both before and after the construction repayment obligation has been settled. Because they are treated differently under the statutes, we must separately address withdrawn and acquired lands.

A. Withdrawn Lands and the Mineral Leasing Act of 1920

The first statute to specifically deal with the general disposition of the revenues from withdrawn Reclamation lands was the Act of July 19, 1919, 41 Stat. 202; 43 U.S.C. § 394, which gave the Reclamation fund all the proceeds from all revenues generated by leases or sales of products from withdrawn Reclamation lands, e.g., as timber. That statute, however, did not apply to mineral lease revenues because at that time there was no statutory authority to lease minerals on Federal lands.

The next year, Congress passed the Mineral Leasing Act of 1920, 41 Stat. 813; 30 U.S.C. §§ 181-287 (as amended). This Act made several important changes in both the disposition policy for public domain lands and in the funding of the Reclamation program. Instead of allowing public domain lands with certain mineral deposits to be sold or claimed through patents under the General Mining Law of 1872, 30 U.S.C. §§ 21-42, 30 U.S.C. § 181 of the Mineral Leasing Act provides that “deposits of coal, phosphate, sodium, potassium, oil, oil shale, gilsonite (including all vein-type solid hydrocarbons), or gas and lands containing such deposits owned by the United States . . .” were no longer to be alienated from ownership by the United States but were to be leased instead. 30 U.S.C. § 191 (as amended) mandates that “all monies received . . . shall be paid into the Treasury of the United States; 50 per centum thereof shall be paid . . . to the State . . . within the boundaries of which the leased lands or deposits are or were located; 40 per centum thereof shall be paid into . . . the reclamation fund . . .” with the remaining 10 percent going to the Treasury as miscellaneous receipts.

This new congressional provision vastly increased the amount of lands from which revenues would flow into the Reclamation fund. This is a general credit to the Reclamation fund statute where revenues from lands unrelated to the Reclamation program are placed into the fund to help it grow. Revenues from leases of the specified minerals from
withdrawn reclamation lands distributed according to the formula found in the Mineral Leasing Act. 19

B. Acquired Lands and the Acquired Lands Act of 1947

Congress addressed the question of leasing mineral deposits on lands acquired by the United States in the Mineral Leasing Act For Acquired Lands of 1947 (Acquired Lands Act), 61 Stat. 913; 30 U.S.C. §§ 351-59 (as amended). The minerals covered under the Acquired Lands Act are listed in 30 U.S.C. § 352 and are essentially the same as those covered by the Mineral Leasing Act of 1920, specifically, "all deposits of coal, phosphate, oil, oil shale, gilsonite (including all vein-type solid hydrocarbons), gas, sodium potassium, and sulfur . . . or lignite . . . ." Section 355 specifies that the revenues of such leases are to be disbursed as follows:

All receipts derived from leases issued under the authority of this chapter shall be paid into the same funds or accounts in the Treasury and shall be distributed in the same manner as prescribed for other receipts from the lands affected by the lease, the intention of this provision being that this chapter shall not affect the distribution of receipts pursuant to legislation applicable to such lands . . . . (Italics added.)

Thus the proper method of distributing mineral leasing revenues from reclamation acquired lands will be determined by finding other statutes that provide for the distribution of other types of revenues from the same lands and disbursing the mineral leasing revenues in the same manner. 20

As has been described above, there are three general methods established in the statutes for distribution of revenues from reclamation lands: 1) credit generally to the Reclamation fund; 2) back-end credit to the construction obligation of a project or credit to the project; and 3) front-end credit against the annual obligations of the water users. Our task is to determine which of these distribution schemes should be used under the 1947 Act in distributing mineral revenues from acquired reclamation lands.

A review of the myriad statutes applicable to distribution of revenues from acquired lands leads us to conclude that Congress has differentiated between revenues produced by lands and facilities donated by the United States to a project and those for which the United States has received reimbursement from project users. In the first instance, Congress has generally indicated its intent that the revenues be credited to the Reclamation fund. In the second instance,

19 See Memorandum of Assistant Solicitor Leggette, acting for Associate Solicitor Sanzenetti on Sept. 6, 1988, pp. 47-50.

20 It is essential to remember that title to these project lands, whether withdrawn or acquired, resides in the United States as stated in secs. 6 and 7 of the Reclamation Act of 1902, supra, and that the revenues which derive therefrom are the revenues of the United States. The Constitution of the United States in art. I, sec. 9 states that no funds may be paid from the Treasury without an appropriation by law. This restriction is reinforced by 31 U.S.C. § 1301(d) which specifies that "a law may be construed to make an appropriation out of the Treasury . . . only if the law specifically states that an appropriation is made . . . ." The standard for finding an appropriation is very high so that appropriations may not be inferred or made by implication. See Solicitor's Opinion, M-36942, 88 I.D. 1090, 1092 (1981) and 50 Comp. Gen. 883 (1971). Therefore, particular care must be used in determining the proper distribution of Federal revenues. 30 U.S.C. § 355, like 30 U.S.C. § 191 in the MLA, is a permanent indefinite appropriation.
Congress has generally credited revenues to the projects producing them. For the reasons given below, we believe this second means of crediting is the scheme properly applied under the 1947 Acquired Lands Act.

A common strain that runs through the revenue allocation statutes that provide for a general credit to the Reclamation fund is that the cost of the lands, projects or governmental functions that produced the revenues involved had never been charged against the users of any project, see, e.g., the Reclamation Act of 1902, supra; the MLA, supra; the Federal Water Power Act of 1920, supra; and the Federal Power Act of 1935, supra. The lands producing most of these revenues had nothing whatever to do with the Reclamation program. All these laws were efforts by Congress to enrich the Reclamation fund so that it would have sufficient resources to carry out its mission of providing water for the West. These statutes provided funding for the Reclamation fund by taking revenues from such disparate sources as lands unrelated to reclamation together with power licensing revenues as well as irrigation and power revenues from projects that had been paid for by the United States, and putting them into the Reclamation fund. Because these revenues originate from sources that were not paid for by anyone but the Federal Government, it is obvious that this is Federal funding in the fullest sense and the express direction of Congress was that these revenues were to go to the Reclamation fund as a general credit.

In the Hayden-O’Mahoney Amendment, 52 Stat. 322; 43 U.S.C. §§ 391a-1, 392a, Congress emphasized the point that moneys derived from sources that did not create a reimbursement obligation from a project to the Federal Government should go as a general credit to the Reclamation fund. This Act first provided for revenues from leases of lands in the Naval Petroleum Reserves to be added to miscellaneous appropriations already disbursed from the Treasury to the Reclamation fund to keep the latter solvent. It should be noted that the revenues from the Naval Petroleum Reserves and the appropriations from the general Treasury are unrelated to the Reclamation program. Thus, when Congress directed that these funds be applied as a general credit to the Reclamation fund, Congress was perfectly consistent with its prior approach of distributing revenues derived from non-Reclamation sources or from sources for which water users did not have to repay the costs. In furtherance of this policy, after providing for the appropriation, the Act further states:

All moneys received by the United States in connection with any irrigation projects, including the incidental power features thereof, constructed by the Secretary of the Interior through the Bureau of Reclamation, and financed in whole or in part with moneys heretofore or hereafter appropriated or allocated therefor by the Federal Government, shall be covered into the reclamation fund, except in cases where provision
has been made by law or contract for the use of such revenues for the benefit of users of water from such project.

Thus, the revenues from lands or facilities for which the water users do not pay the costs but whose costs are instead borne by the United States on a non-reimbursable basis shall go as a general credit to the Reclamation fund. This is a reasonable provision in a law that was intended to increase the revenues available for Reclamation projects.

In keeping with this intention, under the terms of the Acquired Lands Act, the proper crediting formula for mineral revenues produced by acquired lands that have not been charged to a project on a reimbursable basis is that of a general credit to the Reclamation fund. Where these lands are a free donation by the United States to the various projects, as is the case with other contributions, the recipient is the Reclamation fund general account. There are, however, statutes that provide that, when the project users must ultimately repay the costs of the lands or facilities that produce the revenues, another result will obtain.

Our review indicates that reimbursability changes the distribution scheme of mineral revenues derived from acquired lands. Repayment of funds advanced from the Reclamation fund and used for construction has been a feature of the Reclamation program since section 4 of the Reclamation Act of 1902 which provides:

Upon the determination by the Secretary of the Interior that any irrigation project is practicable, he may cause to be let contracts for the construction of the same, in such portions or sections as it may be practicable to construct and complete as parts of the whole project, providing the necessary funds for such portions or sections are available in the reclamation fund, and thereupon he shall give public notice of the lands irrigable under such project, and limit of area per entry, which limit shall represent the acreage which, in the opinion of the Secretary, may be reasonably required for the support of a family upon the lands in question; also of the charges which shall be made per acre upon the said entries, and upon lands in private ownership which may be irrigated by the waters of the said irrigation project, and the number of annual installments, not exceeding ten, in which such charges shall be paid and the time when such payments shall commence. The said charges shall be determined with a view of returning to the reclamation fund the estimated cost of construction of the project, and shall be apportioned equitably.21 (Italics added.)

A back-end credit to the project expands the concept of repayability established in section 4 by allowing project revenues to be used, not as a general credit to enlarge the fund, but as a project credit to pay off the individual project. Reimbursability is a feature of each of the statutes cited above allowing a credit to the project. In each case the cost of lands or facilities that produced the credited revenues had been charged to the project’s reimbursable construction account under section 4 of the 1902 Act or some other Reclamation statute. The Act For the Sale of Surplus Lands of 1911, 36 Stat. 895; 43 U.S.C. § 374, involved the sale of acquired lands that had been charged to the projects. The 1920 Act for supplying water for purposes other than

21 See also the Reclamation Extension Act of 1914, 38 Stat. 686; 43 U.S.C. § 414, 471 etc.
irrigation involved a product, storage water, of facilities that were paid for by project users. See 41 Stat. 451; 43 U.S.C. § 521. A subsequent 1920 act granted a project credit for the revenues from sales of withdrawn lands that had been improved at the expense of the water users. See 41 Stat. 605; 43 U.S.C. § 375. This Act is striking because, under the terms of the Reclamation Act of 1902, revenues from the sale of withdrawn lands are to go to the general account of the Reclamation fund; in the 1920 Act, by contrast, Congress allowed the proceeds from both the lands and the improvements to go to the credit of the project when the costs of the improvements had been charged to the project. This approach was continued in subsection J of the Fact Finder's Act in 1924, 43 Stat. 703; 43 U.S.C. § 526, and the defaulting contractors act in 1930 as well. See 46 Stat. 522; 43 U.S.C. § 401.

That Congress favored a back-end credit to the project where reimbursability or the cost of the revenue-producing feature was involved is also abundantly clear from the legislative histories of the various acts providing for credits to projects. In 1914, Congress authorized the Secretary to sell public lands once set aside for parks and community centers but which had reverted back to the United States because they were not so used. 43 U.S.C. § 569(c), Act of October 5, 1914, § 4. The costs of supplying water to such facilities at that time were charged to the reimbursable project construction costs. 43 U.S.C. § 569. As originally proposed, the bill that became section 569 directed that proceeds from sales under its authority "shall be turned over to the organization representing the owner of the lands within such project." When the Department commented on the bill, S. 657, it objected to this language and suggested substituting language that was consistent with Departmental policy. The Department's letter stated:

Proceeds . . . should be covered into the reclamation fund and placed to the credit of the project . . . as is the general practice under existing laws relating to the disposal of lands or resources within reclamation projects, rather than turned over to the organization representing owners of the land . . .

[After management of project works has passed to the water users] moneys derived from the sale of lands and water rights in the several projects are required to be returned to the reclamation fund. The irrigable lands utilized for park purposes will be relieved from contributing their proportion of project costs, enhancing to that extent the costs of water rights on other lands in the projects, and it would seem that any lands or rights reverting, or not contracted for, should be turned back to the project and disposed of to aid in repaying its cost.

S. Rep. No. 426, 63d Cong., 2d Sess. 2 (1914). Congress adopted the proposed revision. Therefore, as to the disposition of revenues from the sales of these lands, Congress directed:

[The proceeds from the disposition of lands reverting to the United States under the provision of this act and from the sales of water rights, shall be covered into the Reclamation fund and placed to the credit of the project wherein the lands are situate.
The Act of May 20, 1920, 43 U.S.C. § 375, authorized the sale of withdrawn lands improved at the expense of the Reclamation fund. That Act also directed that proceeds from those sales were to be covered into the Reclamation fund and credited to the project. The Secretary of the Interior commented favorably on the legislation. His letter demonstrates the Department's position on the meaning of the term "credit to the project" and explains the policy behind crediting specific revenues to the project:

Frequently lands which have been withdrawn for construction or operation and maintenance purposes in connection with a reclamation project and which have been improved at considerable expense to the reclamation fund become no longer necessary for the interests of the project. These improvements are frequently of such a character that they are not removable without material depreciation or total destruction of value.

The moneys expended in improvements upon this class of lands come from the reclamation fund and are charged to the water users on the project who are required to repay such expenses. In order to keep down the charges against the water users to the lowest practicable point it is important that lands of this character no longer needed and the improvements thereon should be so disposed of as to reimburse the project for the expenditures made.

S. Rep. No. 367, 66th Cong., 2d Sess. 2 (1920). Thus, the credits were intended to reduce the overall cost of the project that the water users would be required to repay.

Thus, when revenues are derived from acquired lands which have been charged to a project on a reimbursable basis, those revenues should not be credited to the Reclamation fund generally but should go as a back-end credit to the project from which they came.

In the past, however, the Bureau of Reclamation has used subsection I of the Fact Finder's Act, requiring a front-end credit, as a pattern for distribution of mineral leasing revenues. Our review indicates that subsection I treatment is not appropriate for mineral revenue distribution except where there is specific statutory authorization for such distribution.

The purpose of the credit to the project in the statutes cited above was to make the Reclamation fund revolve faster and to reduce the cost of the projects to the users, but not to make their annual payments for them. This faster payment of outstanding project debts was accomplished by requiring that the credit be applied as a back-end credit to the project's construction obligation. Since the project revenues were applied against the last installment due on the construction obligation and the water users were still required to make their annual payments on the current installment of the same debt, the fund was repaid (or revolved) faster and the cost of the projects were ultimately reduced for the users.22 If a back-end credit was not

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22 The accelerated revolving of the fund was particularly desirable as repayment periods extended from 10 years under the 1902 Reclamation Act to 40 and 50 years under later statutes.
required and a front-end credit were allowed, the number of years in which payments were due would not be decreased and thus the debt to the United States would not be repaid any faster and the Reclamation fund would recognize no increase in funds available for new projects or programs. See Sundry Civil Appropriations Act for 1918: Hearings on H.R. 11 Before the House Committee on Appropriations, 65th Cong., 1st Sess. at 638 (1917), which is reproduced on p. 31, infra.

That “credit to the project” is a statutory term of art that mandated a back-end credit also is clearly shown by the legislative history of various statutes cited. In addition to establishing the meaning of the term “credit to the project,” the Secretary’s statement cited above regarding the Act of May 20, 1920, reveals the purpose of such back-end credits. Although the lands to be sold were withdrawn lands and contributed by the United States to the project at no cost to the users, money from the Reclamation fund had been expended to construct improvements on those lands. The water users were obligated to repay the costs of those improvements. Therefore, the sale proceeds would be applied to reduce the overall project costs and thereby reduce the obligation owed by the project beneficiaries to reimburse the Reclamation fund. S. Rep. No. 367, 66th Cong., 2d Sess. 2 (1920).

The general rule that such project revenues should credit the overall reimbursable obligation and not reduce the water users’ annual payments was also discussed in hearings before the House Committee on Appropriations in 1917. At that time, section 5 of the Town Sites and Power Development Act controlled the disposition of revenues derived from leases of surplus power or power privileges. Section 5 directed that they should be “covered into the reclamation fund and be placed to the credit of the project from which such power is derived.” 43 U.S.C. § 522. When questioned about the disposition of power revenues by the Appropriations Committee Chairman, the Director of the Reclamation Service discussed how those revenues would be distributed under current law and discussed a public notice alerting those concerned as to the required disposition of those revenues:

Director Davis: The public notice requires them to pay the cost of operating and maintaining the reservoir and canal system for irrigation and 2 percent of the total construction charge. The cost of operating the power plant is paid out of the power receipts and the net returns are credited on the cost of the project, which is applied on the last payment, and when that is liquidated then the next to the last, and so on . . .

. . . The way that is expressed in the public notice is this:

“The money derived from the leases of surplus power or power privilege will be covered into the reclamation fund and be placed to the credit of the project. Whenever the proportionate part of the moneys so credited to the project shall equal the unpaid portion of the construction charge on account of any water-right application, no further payment on account of such water right application will be required.”
Sundry Civil Appropriations Act for 1918: Hearings on H.R. 11 Before the House Committee on Appropriations, 65th Cong., 1st Sess. at 638 (1917). The Committee Chairman questioned Director Davis about the possibility of crediting such revenues to reduce users' annual payments instead of reducing the overall reimbursable construction obligation.

Director Davis: If the net power receipts were credited to the current payments as they come due it would more than cover them for the first four years and the surplus of those four years and the receipts would about cover them for the next two years, so that for six years the power profits would pay the entire construction charges and after the sixth year they would pay about one-half of what the law requires.

The Chairman: While it would be very advantageous to [the users] it would be very unjust to the reclamation fund and the project?

Mr. Davis: Yes, sir. The result would be that the Government's investment in the power plant would remain unliquidated for the entire 20 years, whereas now the effect will be to liquidate that entire investment in power very much sooner . . .

It is now held by the law officers of the Reclamation Service, and I think also the department, that this method of crediting that I gave described is required by the law, and I think it will continue to be so held unless Congress changes it. I think there is little doubt about that.

Id. at 639. Thus, when Congress used the term "credit to the project," it meant that revenues were to be applied to the total reimbursable construction obligation of the project, reducing the total amount project beneficiaries would repay, but not subsidizing current annual construction repayment or operation and maintenance installments. As these hearings show, Congress emphasized reducing the cost of the project, recouping the project investment as quickly as possible, and therefore, making that money available for other reclamation activities. "Credit to the project" statutes placed the priority on recouping the project investment and on benefitting the reclamation program as a whole—not on benefitting individual beneficiaries at the expense of the program. Id.

This conclusion was also reached in the Memorandum of Associate Solicitor Fisher on October 26, 1956, in re Proposed Use of Water by Public Service Company of Colorado-Grand Valley Project, Colorado. The situation considered in that memorandum involved the sale of irrigation water for municipal use from a project for which the irrigation district had been charged with the construction costs. The Associate Solicitor ruled that the water could either be sold under the terms of the 1920 Act for Sale of Water for Miscellaneous Purposes, supra, or the Reclamation Project Act of 1939, 53 Stat. 1187; 43 U.S.C. § 485h(c). He ruled that irrespective of the statutory authority for the water sale:

Revenues arising from the furnishing of water to the Public Service Company should be applied as a credit to the obligations of the Association and the District, said obligations being both the respective construction costs and the R&B (rehabilitation and betterment) costs. In applying this revenue it should be made as a tail-end credit on the total of both
PROPER DISBURSEMENT & CREDITING OF MINERAL LEASING REVENUES FROM RECLAMATION ACQUIRED LANDS

September 8, 1989

obligations of each organization and would not be applied annually on the Association's and the District's construction charge obligation as they propose.

Any contract entered into (should) make clear that revenues received by the United States shall be credited to the obligations of the Association and the District proportionately until such obligations are paid in full by the Association and the District, then the revenues (should) be retained by the United States pursuant to existing law.

Those advocating a front-end credit for mineral revenues from acquired lands cite the use of that treatment in subsection I of the Fact Finder's Act. Our research indicates that subsection I represented a unique situation not repeated again in Reclamation law and specifically disfavored in the Hayden-O'Mahoney Amendment. Subsection I is an isolated statute, in which even revenues from withdrawn lands were given as a direct subsidy to water users rather that to fulfill Congress' traditional purpose of strengthening the Reclamation fund. The name of the Act is instructive, for the Second Deficiency Appropriation Act for 1924 or Fact Finder's Act was a response to an investigation into the rash of defaults by water users on their obligations during the agricultural depression following World War I.23 In this light it is clear that subsection I was an aberration which was never repeated and which in the 1938 Hayden-O'Mahoney Amendment Congress said should have no new applications.24

This conclusion is clearly supported by not only the language of the law but also the legislative history of Hayden-O'Mahoney which indicates that any new use of credit to annual obligations which are provided for in subsection I is cut off by the amendment. In general,

23 In a prefacing message to a report to the Senate on irrigation reclamation in 1924 which led to the Fact Finder's Act, President Calvin Coolidge wrote the following:

I would respectfully urge on Congress the immediate necessity of revising the present reclamation law. The Secretary of the Interior appointed a special advisory committee of six members to study reclamation and make report to him. That committee has completed its work and has made its report to the Secretary of the Interior and he has transmitted that report to me. I herewith transmit it to you.

Many occupants of our reclamation projects in the West are in financial distress. They are unable to pay the charges assessed against them. In some instances settlers are living on irrigated lands that will not return a livelihood for their families and at the same time pay the money due the Government as it falls due. Temporary extensions of time and suspension of these charges serve only to increase their debts and add to their hardships. A definite policy is imperative and permanent relief should be applied where indicated. The heretofore adopted repayment plan is erroneous in principle and in many cases impossible of accomplishment. It fixes an annual arbitrary amount that the farmers must pay on the construction costs of projects regardless of their production.

Because of high rates of interest and other agricultural difficulties existing farmers are often unable to borrow money for temporary relief. The establishment of a credit fund by the Government from which farmers on projects may secure capital to make permanent improvements, buy equipment and livestock, should be considered. More than 30,000 water users are affected by the present serious condition. Action is deemed imperative before the adjournment of Congress that their welfare may be safeguarded.

The probable loss and the temporary difficulties of some of the settlers on projects does not mean that reclamation is a failure. The sum total of beneficial results has been large in the building up of towns and agricultural communities and in adding tremendously to the agricultural production and wealth of the country. Whatever legislation is necessary to the advancement of reclamation should be enacted without delay.

S. Doc. No. 92, 68th Cong., 1st Sess. IX (1924). See also pages 36-40 and 121-131. id.

24 There are limits on the application of subsec. I revenues as well. They may not be distributed as profits but may only be used as credits against project related costs such as O&M. See 16 U.S.C. § 825.
the intent of Hayden-O'Mahoney was to secure additional funds for the Reclamation fund and to achieve a quicker payout of projects. See Memorandum of Associate Solicitor Leshy on July 11, 1978, in re Quincy-Columbia Groundwater Revenue Dispute. A credit to a project would accomplish this; a credit to annual obligations would not.

The following colloquy between Commissioner Page and the Committee Chairman demonstrates that Congress meant to terminate subsection I treatment of revenues in Hayden-O'Mahoney:

THE CHAIRMAN: Under the provisions of the [prior] reclamation laws, as I understand it, the cost of the project in its entirety has been allocated to the land, paid for by the [irrigation] water users, and when the payments are completed by the water users, whether they get title to the power plant or not, [they] still own that energy and the revenue from the sale of energy goes to them, or is income to the water users of the district and is used by them as they see fit.

MR. PAGE: That is the general provision.

THE CHAIRMAN: That is not affected?

MR. PAGE: No; that is not affected in this bill, nor is it by the Hayden-O'Mahoney amendments.

THE CHAIRMAN: But there is nothing anywhere in the terms of this act that such contracts shall be made.

MR. PAGE: That is right. Under the Hayden-O'Mahoney amendment a new contract of that kind could not be made.


The conclusion that Hayden-O'Mahoney cut off subsection I treatment is supported by the conclusion reached by Solicitor Melich when reviewing the entitlements of the Strawberry Valley Project in Solicitor's Opinion, M-36863, August 8, 1972, 79 I.D. 514. After finding that because of the project-specific Act of April 4, 1910, the project was entitled to use grazing and power revenues as a credit against operation and maintenance after construction costs had first been repaid, he states at 519:

In reaching this conclusion, we also find that Strawberry Valley Project is exempted (sic) from the application of the Hayden-O'Mahoney Amendment (Act of May 9, 1938, 43 U.S.C. sec. 392a). If applicable to the Strawberry Valley Project, the Hayden-O'Mahoney Amendment would have required that net power revenues from the Government's investment in the power system be deposited in the Treasury after such investment had been repaid, instead of continuing to be available for disposition under subsection I, as provided by the 1940 contract.

The impropriety of future Subsection I contracts is also reinforced in a Memorandum from Associate Solicitor Leshy regarding the Quincy-Columbia Groundwater Revenue Dispute dated July 11, 1978, which states:

Quincy-Columbia argues that the Hayden-O'Mahoney Amendment contains an exception to this general rule if a contract exists which provides for the use of the revenues for the benefit of project users...
We have now concluded that the existence or nonexistence of such a contract is immaterial because the exception in the Hayden-O'Mahoney Amendment was intended only to protect pre-existing contract rights. Congress never intended to give the Secretary or Interior the discretion to provide for distribution of net project revenues as he saw fit, simply by entering into contracts providing for a different disposition of the funds. Rather, Congress wished only to protect certain specific project beneficiaries who feared that the legislative process was impairing a contract already in existence.

It thus becomes clear that, in Hayden-O'Mahoney, Congress allowed revenues to continue to be used to increase the Reclamation fund as a general credit or make it revolve faster as a credit to the project construction obligation, but not to meet the annual obligations of the users. For this reason we conclude that it would be highly inappropriate to choose a subsection I, annual obligation credit as a pattern for mineral revenue distribution under the Acquired Lands Act.

C. Distribution of Revenues after Payout

You also asked whether repayment of a project construction obligation will affect the distribution of revenues. There will be no change in the distribution of revenues from withdrawn lands. Payout will make a difference, however, with respect to mineral leasing revenues from acquired lands.

While the credit to the project formula is appropriate for distribution of revenues from acquired lands so long as there is a construction obligation on the part of the project to which these revenues may be credited, its use is more problematic when there is no reimbursable construction charge which may be credited with the revenues. This is a problem which was never contemplated by Congress. From its inception in 1902, Congress envisioned that when the users had paid off the cost of the projects, they would, with congressional approval, take title to the works. Of course, this has not occurred as anticipated in 1902.

This situation was addressed in Solicitor's Opinion, M-36863, as cited above in part, when the Solicitor noted that:

If applicable to the Strawberry Valley Project, the Hayden-O'Mahoney Amendment would have required that net power revenues from the government's investment in the power system be deposited in the Treasury after such investment had been repaid, instead of continuing to be available for disposition under subsection I, as provided by the 1940 contract.

25 There are some few districts such as the Strawberry District in Utah which, under the specific terms of their enabling legislation, are eligible to receive subsec. I treatment for various non-subsec. I project revenues. See Solicitor's Memorandum, M-36863, Aug. 8, 1972, supra. It is very likely that the variation in the entitlements of these unique districts is the reason that any erroneous applications of subsec. I were made. In addition, a district which has a pre-1938 contract with subsec. I language will be entitled to the specified revenues credited in the specified manner. Associate Solicitor Leshy makes it quite clear that the Strawberry District was the primary reason the grandfather clause was inserted in subsec. I. See Memorandum of Associate Solicitor Leshy, supra.

26 See e.g., sec. 6 of the Reclamation Act of 1902.

27 The Bureau of Reclamation's listing of district repayment standings entitled Status of Irrigation Districts with Respect to Reclamation Law (Apr. 1, 1989) shows that title for very few, if any, project works have passed to the districts.
A 1956 Memorandum of Associate Solicitor Fisher, quoted from above, also indicates that revenues from paid-out projects are not to be credited to those projects.

Any contract entered into (should) make clear that revenues received by the United States shall be credited to the obligations of the Association and the District proportionately until such obligations are paid in full by the Association and the District, then the revenues (should) be retained by the United States pursuant to existing law.

This conclusion makes perfect sense when one considers that one of Congress’ primary purposes in enacting credits to projects was to make the reclamation fund revolve faster. To credit mineral leasing revenues to operation and maintenance or other non-construction annual obligations after pay-out does not serve this purpose but merely serves to relieve project users of their statutory obligation to pay their yearly costs.  

Thus we conclude that while there may be some project-specific acts which allow otherwise, when there is no reimbursable construction obligation against which mineral leasing revenues may be applied, the proper disbursement is to the general account of the Reclamation fund. However, the statutes which direct the crediting of revenues to the accounts of the various projects are still in effect.

The plain language of the credit to the project statutes still requires that the subject revenues are to be “credited to the project . . . to which the construction cost has been charged.” See e.g., subsection J of the Fact Finder’s Act, supra. The opinions and legislative histories cited above show that those credits can only be applied against the back end of the project’s reimbursable construction obligation. Thus, when a project has no construction obligation against which it may properly apply the credits, the revenues must go into the general account of the Reclamation fund instead of being applied against other user obligations, but the statutory credit to the project remains.

When additional construction obligations are incurred which comply with the conditions set out in the credit to the project statutes, the credit may be used.


\footnote{Perhaps the best way to visualize this process is to think of an account in a bank. The actual dollars which are deposited in the account do not remain in any special place, but are put among the funds of the bank. What remains is a credit which may be drawn upon and when the draw is made, the money will be supplied from the general funds of the bank. This is very close to the operation of the Reclamation fund. The revenues which go to the credit of a particular project remain as a credit if there is no allowable obligation against which the credit can be applied. The revenues which form the basis of the credit go into the Reclamation fund where they are available for disbursement subject to reimbursement on other projects. The fact that the revenues which are paid out of the fund must be repaid means that funds will be available to use when the projects which have unused credits are in a position to call upon them, e.g. when those projects have reimbursable construction debts.}

When the betterment portion of R&B constitutes new construction, there is good reason to think that revenues credited to the project would be available to help repay those costs. If, however, the money for R&B was obtained under the provisions of the Rehabilitation and Betterment Act of 1949, 63 Stat. 724; 43 U.S.C. § 504, the work done would be statutorily precluded from being classed as construction.
The continued operation of these credit to the project statutes is further justified by the fact that their enforcement continues to fulfill the congressional intent of helping the Reclamation fund to revolve more quickly. There is also the continued reasoning that the water users should obtain the benefit of revenues which are generated by lands or facilities for which they have repaid the construction cost under the earlier reimbursable obligation even though title has remained in the United States. 30

CONCLUSION

The requirement of the Acquired Lands Act that mineral leasing revenues be distributed “to the same funds or accounts . . . and in the same manner as other receipts from the land affected by the lease . . .” is most fully met for revenues from acquired reclamation lands that have been charged to the reimbursable component of a project by the “credit to the project” disbursement formula. When revenues are generated from acquired lands which have not been charged to a project, a general credit to the Reclamation fund is appropriate. A credit to the annual obligations or the project is not appropriate for mineral leasing revenues from acquired lands because future use of the subsection I annual credit method was cut off by the Hayden-O’Mahoney Amendment in 1938 except where such treatment was grandfathered in under those amendments. We further conclude that the credits created by the statutory disbursement of mineral leasing revenues to projects may be used to satisfy new construction obligations in the same manner that such credits were applied against past obligations.

MARTIN L. ALLDAY
Solicitor

SHELL OFFSHORE, INC.

113 IBLA 226

Appeal from a decision of the Director, Minerals Management Service, affirming assessment of interest charges for late payment of royalties. MMS-87-0124-OCS.

Set aside and remanded.

1. Federal Oil and Gas Royalty Management Act of 1982: Assessments—Federal Oil and Gas Royalty Management Act of 1982:

30 This continued credit will serve to create a type of dilemma for water users in that the use of R&B loans does not require additional approval but cannot be repaid using credits to the project while construction, which can be repaid using such credits, generally requires congressional authorization.
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Royalties—Oil and Gas Leases: Royalties: Interest—Oil and Gas Leases: Royalties: Payments

An exception to late payment charges for royalty payments filed after the end of the month following the month in which the oil and gas is produced and sold may be recognized where the payor has filed a sufficient estimated payment in accordance with the instructions in the Payor Handbook. An estimated payment is made on Form MMS-2014 and requires identification of the payor, the lease number, and the product code and selling arrangement number. An estimated payment may only be established initially for the month immediately preceding the month in which the report and payment are filed and, thereafter, the estimated balance is rolled over monthly to cover production and sales in succeeding months.


As a general rule, an administrative decision is properly set aside and remanded where it is not supported by a case record providing the Board with the evidence necessary for an objective, independent review of the basis for the decision.


OPINION BY ADMINISTRATIVE JUDGE GRANT

INTERIOR BOARD OF LAND APPEALS

On October 9, 1986, the Royalty Management Program (RMP) Office of the Minerals Management Service (MMS) issued Bill of Collection No. 05600932 to Shell Offshore, Inc. (Shell), assessing late payment interest charges in the amount of $58,376.81. With its payment of the full amount, Shell filed a timely notice of appeal to the Director of MMS. The appeal challenged assessment Nos. 65 through 88, 92, 93, and 97, in the amount of $22,593.79.

Prior to a ruling on the appeal by the Director, the RMP Office agreed to review assessment Nos. 65 through 88 and 93, which totaled $4,316.89. The RMP Office determined that all of these assessments except for Nos. 72 and 73 were invalid and agreed to initiate a refund in the amount of $3,288.84. It appears that Shell was satisfied with the review of assessment Nos. 72 and 73, as its statement of reasons filed with the Director addressed only assessment Nos. 92 and 97, totaling $18,276.90.

In its appeal to the Director, Shell asserted that it had made "a one-time estimated royalty payment at the Payor level which exceeded actual royalties due." Specifically, Shell asserted that:

[Review of the Bill reveals assessments totalling $18,276.90 for late payments resulting from not having estimates at the AID [accounting identification number], Product Code/Selling Arrangement level, even though [Shell] made a sufficient estimated royalty payment at the Payor level to cover [Shell's] actual royalty obligations. Qualifier F of the Payor Handbook * * * states that, for Federal leases, *[iln any reporting month that the total of the estimated payments previously reported for a specific payor code equals or exceeds the actual royalty due on those same AIDs, products codes, and selling
arrangements no late payment will be assessed.” Payor Handbook p. 3.070-4 (12-84 revision) (italics added). [1]

(Statement of Reasons to the Director at 2).

A report on the appeal was submitted to the MMS Division of Appeals by the RMP Office. It stated that the royalty for the two offshore leases at issue was due at MMS by the last day of August 1985 because SHELL was reporting the July 1985 sales. According to MMS records, the estimate for lease 054-003936-0 was established for September 1985 sales, and the estimate for lease 054-004424-0 was established for August 1985 sales. Therefore, when the report and payment for July 1985 for these leases was received by MMS on September 27, 1985, the royalty was 27 days late because SHELL had not established estimates for the July 1985 sales month, and royalties were due by the last day of the following month, or August 31, 1985.

(RMP Field Report at 2). In regard to Shell’s argument, the report stated simply that “[a]lthough SHELL may have had estimates at the Payor level sufficient to cover actual royalty due, the bill was not issued for insufficiency of estimates.” Id.

By a decision dated May 19, 1987, the Director ruled on the appeal. The decision held that:

The royalties for these two leases were due August 31, 1985, because Shell was reporting July 1985 sales. The MMS received the July report and payment on September 27, 1985. However, MMS’s records show that an estimate for one lease was established for August 1985 sales and for the other lease for September 1985 sales, but an estimate was not on file for either lease for July 1985 sales. Since the royalties were paid late and there were no estimates filed on these leases for the appropriate sales month, the interest assessments are valid.

(Director’s Decision at 2).

Shell appealed the MMS decision of May 19, 1987, to this Board. The statement of reasons for appeal filed with the Board repeats the argument raised with MMS. Shell additionally argues that MMS’ grant of its appeal on Bill for Collection No. 04600585 involving the same issue as this appeal shows that MMS agrees with Shell’s position.

In its answer, MMS contends that “estimated payments must be sufficient at a lease level, not a payor level, and for the two leases at issue Shell did not have an estimated payment established” (Answer at 1). In support, MMS quotes Qualifier A of the Payor Handbook which stated: “The estimated payment must be made against a specific AID and MMS assigned product code and selling arrangement number. Estimated payments are only reported once.” (Payor Handbook) at 3.070-2, rev. 12/84 (italics in original). MMS states that “[a]n AID is equivalent to a lease number” (Answer at 3). MMS also presents a copy of Form-2014 which appeared in the Payor Handbook at page 3.070-3 to

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[1] Minerals Management Service, Royalty Management Program, Oil and Gas Payor Handbook [hereinafter cited as Payor Handbook]. The various explanatory paragraphs in the Payor Handbook under the heading “Reporting Estimated Royalty Payments” are labeled alphabetically from A through F and described as “Qualifiers.” The requirements for estimated royalty payments found in the current version of the Payor Handbook are substantially the same although the format of the codification has changed. See 2 Payor Handbook § 3.5 (1986).
illustrate the method of establishing an estimated royalty payment for a lease. MMS notes that the instructions for filling out the form on page 3.070-2 cited by Shell require the payor to enter the “MMS assigned accounting identification (AID) number in block 6.” Finally, MMS states that the appeal of Bill for Collection No. 04600585 referred to by Shell was granted because upon investigation it was determined that an estimated payment was on file for the leases in question (Answer at 5).

[1] As a general rule, royalty payments on production are due by the end of the month following the month in which the oil and gas is produced and sold. 30 CFR 218.50(a). Section 111(a) of the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), 30 U.S.C. § 1721(a) (1982), specifically provides that “where royalty payments are not received * * * 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 * * *. The assessment of interest charges on late royalty payments is also required by provisions of the implementing regulations. 30 CFR 218.54. Exceptions to a late payment charge are authorized “when estimated payments on minerals production have already been made timely and otherwise in accordance with instructions provided by MMS to the payor.” 30 CFR 218.150(b). The instructions for making estimated payments are found in the Payor Handbook.

Paragraph F of the Payor Handbook cited by appellant provides that: “In any reporting month that the total of the estimated payments previously reported for a specific payor code equals or exceeds the actual royalties due on those same AIDs, product codes, and selling arrangements no late payment charges will be assessed.” Payor Handbook at 3.070-4 (12/84). An understanding of the requirements for establishing an estimated payment requires reference to the other relevant paragraphs of this section of the Payor Handbook. Thus, paragraph A provides that “[t]he estimated payment must be made against a specific AID [*] and MMS assigned product code and selling arrangement number” (Payor Handbook at 3.070-2 (12/84) (italics in original)). The Payor Handbook further explains that once the estimated payment is made, the full amount of the estimated payment carries forward from one month to the next month and the amount of the estimated payment is not reduced by the actual royalties paid. The result is that the payor is allowed to delay payment of the actual amount of royalty due until the end of the second month following the month the production is sold so long as a sufficient estimate balance exists. Id.; see Yates Petroleum Corp., 104 IBLA 173 (1988).

Estimated payments are reported on Form MMS-2014 and must be established for the sales month immediately preceding the month the report and payment are filed with MMS (retroactive establishment of

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2 An AID or accounting identification number “is assigned by MMS and consists of a 10-digit lease number followed by a three-digit revenue source code. * * * The AID number is provided by MMS on a Payor Confirmation Report (FCR) after a payor submits appropriate data on a Payor Information Form (PIF).” 2 Payor Handbook § 2.3.3 (1986).
estimate balances to avoid interest charges is not allowed) (Payor Handbook at 3.070-2, Paragraph C, and 3.070-3 (12/84)). This Board has affirmed the necessity of careful compliance with the procedures for estimated payments in order to avoid interest charges for late payments. See Yates Petroleum Corp., supra (estimated balance on file will not bar interest charges for late payment where the royalty payment was made after the second month following the sale month because the estimate rolls over from one month to the next to cover sales in the latter month).

Accordingly, the issue presented is whether appellant properly filed an estimated royalty payment on Form MMS-2014 for each of the leases at issue for the July production/sales month. Such an estimated payment would have to have been filed by the end of August 1985. MMS has asserted that this was not done as an estimated payment for lease 054-003936-0 was established for September 1985 sales and the estimate for lease 054-004424-0 was established for August 1985 sales. Unfortunately, the administrative record before the Board contains neither copies of the Form MMS-2014 on which the estimates were submitted nor copies of the forms on which the payments for July 1985 production were submitted late. Thus, the record before the Board does not contain any documentation establishing the facts from which the issue of proper application of the provisions of the Payor Handbook arises. The record contains copies of the MMS bill for collection; Shell’s November 14, 1986, cover letter enclosing payment of the assessment and notice of appeal; Shell’s December 24, 1986, letter discussing the resolution of assessment Nos. 65 through 88 and 93; Shell’s statement of reasons to the Director and cover letter; the RMP Office field report and cover memorandum; MMS’ docketing letter of April 1, 1987, acknowledging receipt of the appeal to the Director; MMS’ decision of May 19, 1987; and MMS’ May 22, 1987, cover letter transmitting the decision to Shell. It does not contain documents related to the estimated payments MMS asserts were made for August and September 1985 sales. In particular, it does not contain any documentation of receipt of Shell’s royalty payments by MMS for which MMS is assessing late payment interest charges.

[2] As a general rule, an administrative decision is properly set aside and remanded if it is not supported by a case record providing this Board the information necessary for an objective, independent review of the basis for the decision. Fred D. Zerfoss, 81 IBLA 14 (1984). The reason for filing the complete agency record with the Board is evident: it is impossible for this Board to engage in intelligent, objective review of the agency’s decision without knowing the circumstances leading to the action and the agency’s reasons for taking the action. See Soderberg Rawhide Ranch Co., 63 IBLA 260 (1982). The Board is expressly authorized to review MMS decisions such as the one under appeal in order to issue the final administrative decision on behalf of the
Secretary. 43 CFR 4.1(b)(3), 4.21(c). Obtaining the complete administrative record is indispensable to the responsible exercise of this review authority.

As explained in Mobil Oil Exploration & Producing Southeast, Inc., 90 IBLA 173 (1986), the agency case file must be complete as it may be subject to direct judicial scrutiny. It is well established that, absent a complete record, this Board and a reviewing court are incapable of complying with the review requirements statutorily mandated by the Administrative Procedure Act. See, e.g., Higgins v. Kelley, 574 F.2d 789, 792 (3rd Cir. 1978). When the validity of the agency's action is not sustainable on the administrative record compiled by that agency, courts are obligated to vacate the agency decision and remand the matter for further consideration. See Camp v. Pitts, 411 U.S. 138, 143 (1973). Accordingly, we find it necessary to set aside and remand the decision appealed from in order to ensure that a record is established which will support the administrative decision.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision of the Director, MMS, dated May 19, 1987, is set aside and the case is remanded.

C. Randall Grant, Jr.
Administrative Judge

I CONCUR:

Charles B. Cates
Director, Ex Officio

APPEALS OF HARVEY C. JONES, INC.


Contract No. M0014204022, Bureau of Indian Affairs.

Granted in part.

Contracts: Construction and Operation: Drawings and Specifications—Contracts: Disputes and Remedies: Equitable Adjustments

Under a contract for the construction of an urban road project, the Board found that the liability of the Government for the majority of the items of claim (failure to secure the timely removal of utility lines from the work areas; erroneous staking; improper testing standards; design problems) was established by a preponderance of the evidence, as was the failure of the Government to properly administer the contract in a number of respects. After noting that the evidence offered by the appellant in support of its total cost claim failed in a number of instances to establish a nexus between the cause of delay assigned and the amount of damages claimed and failed to separate delays for which the Government was responsible from delays attributable to actions of the contractor, the Board concluded (i) that the use of the total cost method for determining the amount of the equitable adjustment in such circumstances was not warranted; and
February 28, 1990

(ii) that where the liability of the Government had been established but the amount of the equitable adjustment could not be determined with any degree of mathematical precision, it was proper to resort to the so-called jury verdict approach for the purpose of determining the amount of the equitable adjustment to which the appellant was entitled.

APPEARANCES: Bernard P. Metzgar, Attorney-at-Law, Lamb, Metzgar & Lines, P.A., Albuquerque, New Mexico, for Appellant; Barry K. Berksen, Margaret C. Miller, Government Counsel, Santa Fe, New Mexico, for the Government.

OPINION BY ADMINISTRATIVE JUDGE McGRAW

INTERIOR BOARD OF CONTRACT APPEALS

These appeals relate to contract work performed by appellant Harvey C. Jones, Inc. (hereinafter HCJ), for the Bureau of Indian Affairs (hereinafter BIA) in 1983 and 1984. The principal contract work was the construction of an urban road project and associated appurtenances in the “Mesita Streets” subdivision in the Laguna Agency reservation in Cibola County, New Mexico. Ultimately, the project was accepted as complete as of October 12, 1984 (Appeal File (hereinafter AF), Tab 33 (letter dated Dec. 13, 1984)). In a letter dated May 31, 1985, HCJ filed a claim with the successor contracting officer (hereinafter CO). The claim amount therein was in excess of $559,000 (AF, Tab 33). The CO never issued a final decision on this claim. HCJ filed an appeal that was docketed on August 14, 1985. After an order of dismissal without prejudice to allow the CO to issue a decision and other orders directed at curing certain procedural deficiencies and allowing discovery, we reinstated the appeals on December 3, 1987, still lacking a final decision, having treated the CO’s silence on the claim as a denial. One of the areas of procedural deficiency was in the matter of the adequacy of the complaint under our rules, and the form HCJ chose to cure that problem moved us to assign docket numbers to each of the complaint’s counts as a measure promoting convenience and expedition. The Board conducted a fact-finding hearing in the case in Albuquerque, New Mexico, during March and April 1988.

Background

BIA awarded the contract to HCJ on August 5, 1983 (AF, Tab 1). During subsequent contacts between the parties, they orally decided that the start date would be September 12, but BIA did not deliver a written notice to proceed until September 16, a Friday; HCJ moved onto the project site on September 19 (Tr. 41-42). The contract allowed 120 calendar days for the completion of the work. HCJ delivered to BIA a proposed work schedule on September 23, 1983, calling for completion in 75 calendar days. BIA did not timely register any misgivings over this schedule, and we find that given a reasonable manpower level, a lack of significant delaying factors of the reasonably
unforeseeable variety, and a reasonably satisfactory administrative and productive effort, this contract was capable of being performed in 75 calendar days. The project was accepted as substantially complete on May 25, 1984, and finally accepted, as mentioned, as of October 12, 1984 (Supplemental Appeal File (hereinafter SAF), Tab 45).

The work involved was the building of a road in the Mesita Streets subdivision. It was a relatively small project comprising a total of about 2 miles of completed road (Tr. 602). The parties referred to six parts of the project for convenience in placing various of the events central to the case. There was a section of road proceeding in a straight orientation from the State highway and this section is known as Spur Road. At a point on Spur Road, the name changed to Loop Road, which proceeds in a straight direction for some distance and then loops back in a more-or-less circular orientation onto Spur Road at the point where Loop Road began. There are then four “interior streets” connecting Loop Road at one point of its length with itself at another point; these streets are designated Streets (or Roads) A, B, C, and D, respectively (App. Exh. B; Drawings, AF, Tab 1).

The Mesita area is residential in character, and the project purported to improve existing earthen “roads” with a durable paved structure less susceptible to difficult passage during weather events. Being residential, the area would normally be a candidate for what is called an “urban” road design, but the contract called for the project to be built in what is called a “rural” design (Tr. 61, 70, 87-90). Although this design is unusual for such an area, the choice of that design is not evidence of faulty design in itself (Tr. 635, 1087-88). The principal distinction between the urban and rural styles is that the latter accomplishes drainage by means of roadside ditches while the principal drainage facility of the former is curb and gutter. The contract also called for HCJ to move fire hydrants and relocate water valves that otherwise would be in the area of ditch excavation. The responsibility for the removal of existing utility lines is a matter of significant dispute which will be discussed in depth later herein. The principal contract language covering this matter provides that utilities “will be removed and relocated by others” (Drawings, AF, Tab 1).

HCJ’s plan for accomplishing the work called for it to excavate the ditch line and use the excavated material to the extent possible to build the adjacent area of the road. Not only would this be a valid, efficient means of operating to the extent practicable in normal circumstances, but also a contract provision mandated that all project excavation be exhausted for grading the road before HCJ would be permitted to obtain material for grading from the borrow pit that was located essentially at the site (Tr. 91-93). If the amount of the excavated material were insufficient to grade the road area adjacent to the ditch line, logically this meant that ditch line material excavated

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1 This is not to say in terms of management skill available to the contractor or the personnel and equipment devoted to the performance of the contract work that HCJ could have completed the contract within 75-calendar days. For consideration and resolution of this question, see quantum section, infra.
later in the project had to be transported back to a road area adjacent to a ditch line where material had long before been excavated.

Because there were residences to be served by the project, it was necessary to construct "turnouts" over the ditch to the dwelling, and this required the installation of culvert pipe under the turnout to keep the drainage line unimpeded. The original plans called for 49 such turnouts, and amendments brought this number to 61 (Tr. 662).

Consistent with its theory of the case, HCJ presented a considerable body of evidence probative of the conclusion that BIA had caused substantial delays in HCJ's progress ultimately resulting in financial damage. The particular delay matters on which HCJ's case centered were in the areas of utilities removal, surveying and staking, testing (particularly testing of compaction of the various road courses), and faulty design. HCJ raised a number of other matters of less central concern. Some related to issues involving BIA's alleged deficient contract administration for which HCJ did not seek compensation but which were important to HCJ apparently as collateral corroboration for that portion of its case for which it does seek compensation. Others related to instances purportedly also indicative of inadequate contract administration for which HCJ does seek compensation but in a magnitude lesser than the four major areas mentioned above. An example of this latter category centered on BIA's refusal to permit work in some of the later days of performance in 1983 because of frozen ground; HCJ contends that there was no frozen ground on many of these days and that BIA's unreasoning intransigence on this matter caused it delay with identical effect to that caused under the main areas of alleged delay. There are many other factual areas of importance which for the sake of convenience and logic are better addressed in the sections on Entitlement and Quantum which follow than in this Background section.

One of the factors which emerged during the hearing was that in the administration of this contract, BIA spread its authority among a greater number of delegates than is the typical case. For instance, the administration of the Laguna Agency had a semi-official status in the hierarchy of persons involved in contract administration (Tr. 482-83). Also, BIA hired a crew of residents of that agency to conduct surveying and testing operations (Tr. 847-48). This crew was relatively inexperienced in the functions it was to perform, and a significant portion of HCJ's case centered on the alleged incompetence of this crew in the early days of contract performance. Ultimately, the crew was (essentially) replaced with a more experienced crew (Tr. 107). It is clear, however, that there were significant problems affecting the performance of the contract resulting from the use of the crew of residents from the Laguna Agency and the imposition of the Laguna Agency itself into the administrative chain of command. Despite these clear indications that there were such problems, the BIA witnesses
invariably denied that there were any problems for performance created by the presence of these factors (e.g., Tr. 848-49). The impression created was that BIA had compelling policy reasons for choosing this method to administer the contract. The actual implementation of such a policy created serious problems for the contractor. Weighing the evidence received, we find that a significant portion of such problems was due to the inexperience or the incompetence of the personnel used by BIA from the Laguna Agency in the early stages of contract performance.

There was testimony from one witness which we found to be somewhat more reliable than that of many others; that witness was Mr. Robert Garcia, the CO who administered the contract starting with award and continuing throughout the great bulk of the prosecution of the contract work. He was no longer employed by BIA at the time of the hearing and that circumstance was a significant factor in our conclusion on the relative reliability of his testimony. Appearing (under subpoena) as HCJ’s witness, Mr. Garcia testified that during his tenure as contracting officer he was aware that the utility problems were causing delay to HCJ (Tr. 372-73) and that HCJ had valid complaints regarding the staking (surveying) problems (Tr. 376-77). In arriving at the determinations reached in this case, the Board has relied heavily upon the testimony of Mr. Garcia in the areas as to which he testified.

**ENTITLEMENT**

IBCA-2150, 2151, 2152

The subject matter areas covered in IBCA-2150, 2151, and 2152 have been described by HCJ as “Unclassified Excavation and Borrow Excavation,” “Pipe,” and “Base Course,” respectively. The principal HCJ theory for recovery in these cases is that BIA delayed HCJ’s progress in these areas ultimately causing financial loss. The underpinning of the theory is that BIA’s performance of its responsibilities was deficient in the areas called “utilities,” “staking,” “testing,” and “design.” These alleged deficiencies relate to the subject matters in each of these three cases (except “design” in IBCA-2152, “Base Course”), so we will proceed by treating the alleged deficiencies, relating our findings to the issue descriptions in the three cases and adding comments on subissues unique to each of the cases as necessary.

**Utilities**

HCJ claims that it had adequate manpower and equipment to prosecute the contract work as bid in 75 days. It contends that it was significantly delayed in its progress when it encountered utility lines (water, sewer, power, gas, and telephone) which caused it to stop work and either wait for the line to be repaired or transfer its efforts to another part of the site. Not all of the problems connected to utility
lines were caused by HCJ's actually hitting the particular line. Often it was a matter of one utility's crew hitting its own line or another utility's line as it was searching for one of its own so it could move it (Tr. 148-51; App. Exhs. E, F, G). HCJ's project manager, Mr. Sandy Jones, recounted the events of one day by referring to the record thereof in the trip report prepared by BIA's supervisor of the survey crews Mr. Montoya. Mr. Sandy Jones testified regarding December 1, 1983:

And then he took our foreman—my foreman picked [Mr. Montoya] up to go look at a pipe that the Bureau had staked, and my foreman was going to show him where he was going to actually move that pipe around to miss a certain utility that we hadn't hit already. While he was digging that, he hit a telephone line that was dead, that had been previously repaired or moved or fixed. And after that happened, after we showed where we were going to move the pipe around to accept what was on the ground, Mr. Montoya says the phone company was on the project that day, because they were repairing a telephone line that the Gas Company hit yesterday, and the Gas Company had just broke a water line.

So that is real typical of the amount of people that were on the job. Everybody was digging. We were trying to work; they were hitting this guy's line; we were hitting their line; the Gas Company was hitting the telephone lines; we were busting water lines; * * *

(Tr. 151-52).

In normal circumstances, a contractor trying to construct a road can shift his efforts to another portion of the project when there is a utility line problem necessitating a cessation of activity in the immediate area of the problem. This causes inefficiency and some, presumably slight, amount of delay and if it happens infrequently the overall impact to the contractor is not great. Indeed, encountering a certain number of such problems is considered normal in the industry (Tr. 734-35). In fact, HCJ attempted to move to other work when these problems occurred, but they were so great in number that Mr. Sandy Jones described his operation as being "tied up" and requiring that HCJ "jump around hunting places to find a little bit of excavation material" (Tr. 92, 94). BIA has contended that the utility problems did not cause delay because HCJ always had other work to do outside of the vicinity of the problem; BIA also, however, to establish that HCJ's delay was of its own making complained about some of the unorthodox measures HCJ took that HCJ contends were of the "jumping around" variety, undertaken to accomplish some progress despite the utility problems. HCJ contends that normal circumstances did not prevail on this project principally for two reasons. One was the great number of incidents involving the breaking of utility lines either by HCJ or by others (App. Exhs. E, F, G), totalling 38, according to HCJ's count, from start-up in September 1983 until HCJ shut down the project in late December because of winter weather conditions. The other reason is that the contract demanded that all excavation material (principally from the ditch line) be used before borrow material could be used for
grading the road surface (Tr. 92-93). Thus, after HCJ moved the hydrants and other items that were its responsibility, it would scarify, process, grade, and compact the existing roadway, then cut the ditch lines, essentially contemporaneously with grading and compacting the excavation material from the ditch line on the adjacent roadway. If the excavation material were insufficient in quantity for the roadway course, then under the terms of the contract the cut operation in the ditch line had to proceed ahead of the grading operation, eventually leading, logically, to inefficiency as compared to importing borrow from the borrow pit for some roadway sections. Pipelaying would follow the completion of road grade and ditch line built as one operation; base course and hot mix steps could also follow later, each presumably in one single sweep through the project (Tr. 125). Thus, proceeding in a "jumping around" fashion was even more inefficient on this project than it would be on others, because the building of the roadway could not be done prior to the ditch cuts; aggravating this situation was the fact that most of the utility problems occurred in the ditch line (Tr. 133). Also aggravating the problem was a design controversy relating to the placement of the culvert pipe under the turnouts. We will treat that controversy more in depth under "Design" below; for purposes of this "Utilities" section, however, we note HCJ's contention and evidence that the design problem meant that the ditch line cut ultimately was at a greater depth than anticipated on the plans and that meant that more utility lines were in jeopardy of being cut at the greater depth than the utility companies could have anticipated by looking at the plans (Tr. 132-33).

HCJ's case, then, is that it was delayed by the various utility problems and that the Government was responsible for the delays because the Government was responsible under the contract for seeing that utility lines were removed, and it failed to discharge that responsibility.

BIA denies the charge and had a number of witnesses who offered their conclusions on whether HCJ had been delayed. It is difficult for us to accept this testimony on the effect of utility problems on HCJ's progress at face value.

For instance, although BIA had several witnesses who testified that HCJ was not delayed by the utility problems, it presented two principal witnesses on this issue (and on many others). One was the Contracting Officer's Representative (COR), Mr. David Holmes, who appeared to be well qualified for his position by temperament, training, and experience; the other was Mr. Kimo Natewa, who was the agency Road Engineer for the Southern Pueblos Agency which provided the crew that replaced the Laguna Agency crew, mentioned above. Mr. Holmes testified that certain utility problems did not delay HCJ (Tr. 632-33, 637, 756, 766). Some of this testimony was to the effect that HCJ was not delayed in building the "main street" by the utility problem. Even disregarding the borrow pit/"jumping around" inefficiency argument as it relates to Mr. Holmes' qualification of
delay to the building of the "main street," we note that the clear import of the entirety of his testimony is that HCJ simply was not significantly delayed on the whole project by the utility problems, nor for that matter by any of the other alleged problems, as we will note again later (Tr. 766-68). Similarly, Mr. Natewa testified that he was unaware of any delays to HCJ occasioned by utility problems (Tr. 1065). Both Mr. Natewa and Mr. Holmes also testified that there was no delay caused to HCJ because of testing by any BIA personnel (Natewa, Tr. 1071; Holmes, Tr. 691-92, 698). Another BIA witness Mr. Charles Hatch also testified on these matters. He is a construction maintenance engineer for the Federal Highway Administration (FHA). The FHA has certain oversight responsibilities for BIA road construction, and as part of performing that function, it performs a final inspection on BIA projects (Tr. 1102-03). In pursuance of that responsibility, Mr. Hatch visited the project site on two occasions. On the first of those occasions, February 19, 1984, he made a trip report about which he testified. One part of the report reads (regarding the BIA crew that was assisting in inspection chores, i.e., testing, surveying, etc.): "This crew was inexperienced and did cause some problems for the contractor as far as testing was concerned" (Tr. 1105; read from the trip report by BIA counsel). When the witness was then questioned about whether he knew that from his own experience, he responded: "No, sir, that was told to me by the project people that I talked to," project people whom he had earlier identified as Mr. Holmes and Mr. Natewa (Tr. 1105, 1103). Although this evidence was about testing, we note that Mr. Natewa and Mr. Holmes' testimony on utilities was very similar in its conclusion and in its certitude to what it was on testing. Essentially, they testified that HCJ was absolutely not delayed by utilities or by testing and that there were not any significant problems on either, yet they told Mr. Hatch that testing caused problems for the contractor. We recognize that this is hearsay evidence, but much of BIA's case is based on hearsay (as is HCJ's for that matter), and this was BIA's witness; counsel had ample opportunity to clarify what was meant using this or another witness; counsel did not do so.

We also recall the CO's testimony, mentioned earlier, in which he acknowledged that there were utility problems causing delays to HCJ.

Based on the foregoing analysis, we find the testimony offered by HCJ to be more reliable and therefore find that problems relating to the removal of utility facilities delayed construction to some extent.

BIA has a second, legal tack on the issue of entitlement, insofar as it relates to the utility area. BIA contends that regardless of any delay that may have been occasioned, it was HCJ that assumed the risk of such delays under the contract's provisions and it is thus not entitled to recover from BIA the amount of any financial hardship it suffered as a result. BIA has characterized HCJ's position on this issue as
contending that BIA promised a “utility free” project site. HCJ on the other hand has characterized BIA’s position as proceeding from the notion that it had no responsibility for the removal of utility lines other than to notify the utility companies that the lines should be moved. Neither characterization of the other’s position is totally correct but the evidence and testimony indicates that HCJ’s characterization of BIA’s position is closer to the fact than is BIA’s characterization of HCJ’s.

BIA first points out that notes on contract drawings provide that: “All existing power poles, telephone repair boxes and gas meters within the right-of-way limits will be removed and relocated by others” (Contract, AF, Tab 1, Drawings 7, 8, 9, 10; BIA Br. at 4). At other places on those and other drawings, there were clear indications that HCJ was responsible for elevating manholes and relocating water valves, fire hydrants, and the like from or near the right-of-way. BIA next points out that neither the drawing notes nor any other contract provision specifically mentions water and sewer lines (BIA Br. at 4) (or telephone, gas, or power lines for that matter). It contends, however, that by incorporating the Standard Specifications for Construction of Roads and Bridges on Federal Highway Projects (hereinafter FP-79) the contract adopted FP-79’s provisions relating to this issue (Contract, AF, Tab 1, Special Notice). Section 107.17 of the FP-79 reads, in pertinent part:

107.17 Contractor’s Responsibility for Utilities. The Government will notify all utility companies, all pipe line owners or other parties affected, and endeavor to have all necessary adjustments of the public or private utility fixtures, pipe lines, and other appurtenances within or adjacent to the limits of construction, made as soon as practicable.

Water lines, gas lines, wire lines, service connections, water and gas meter boxes, water and gas valve boxes, light standards, cableways, signals, and all other utility appurtenances within the limits of the proposed construction which are to be relocated or adjusted are to be moved by others, unless otherwise provided in the contract.

It is understood and agreed that the Contractor has considered in his bid all of the permanent and temporary utility appurtenances in their present or relocated positions as shown on the plans and that no additional compensation will be allowed for any delays, inconvenience, or damage sustained by him due to any interference from the said utility appurtenances or the operation of moving them.

Any damage to underground utilities not shown on the plans, due to unforeseeable causes beyond the control and without the fault or negligence of the Contractor, shall be repaired by the Contractor, and payment will be made in accordance with subsections 109.07 and 109.08. Time extensions may be authorized.

BIA contends that this provision clearly places on HCJ the risk of what did happen here (BIA Br. at 6-7). Our view of the provision is that, except for those particular utility facilities specifically mentioned in the contract or its drawings as being the responsibility of either HCJ or BIA to move or remove, the utility companies (others) were to move all such facilities. That comes from the second quoted paragraph. The first quoted paragraph shows that BIA’s responsibility was literally to “notify all utility companies” and to “endeavor to have all
necessary adjustments [in the various facilities] made as soon as practicable.” HCJ, under the third quoted paragraph, warranted that its bid contemplated all of the “permanent and temporary utility appurtenances in their present or relocated positions as shown on the plans” and that it may make no claim for any hardship suffered by interference from such “appurtenances.” Finally, in the case of utilities damage from unforeseeable causes, the CO may authorize time extensions and must pay for repair work done by HCJ in such cases by alternate means including equitable adjustment (Section 109.07 of FP-79).

Many of the utility problems encountered involved lines that were not shown on the plans (Tr. 115-20), so the contractor’s waiver under the third paragraph of entitlement to additional compensation for those incidents does not apply. Indeed, it is possible to read the section as allowing BIA to comply literally (if not in spirit) with the first paragraph’s requirements while still allowing compensation for “delays, inconvenience, or damage” to HCJ as long as the circumstances invoking its warranty under the third paragraph do not apply. (Moreover, there certainly were some fourth paragraph incidents because there were change orders issued to take care of “unforeseen work,” among other items in the orders, and these applied to water and sewer lines (AF, Tab 34). These paid for the repair work but not for any consequential loss, i.e., for delay.)

In any event, we do not read out the spirit of the provision as BIA apparently does. BIA produced much testimony to the effect that it had discharged its responsibilities under the provision by merely notifying the utility companies of the need to remove their facilities (e.g., Tr. 569). We note that the term “endeavor” appears in the provision also, and we read “reasonable” and “good faith” into that portion of that paragraph.

Our view is that BIA did not make a good faith effort in its endeavor to have the facilities moved. Several witnesses said they were not sure if all of the utility companies had followed up on the BIA notification. The CO testified that the major effort at removing utilities occurred during the winter shutdown starting in late December 1983 (Tr. 372-73). Also, in the preconstruction conference on September 2, 1983, BIA represented that all utilities had been moved with a small number of minor exceptions that would be handled expeditiously (Tr. 38, 568); since the award was made on August 5, 1983, it seems reasonable that the delay in issuing the notice to proceed until September 12, 1983, was largely a matter of the BIA’s endeavoring to have the utilities removed, and this conclusion is corroborated by a telephone message on August 13, 1983, to HCJ from the CO’s office advising that at least part of the delay was for just that reason (Tr. 368-69; SAF, Tab 49). Regardless of what the FP-79 provision details in terms of utility removal responsibility, both parties clearly contemplated that the
utilities would be removed before start-up, and the record supports the notion that HCJ was induced to accept the September start-up date by that contemplation (Tr. 42).

Another part of our "reasonable," "good faith" qualification on the BIA utility obligations is found in some tangential testimony submitted on the provision's meaning. Several witnesses testified that there is no such thing as a "utility free" project, because records adequate to locate each and every utility line do not exist, and that every project in the witnesses' experience entailed the contractor's encountering at least a few utility problems (e.g., Tr. 634-35, 568). We accept that testimony and use it to measure the reasonableness of BIA's effort, i.e., if there were but a few utility problems, that would be an indicator of BIA's discharging its responsibility under the contract. Here, however, there were 38 utility problems before the winter shutdown, a number that BIA has not challenged, and a few more after the spring 1984 restart. Since there were so few after the shutdown and since the CO testified that the major removal effort occurred during the shutdown, we conclude that the reasonable, good faith effort required did not occur before HCJ began the project but actually occurred much later.

Considering all of these circumstances, we cannot agree with BIA that the delays suffered by HCJ were not the responsibility of BIA, at least in major part, and we therefore conclude that HCJ is entitled to recover for the value of such delays to the extent that they are shown to have been caused by utility problems.

**Staking (Survey)**

On the question of staking, the parties are again far apart on the actions taken or omitted and on the effect thereof. HCJ's principal case was presented through the testimony of Mr. Sandy Jones who reported that BIA announced at the preconstruction conference that all staking was already in place but that his site inspection on September 19 revealed that there were some stakes in the ground but that they had no stationing data and that there were no offset stakes (Tr. 38-39, 52). Another HCJ expert witness testified that offset stakes are required by standard surveying procedures (Tr. 339-40). On this point several BIA witnesses testified about the lack of specific offset stake requirement on slope stakes in the contract or the FP-79 but none refuted the notion that standard surveying procedures require them (Tr. 899, 936). Mr. Sandy Jones also testified about a 1-foot "bust" in the stakes on Street A and about clear errors that had the road slope going into residents' yards and through buildings (Tr. 108, 47-48). The result of these alignment errors in two cases was that HCJ "eyeballed" the grade work in those locations, meaning that the staking was insufficient for the contractor to know how and where to build the road and that HCJ thus relied on the physical senses and seat-of-the-pants judgment of its equipment operator to do the job (Tr. 112-13, 351-53). HCJ's surveying expert testified that occasional "eyeballing" is an accepted practice but that the need for it is an indication of poor
design or of poor execution in staking of an acceptable design (Tr. 336). Mr. Sandy Jones also testified that Mr. Natewa agreed on one occasion to raise the grade of Street C because the grade as staked was incompatible with entrances to residences and with the location of utilities (Tr. 112-13). After a BIA attempt to explain how the 1-foot "bust" was not an error at all, HCJ’s surveying expert on rebuttal offered a cogent technical explanation on how there must have been a "bust" where Mr. Sandy Jones identified one (Tr. 1213-16).

On staking for pipe installation, Mr. Sandy Jones testified that the survey crew originally staked the ditch for what the plans apparently called for, a ditch cut with a bottom 18 inches below final road grade. After HCJ built the ditch as originally staked, BIA restaked the ditch for a deeper cut (Tr. 127-29). We will explore this area in greater detail under “Design” below. BIA did set “offset” stakes for the ditch cuts, but they set them a certain distance from the center of the roadway resulting in their being set “within” the ditch slopestakes, effectively eliminating the benefit that offset stakes are intended to provide (Tr. 918-19).

There are many other record entries of evidence probative of the point that HCJ was delayed by survey inadequacies and inefficiencies, and the foregoing are only examples. Clearly, HCJ has produced a prima facie case on this issue. It also used the testimony of BIA witnesses to prove its case.

Much of the Government’s case consisted of its witnesses’ opinions that HCJ was not delayed by any staking problems (Tr. 706, 849, 903, 1068). BIA also produced a great deal of testimony other than opinion on the subject. The COR, Mr. Holmes, directly contradicted Mr. Sandy Jones on some staking matters (Tr. 737). The project engineer supervising the Laguna Agency crew, Mr. Carr, testified that there were no serious problems with staking; also, he said the “eyeballing” of 400 feet of Street D roadway was a procedure accomplished very easily and quickly (Tr. 851-53). The Laguna Agency surveyor, Mr. Riley, testified, contrary to the HCJ assertion, that the project was completely staked by September 20, 1983, and that BIA did set reference (or offset) stakes. BIA contends that his testimony was that staking did not interfere with adjacent residences and that, although there were staking mistakes numbering around 3 in 1,000 linear feet, they were corrected very quickly before they could affect HCJ’s work (BIA Br. at 26).

The Southern Pueblos Agency surveyor, Mr. Salas, disagreed with Mr. Riley contending there were even fewer mistakes in the Laguna staking work than Mr. Riley thought (Tr. 924). In fact, his spot checks of Mr. Riley’s work found no errors at all (Tr. 927), and the alignment problem (road staked through residential property) was a minor issue (Tr. 927-28).
One of the curious things about BIA's case is that it used one witness, Mr. Salas, to refute the testimony of another, Mr. Riley. It is possible to view the two testimonies as being consistent with the general point that there were relatively few staking errors, especially considering that some would be expected on any job, but we hold a different view. Mr. Salas' testimony is more than a mere qualification of Mr. Riley's. Mr. Riley testified about his own work and admitted that there were some errors, and then Mr. Salas testified about the same work, Mr. Riley's, and said there were practically none. Effectively, BIA impeached its own witness, an activity it engaged in elsewhere. Both testimonies are consistent with the "few errors" conclusion, but in this case, we are impressed that there is a significant difference between "some" and "none." Also, testimony was contradictory in that Mr. Riley testified at one point that there were offset stakes (Tr. 898) and that there were not at another (Tr. 908). Mr. Riley also admitted on cross-examination that there were "quite a few" errors (Tr. 910), and he is one of the sources of the fact that offset stakes for the ditch line were set inside slope stakes (Tr. 918-19). Also on cross-examination, Mr. Salas significantly qualified and detracted from the impact of his direct testimony (Tr. 949-51). Where Mr. Riley testified that staking "did not interfere with people's houses" (BIA Br. at 26) and that he thought that stakes found on residents' property were offset stakes (Tr. 900), Mr. Salas testified that there were slope stakes there (Tr. 928). We are also not entirely unmindful of the admonition by HCJ that somewhat less weight might be accorded to the testimony of Mr. Riley and of Mr. Carr than to that of some other witnesses on the same matters because as part of the Laguna Agency crew that was effectively replaced in October 1983 these witnesses might have a motivation to view things somewhat differently from others. Along that line, we have trouble reconciling Mr. Riley's general position that there were relatively few staking errors with his admission that there were about three staking errors in every 1,000 linear feet of roadway (BIA Br. at 26). Insofar as there are only 10 stakes normally set in 1,000 linear feet of straight roadway, we note that this admission amounts to a 30-percent error rate, something effectively and repeatedly pointed out by appellant's counsel.

Finally, we recall two other matters. First, the Laguna Agency crew which was responsible for staking and other matters was replaced by the BIA with the more experienced Southern Pueblos crew. The COR, Mr. Holmes, attempted at the hearing to qualify and clarify his earlier deposition testimony on the qualifications of the Laguna crew and we believe that attempt was undertaken in good faith, but the overall import of his testimony was that he believed that the Laguna crew was inexperienced and in need of training (Tr. 248-50). Second, we note again the CO's testimony that there were staking problems and that they had caused HCJ delays.

Based on the foregoing, we must conclude that there were survey problems on the project traceable to BIA's performance of its contract
responsibilities and that some of the delays experienced by HCJ were attributable to such cause.

Design

HCJ’s claim on design centers on three different subissues. The first is that the overall design for the project, being of the rural type was inappropriate for application to this urban-type subdivision. The evidence supports the idea that the design as applied to the circumstances was somewhat unusual but not that it was inappropriate to the extent of constituting a design error. Moreover, the elements of this alleged design deficiency were well known to HCJ as it bid the job; such knowledge is inescapable from the plans and a site visit. In any event, HCJ failed to prove any delays from the overall design itself, so we reject this HCJ position on entitlement for delay.

The second design subissue concerns the placing of culvert pipe in the ditches under turnouts to residences and other community facilities. The plans clearly contemplate a ditch line 18 inches below final road grade. The contract also clearly calls for 24-inch diameter pipe to be placed therein, and the manufacturer specifies that at least 12 inches of cover be placed over the pipe (AF, Tab 1). This obviously means that the cover over the pipe in the turnout will be at least 18 inches above the final grade of the adjacent roadway, which could translate into an unacceptably high hump on which a vehicle could get hung up. When HCJ brought the problem to the attention of BIA, the latter’s response, effectively, was that HCJ would simply have to make cuts deeper (and therefore steeper) in many of the turnout locations. Because HCJ had already made the original cuts and had made at least substantial progress in building the roadway, it could not go back to the ditch line and excavate the ditch deeper by normal means using its equipment. Most of the corrective work thus consisted of hand labor. Because BIA reminded HCJ that proper drainage from the culverts was still required, HCJ had to make deeper cuts in the ditch line away from the pipes as placed, the pipes ultimately being placed 18 to 30 inches below the level of the original cut. Hand labor accomplished the bulk of these corrections as well (Tr. 124-40).

BIA’s brief sets out arguments against HCJ’s case in four places, three testimonial and one legal. It notes that Mr. Holmes said there was nothing misleading in the plans respecting 24-inch pipe in an 18-inch ditch (BIA Br. at 23; Tr. 661-63). It emphasizes that Mr. Natewa, in answering a question as to whether the situation was an aberration from the normal, stated: “No, this was not an unusual situation. I’ve seen it a lot of places” (BIA Br. at 36; Tr. 1068). It also notes that Mr. Hatch of the FHA said:

In areas where they have limited right-of-way, that’s basically all they can do [cut deeper so the pipe will fit]. And they try to get a flatter foreslope, for safety purposes. And in
that case, when you get the flatter foreslope, you're going to have a little narrower ditch, and then warp those ditches to fit the slopes either side or depth.

(BIA Br. at 36; Tr. 1108).

Mr. Holmes' testimony provided the background for Mr. Hatch's testimony on limited right-of-way. Mr. Holmes testified using Government Exhibit 10, which is a full-size set of the plans altered by Mr. Holmes for illustrative purposes, and Government Exhibit 11, a graphic representation in aid of his testimony, also drawn by Mr. Holmes for illustrative purposes. Using Exhibit 11, Mr. Holmes testified that in a typical State highway project, where there might be 75 feet or more of room on either side of centerline, there is enough room laterally to place a 24-inch pipe 18 inches below road grade in a spot far enough from the edge of the shoulder on one side and the right-of-way limit on the other so that the 18-inch "projection" (the hump) above road grade does not create the vehicular passage problem HCJ noted (Tr. 648-49). Then using Exhibit 10, Drawing 2, Mr. Holmes noted regarding the "Typical Section" depicted thereon that there was insufficient lateral space on this project for that kind of construction which he described as "flaring out" the ditches (Tr. 642). He based his conclusion that the lateral space was inadequate on the fact that there was only 25 feet of such space from road centerline to right-of-way limit (Tr. 642). Other testimony backs up Mr. Holmes' statement that the entire right-of-way is only 50 feet wide (Tr. 917). Our problem with the testimony is that to our eyes, Drawing 2, the "Typical Section" shows 31 feet of lateral space. We do not know how much of the assumed 75 feet of lateral space is available for ditch on a State highway project, but we assume that it is considerably more than that available here, and 31 feet is certainly not 75 feet, but for these purposes, we believe, 31 feet is considerably more than 25 feet. Applying what Mr. Holmes' testimony taught us, we see that if there is only 10 feet of space between road shoulder and right-of-way limit and a 24-inch pipe is placed in an 18-inch ditch with a 4:1 foreslope in that space, then the pipe center is 6 feet laterally from the shoulder. If the top of the pipe cover is 18 inches above shoulder grade (6 inches of pipe and 12 inches of cover), then the upslope to the top from the shoulder is also 4:1; and the downslope from pipe center to right-of-way limit is 18 inches down (assuming the natural ground there is as high as the elevation of the road shoulder) over the 4 feet of lateral space that would remain in a 25-foot width. This is a considerable hump just as contended by HCJ. If, however, the width is 31 feet, the downslope would accomplish its 18-inch descent over 10 feet, and to our minds, the hump created in those circumstances would not be nearly as considerable. Our view on this is confirmed by the HCJ expert who testified on rebuttal about four Government photographic exhibits entered for the purpose of showing that HCJ actually did not do as much excavating as it claims to have done (Gov. Exhs. 12, 13, 14, 15). We take the witness' testimony in general to be that the ditches and turnouts depicted in the exhibits are not typical of the job but, in
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particular about Exhibit 15, he testified that essentially the pipe was installed only slightly below grade as shown on Drawing 2's "Typical Section" and yet the hump is not great enough to cause traffic problems. He noted that the pipe cover is only about 6 inches but opined that an additional 6 inches of cover would still not create a problem (Tr. 1202-08). The point of the evidence was to show, by using an aberrational pipe placement example, why it was not necessary to cut the ditch 18 inches or more deeper than shown in the drawings. We believe that this evidence confirms, however tangentially, our view as explained of how a pipe could be properly placed at a specified elevation without creating a passage problem. Our view, of course, depends on a 31-foot lateral width as the drawings apparently portray, not the 25-foot width HCJ found in the field.

One way of analyzing Mr. Holmes' testimony is that he used one exhibit to show what the contract demanded on ditch line and culvert construction and another to show how the project could not be built that way. That analysis is not as cynical as it may sound, because Mr. Holmes also testified that a competent contractor would look at the plans and see just what Mr. Holmes testified to, but we note that all of Mr. Holmes' evidence assumes a 25-foot width. Although Mr. Holmes also highlighted right-of-way markers and lines on other drawings in Exhibit 10, apparently in support of his statement that "we had a very narrow right of way" (Tr. 649), we do not see where markers or lines or anything else on those drawings alert a viewer to a narrower right-of-way than that apparently depicted on the "Typical Section." In fact, our thorough search of the contract has revealed nothing other than that the cross-section plans show an 18-inch ditch in a 62-foot-wide project area, while the testimony indicates a right-of-way no wider than 50 feet in a major part of the project.

BIA's legal argument is connected to the various testimonies cited. BIA contends that even if there were a design (or other specifications) deficiency, it was a patent flaw for which HCJ may not recover its damages if it has not sought clarification from BIA in a timely fashion (BIA Br. at 38, citing Speer Construction Co., IBCA-2164 (May 24, 1988), 88-2 BCA ¶ 20,823). The patency, according to BIA, is that the contract clearly and frequently calls for 24-inch pipe in an 18-inch ditch. We question how patent the assumed flaw was, given that the survey crew twice staked those portions of the ditch where a deeper cut was needed, first at 18 inches and then, second, considerably deeper after HCJ made the first cut (Tr. 127-29). It is not clear if that means that the survey crew was also confused by the design or whether it points up the correct configuration of the question. If the flaw were patent, the plans would have to show a 24-inch pipe in an 18-inch ditch with insufficient width of ditch to allow a proper placing of that component in that excavation. Our search of the record does not reveal that the lack of width was patent. BIA seeks to overcome HCJ's case essentially
by stating that deeper cuts in this context are normal when width of right-of-way is limited and that any competent practitioner in the field knows it, but it did not show that HCJ should have known about the limitation.

Even if there were no problem with accepting BIA’s version of the background to its position on the existence of a patent design flaw and the need for an inquiry on clarification, it would not necessarily follow that no compensable damage arose out of this situation. If the design flaw was patent, the authorities charge the contractor with the responsibility for building the project as amended from the plans without charge to the Government. We do not believe, however, that BIA can escape all liability for a faulty design by invoking those authorities. Here, HCJ did, finally, point out what it thought was a flaw, and BIA’s response was to point out that the ditch should simply be cut deeper. This would assign HCJ the risk of greater cost resulting from its failure to inquire about the patent flaw before it bid. Here, however, in performing the work as thus modified, HCJ encountered more utility problems than it would have if it built the project as shown on the plans. We do not believe that the failure to inquire would assign the risk of the costs of delay and corrective efforts occasioned when it encountered utility lines as a result of performing the work necessary to the cure of the design defect, especially where the removal of those utility lines was, effectively as discussed, the responsibility of the Government. The fact that there were utility lines struck during the deeper excavation is another factor in questioning whether the asserted flaw was so patent as BIA contends: if it were clear to HCJ what must be done in the circumstances, then it was also clear to BIA, and BIA would have endeavored to have the deeper lines moved. That BIA did not have those lines moved is an indication that it was not as clear to BIA as BIA contends it should have been to HCJ. This position becomes more compelling, of course, if there were no design flaw at all as BIA posits rather than a patent flaw requiring HCJ inquiry. If there were no flaw, then it was clear that a deeper cut than shown on the plans was necessary in many places and that means that utilities should have been removed from those areas.

Because of the additional corrective work including the unknown encountering of utility problems, we conclude that HCJ has carried its burden of proving delays for excavation and pipe-laying under the heading of “Design.”

The third “Design” argument involves plans changes on the number and locations of turnouts, HCJ contending that there were so many major changes that it was considerably delayed in accomplishing final conduit placement and turnout building. The problem was so great, according to HCJ, that effectively the inspector was in charge of HCJ’s work through day-to-day direction of where to build turnouts, where normal good construction practices would call for a general plan delivered to the contractor and the latter’s day-to-day responsibility for such direction (Tr. 333-35).
The BIA defense essentially consists of the contentions that (1) the original plans called for 49 turnouts while HCJ actually built 61; (2) that such a number of changes from plans to as-built is not unusual; (3) that it paid HCJ for all of the extra work; and (4) a certain number of minor changes in location (plus the addition of a relatively few turnouts) is expectable in any project of this type (Tr. 1110).

HCJ's surveying expert, Mr. Phillips, on rebuttal re-explained an exhibit admitted during his testimony delivered during HCJ's case-in-chief and which BIA used to support its case on the expectability of minor changes. He explained that the over 40 changes highlighted on the exhibit were only those of the "major" relocation variety and that if he had also shown the minor-type changes about which BIA spoke, the exhibit would have had many more entries (Tr. 1210-11). BIA did not refute this testimony, and we conclude that HCJ thus preponderated on the "Design" issue of delays resulting from pipe changes.

Testing

There was a major controversy throughout the project regarding compaction testing for the various course constituents of the final road. HCJ contends that there was an excessive amount of testing and that it was done incompetently. The inspector found compaction failures in what HCJ contends is an inordinate number of cases, and the failures caused it delays because of the extra rolling and other compactive effort HCJ took as a result and of the efforts it undertook to find the real cause of the problem, at least according to HCJ. (Mr. Holmes testified that of 135 tests appearing in BIA records during 1983, 111 passed and implied that that was in the normal range of expectability for projects of this type (Tr. 199). Other testimony indicated that the contract required a minimum of 84 tests and that 135 actual tests under such a minimum is not out of line (Tr. 958-59). On cross-examination, however, Mr. Holmes could not with certainty reconcile Mr. Sandy Jones' testimony that there had been a substantial number of failing, unrecorded tests on October 3-5, 1983, insofar as the records from which he testified started on October 6, but Mr. Holmes did have a theoretical explanation (Tr. 808-17).)

There was a great deal of detailed testimony on this subject. BIA used "preliminary" proctors taken in August 1983 by the Laguna Agency crew against which to measure compaction tests taken during performance of the work. BIA designated Albuquerque Testing Labs (ATL) as its monitoring consultant on testing (Tr. 39). One of HCJ's experts testified that the BIA records did not sufficiently identify the samples from which the proctor numbers were derived so that later testing could be related to the same excavation or other grading material (Tr. 307-08). He further testified that color of the soil was the
most important property for purposes of identifying a sample so that the correct proctor could be used for later testing (Tr. 313). Another HCJ expert testified about the importance of visual identifying factors, including color, relative presence of gravel, and clay/silt ratio of composition (Tr. 280). BIA disputes the importance of the color aspect heatedly. One witness testified that color was not a practicable factor in identifying material and that there was no difference in color among the various soils at the site (Tr. 857-58). Another BIA witness, however, described the soil from around the project site in terms that would imply uniformity throughout and included a color factor in his description ("a little red clay in it") (Tr. 955-56). (The uniformity implication is interesting because BIA used at least 10 different proctors for, presumably, various soils (App. Exh. C). The same witness further refuted the earlier BIA witness by confirming that usually coloration is important but that on this particular project color was not particularly important because "basically most of the material is the same" (Tr. 970-71), and there were not different materials coming from different sources (Tr. 960).) The BIA witnesses were not experts while the HCJ witnesses were.

In any event, the concentration on the coloration dispute does little to resolve the basic issue. The real problem appears to lie not in coloration or in compaction testing method but in the fact that the proctors BIA used were incorrect. The proctors used were those same preliminary proctors that the Laguna Agency took in August 1983, the same crew that we know the COR thought was inexperienced and in need of training (see Tr. 812). Mr. Holmes also admitted that the early testing in October 1983 was beset by some kind of error though he did not know whether it resulted from incorrect proctors or from incorrect testing procedure, because his crew had reported to him on its own erroneous test results and later that the error had been corrected (Tr. 811-12). Coloration is ultimately unimportant on the issue of correct proctors, because HCJ’s expert conducted a proctor test at a road location, already built, where the BIA proctor was known. His proctor was significantly lower than the proctor BIA was using, so he rechecked the material using a different method ("one-point check") and got a result identical with his earlier proctor (Tr. 287-89). The witness’s company did other proctor evaluations at other times with similar results (Tr. 304-05; App. Exhs. C, K). Moreover, BIA’s testing consultant, ATL, also made proctor evaluations that differed with BIA’s and which were generally in line with HCJ’s. BIA, nevertheless, continued to use its preliminary proctors (Tr. 1020-27). Interestingly, BIA’s witness Mr. Avila did not testify that ATL’s and HCJ’s expert’s methods had anything to do with his failure to resample for proctors after he became aware of the other testers’ differing proctors; he did testify that those differences caused him to recheck in one instance and that that resulted in a lower proctor by “a major difference,” but he continued using the higher proctor (Tr. 1023-24).
BIA has attempted to counter the HCJ case on proctors by emphasizing that the HCJ experts did their analysis using method A of the American Association of State Highway Transportation Officials testing procedures while the contract required the use of method C of those procedures (BIA Br. at 22). BIA’s testing consultant, ATL, also used method A (Tr. 758). The difference in methods essentially parallels the difference in size of the sieves through which the proctor material is filtered at the first step of the analysis. Method C uses a larger size sieve, meaning that larger size particles (of gravel, for instance) would end up in the proctor sample material than if the smaller method A sieve is used. If a significant portion of the sample is of the larger size particles, then they would be included in the method C sample (having passed through that sieve) but would be excluded from the method A sample, meaning that because the particles are denser than finer material, a higher proctor weight would be expected from using method C than from using method A (Tr. 694-95). We have testimony from BIA’s Mr. Avila, however, that the material gathered for proctors was sandy and silty material that would have passed through either sieve and that in these circumstances method A would yield essentially identical results to method C (Tr. 961-62). This testimony was elicited on direct examination by Government counsel and was part of BIA’s case-in-chief. Mr. Holmes provided theoretical support for that proposition (Tr. 758-60).

In these circumstances we find that the testing problem was a matter of BIA’s using incorrect proctors. We believe that HCJ effectively rebutted BIA’s defense on the use of the “incorrect” proctor sampling method, because the preponderance of the evidence shows that either method would yield the same results. This is supported by the implication that BIA’s testing consultant by using the same, assertedly incorrect, method as HCJ’s expert added probative weight to the conclusion, because two expert groups apparently recognized that the method would mean no difference to the results in these circumstances. We see further support from Mr. Avila’s testimony, already mentioned, that in November 1983 he did a particular proctor analysis and got a result that was so much lower than the preliminary proctor (which BIA had used and then continued to use) that it constituted a “major difference”; Mr. Avila was part of the Southern Pueblos Agency crew, and the preliminary proctors were developed by the Laguna Agency crew.

On the issue of delay, we conclude that there were more tests taken than the 135 (with 111 passing) about which Mr. Holmes testified on direct examination, and HCJ produced substantial evidence to support that conclusion. Additionally, HCJ adduced theoretical support for its delay case on extra compactive effort in cross-examination of Mr. Holmes. He conceded that if early improper test results caused the contractor to perform extra rolls and other compactive effort to get a
passing test at a particular location, the normal range test-passing ratio disclosed by the evidence could well be a matter of HCJ’s having learned what effort would result in a pass and exerting that effort after the early failures where that extra effort would have been unnecessary if the proper lighter proctors had been used (Tr. 817-18).

For the reasons hereinabove stated, we find that HCJ was also delayed by testing inadequacies.

There was one minor area of disagreement that can properly be discussed under “Testing.” This relates to BIA’s initial onsite requirement that the foundation for conduit installation be compacted to 95 percent. BIA based that requirement on the FP-79 criterion that the bedding material be “thoroughly compacted” (FP-79, sec. 603.03) and the asserted industry standard that “thorough compaction” means 95 percent (Tr. 1069). On cross-examination of Mr. Natewa, HCJ brought out that there is a separate FP-79 provision on compaction (Tr. 1090-92). The section mentioning “thorough compaction” is more properly described as an excavation provision than a compaction provision. It is entitled “603.03 Excavation” and calls for excavation “to a width sufficient to allow * * * thorough compaction of the bedding * * * material under * * * the conduit.” (Italics supplied.) Section 603.03 also refers to section 206, which has a subsection which more clearly directs compaction. This is subsection 206.03 (also entitled “Excavation,” incidentally) which contains a paragraph entitled “(c) Pipe culverts.” It calls for “selected fine compressible material” to be “lightly compacted” or “approved granular foundation fill material properly compacted” as bedding material for the pipe depending on whether the natural ground provides a firm foundation or a nonfirm foundation, respectively. (Italics supplied.) Whatever these terms mean, they are apparently distinct from “thoroughly compacted,” and BIA’s 95-percent compaction requirement insofar as it relies on a “thoroughly compacted” term in FP-79 is therefore misplaced.

Although HCJ thus appears to prevail on this interpretation issue, it has failed to preponderate on the issue of delay arising from BIA’s compaction requirement. It appears that BIA acquiesced in an 85-percent compaction effort the day after HCJ’s complaints first came to Mr. Natewa’s attention (while it nevertheless still maintained that a 95-percent requirement was justifiable under the contract) (Tr. 1070-71). We therefore conclude that any delays actually caused to HCJ by the 95-percent requirement (and any related proctor problems) were insignificant.

**IBCA-2153**

**Prompt Payment Act Interest**

HCJ demands reimbursement for Prompt Payment Act interest in the amount of $5,661.10 for late payment of five invoices on normal estimated quantities work and an additional $456.45 on one invoice for force account work. At and since the hearing stage, BIA has strongly
objected to the payment of Prompt Payment Act interest but has failed to offer evidence in support of its position except as to one of the items. It introduced Mr. Natewa's testimony on Mr. Harvey Jones' refusal to sign a pay estimate because BIA proposed making a payment in respect of 80 percent of the quantities estimated since there were serious questions about the adequacy of performance on the items in question (Tr. 1081-86; see AF, Tab 43). Our search of the record, however, discovered that BIA had taken the administrative, prehearing position that no payments were late and any "delay" in payment resulted from HCJ's delay in signing the pay estimates (see, e.g., AF Tab 43 at 4, ¶ 10).

Although BIA's defense would not be sufficient to rebut a properly presented case on this issue, BIA has denied HCJ's contentions and the Board finds that the evidence offered by HCJ was not of probative value. HCJ's hearing presentation consisted of its accountant's testimony and an exhibit he prepared (Tr. 425-26; AF, Tab 50, Schedule 5). The record contains no reliable information which such hearing evidence might serve to corroborate. We conclude therefore that HCJ has failed to prove the elements of its claim, except in regard to one particular item. In regard to that item we find that HCJ filed what amounts to an invoice for force account work in a letter dated January 4, 1984; that Mr. Harvey Jones signed a pay estimate form covering the same force account work, at least by amount, attached to a letter dated January 8, 1984; and that such documents were organized under the same appeal file tab by BIA (AF, Tab 17). The amount demanded for that force account work in January 1984 is higher than the amount on the accountant's schedule. By matching dates, amounts, and other information in the HCJ case with similar information in the audit report (AF, Tab 37), however, we are convinced that it is the same item that was paid in September 1984 and listed in the schedule. Although HCJ's case on this item is thus relatively weak, it does qualify as a prima facie case and in light of BIA's failure to counter it effectively we find that HCJ is entitled to $456.45 interest for late payment. This amount will be reflected in our final recapped recovery amount following the Quantum section below on IBCA-2150, 2151, and 2152. It may be that there is evidence in the record that would similarly corroborate some or all of the other interest items, but the matching process is so difficult and the HCJ information so sketchy that we consider the failure of our considerable efforts to find such as fatal to HCJ's claim.

IBCA-2070

In its brief, HCJ notes that it has announced its decision not to seek damages under this appeal, and we acquiesce. The appeal in IBCA-2070 is denied.
In its brief, HCJ contends that there was a “cumulative impact” of the various specific delays and that cumulatively they caused HCJ to perform the job in the “jumping around,” inefficient fashion already mentioned herein. This is effectively a position that demands reimbursement for inefficiency, but because, as indicated above, the great bulk of HCJ’s various appeals entails claimed reimbursement arising out of delays, we believe the inefficiency HCJ highlights can be fitted into the delay claim, and we do that in the Quantum section below. In this connection the Board notes that HCJ has not in its brief identified with particularity the individual components for which it seeks reimbursement in this appeal.

Neither does the HCJ brief identify what it means by “Additional Costs,” but we have identified one such area. BIA removed Mr. Sandy Jones from the project in early November 1983 (AF, Tab 8). Nothing in the record adequately shows what the reason for this action was, but we know that BIA has admitted that it was a mistake. In a meeting approximately one week later, the CO apologized for the removal. He delivered that apology to the since-deceased Mr. Harvey Jones, president of HCJ, who took over Mr. Sandy Jones’ duties on the project, and made clear that the removal ban was lifted but there is no indication of a written, formal apology and rescission in the record, despite at least two written requests therefor from HCJ (AF, Tabs 14, 17). Mr. Sandy Jones returned to the project at the spring 1984 restart and performed as project manager until completion.

HCJ demands reimbursement for 7 weeks of Mr. Sandy Jones’ salary, being measured from the removal until the winter shutdown in December; it also requests reimbursement for his car expenses during that period and for attorney’s fees allegedly incurred in connection with the removal (Tr. 428; SAF, Tab 50, Schedule 9).

Although BIA has not disputed the correctness of the amounts involved, we are disinclined to grant the appeal in respect of attorney’s fees, because we have no cognizable evidence on how or why the fees were incurred other than the exhibit noting them, which amounts to little more than an allegation. On the other items, there is a sound basis for granting reimbursement because, clearly, the removal was wrongful. It was not unreasonable for HCJ to demand a formal rescission before sending Mr. Sandy Jones back to the project and there is a serious lapse in BIA’s failure to provide that formal rescission. We therefore conclude that HCJ is entitled to recover the sum of $4,449 for salary and auto expenses paid to Mr. Sandy Jones.

Quantum

The quantum portion of this case is factually as complex and as contested as the entitlement portion. There are two related quantum
matters which require discussion prior to the major quantum issue below. Both have reference to the proper equipment rates to be used to figure compensable harm to HCJ. The first concerns the “blue book” rate issue. HCJ contends that the CO refused to accept its early claims (there were ultimately five claims in the case, none the subject of a final CO’s decision), because they were based on HCJ’s “in house” rates for equipment and that the CO rejected them on that basis and ordered HCJ to resubmit using “blue book” rates. The “blue book” referred to is a rental rate guide published by the Equipment Guide Book Co., and used by a number of contracting agencies in similar circumstances; it lists typical national rates for equipment usage based on the publisher’s extensive surveys of a variety of factors making up the rates (Tr. 262-63). HCJ also contends that when BIA conducted its audit of HCJ’s “first final” claim, the auditors suggested that HCJ’s equipment rates were flawed, because the claim used 1983 rates when a significant portion of the claim related to 1984 equipment charges. HCJ then revised its claim to its “last final” version using both 1983 and 1984 “blue book” rates. BIA ordered another audit. The first final claim was in the amount of $559,729; the last final claim was for $866,484 (App. Br. at 4-6).

The basis for the “blue book” claims is an alleged verbal direction from the CO delivered in a meeting on the initial two claims convened on March 30, 1984. There is a tape recording of that meeting on which the “blue book” term can be heard but it is not clear, according to the hearing testimony, whether the speaker was referring to the claims or to force account work. (See Tr. 380.) Mr. Garcia, the CO at that time, and HCJ’s witness could not remember that he had referred to the claim rather than to force account when he mentioned “blue book” at that meeting. Taking his testimony as a whole, however, it is clear that he did not intend to convey that impression to HCJ (Tr. 378-390). HCJ’s evidence depends on the testimony of two witnesses present at the March 30, 1984, meeting, a written statement by another participant and the fact that the CO did not return the allegedly resulting claim for the reason that it used “blue book” rates. HCJ’s case also relies on the conclusion that there was no other reason to return the original non-“blue book” claim, but a reason does appear in that Mr. Garcia testified that there was no substantive justification for the equipment costs in the original claim (Tr. 381).

Generally, a CO’s direction to use blue book rates in a claim would not bind the Government to pay those rates for equipment usage actually found to be compensable, although a CO could conceivably want the blue book rate as a guide for those circumstances when it was difficult to determine the contractor’s actual costs. In its Reply Brief, however, HCJ raised a theory where the existence of such a direction might be controlling. It refers to the Federal Procurement Regulations (FPR), which by its terms was applicable to this contract, and in
particular to the FPR section codified at 41 CFR 1-15.107. That section provides for the use of “advance understandings” on particular cost items that might be difficult to determine because of disagreements on reasonableness, allocability, and other measures of allowability (App. Rep. Br., 27-28). Specifically contemplated by the FPR provision as a suitable subject of such an advance agreement is “Use charges for fully depreciated assets.” 41 CFR 1-15.107(g)(2). The equipment for which reimbursement costs are claimed is fully depreciated equipment, so this subsection would appear to have this controversy within its purview. Although we have serious misgivings about whether the HCJ proof on the alleged CO direction establishes what our unaided construction of an “advance understanding” is, the FPR section itself provides guidance which is prejudicial to HCJ’s case. Section 1-15.107(a) strongly recommends negotiation of an advance agreement “before incurring of the cost covered by the agreement” and requires, inter alia, that the agreement be in writing and incorporated into the contract. There clearly was not a written agreement on blue book rates here, but HCJ spent a good deal of briefing effort on the CO’s authority as CO and as an authorized agent of his principal. It is assumed that HCJ emphasized that argument in an attempt to get around the “in writing” requirement in the FPR provision on advance agreements, i.e., the Government is estopped from denying the existence of a writing because of the clear, oral “agreement” announced by the CO. Besides our finding that HCJ did not preponderate on the factual issue of the CO’s alleged direction, we also note that one element of estoppel as applied to this case would be that HCJ relied on the CO’s blue book direction to its detriment. Except for reworking its claim, for the costs of which no demand has been made, HCJ cannot show detrimental reliance. It clearly did not incur equipment costs because of the alleged oral direction, but rather because that incurring was necessary to perform the work, regardless of what the cost thereof might be. We therefore will not use the blue book rates to measure the costs for equipment to which HCJ is entitled to be reimbursed.

The second preliminary quantum matter also relates to equipment rates and centers on HCJ’s “in-house” rates. The BIA auditors essentially disallowed any equipment charges as a result of their audits of the HCJ claims because they were unable to substantiate any cost from HCJ’s records, and BIA has essentially adhered to that position as it argues against any award (BIA Br. at 39-40).

Although a charge for “depreciation” may not be allowed on fully depreciated equipment, that does not mean that in an equitable adjustment a contractor should not be reimbursed for the ownership costs for such equipment. Indeed, the FPR recognizes that such costs are reimbursable even if “depreciation” is not allowed. 41 CFR 1-15.209(h). The FPR provision just cited relies on a § 1-15.107 “advance agreement” on reasonable equipment use costs for its application, but its importance to this case is that it contemplates that there are ownership costs for fully depreciated equipment for which it is
equitable to allow recovery. Other guidelines used by Federal agencies similarly promote the concept that there are compensable costs of ownership of equipment that has been fully depreciated. (See Sanders Construction Co., IBCA-2309 (Oct. 25, 1989), 26 IBCA 331, 90-BCA 1.)

We believe that HCJ established its “in-house” rates for equipment usage as a reasonable measure to use for this purpose. HCJ’s secretary-treasurer Mrs. Jones testified that she developed the various rates from in-house records (Tr. 446-48, 472-73) (see also Tr. 404-07), and those rates are reflected in App. Exh. M. HCJ’s Mr. Ziler, the CPA, testified about the difficulty a company of the size and nature of HCJ has in keeping auditable records about certain costs, delays, equipment depreciation and other equipment charges especially where such must be allocated (Tr. 1227-28, 1229-30, 1231-34). We take his testimony to mean that although the BIA auditors might not find company records on which to base an allowance recommendation, that does not mean that HCJ did not have costs of ownership even if they were difficult to ascertain precisely. Finally, Mr. Sandy Jones presented evidence on a survey taken for HCJ by the Arthur Anderson Co. to establish the average rental rate for the equipment in the area (App. Exh. L, Tr. 396-404). The evidence of operating costs for the 14 pieces of equipment disclosed that there were 10 above HCJ’s in-house rate, 2 below and 2 about the same even after the surveyed rental rate was discounted for the owners’ presumed profit margin of 15-percent. A substantial portion of the survey rates for idle equipment were also above the same HCJ in-house rates (which were used for both “ownership” and for “operating” purposes), even after the same 15-percent discount. In the circumstances as just detailed, we believe that the HCJ in-house rates for equipment usage are reasonable and applicable here. The amount HCJ demands using its in-house rates is $509,376.65 including all items in the case whether or not related to delay.

Having decided the rate to use for equipment usage, the largest single item in HCJ’s quantum case, we can track its use in the principal vehicle for proof of quantum, its Exhibit M, and see that its ultimate figure for demanded compensation is essentially justified according to its theory on quantum. This applied as well to the other items in its case like labor, overhead, profit, general and administrative, gross receipts tax, etc., to none of which has BIA mounted a serious attack as to amount or rate. Insofar as we have trouble with that theory, however, we do not believe that our ability to track the rate logically through the exhibit applying that theory is particularly helpful in precisely determining the proper quantum. The theory is that since HCJ was delayed, then it should be compensated for all of its costs incurred beyond the chronological point when it would have finished but for the BIA-caused delays, which is the 75-
calendar day period proposed for completion in HCJ’s construction schedule.

The Board has previously found that “given a reasonable manpower level, a lack of significant delaying factors of the reasonably unforeseeable variety, and a reasonably satisfactory administrative and productive effort,” a contractor could perform the work in 75 calendar days. What the Board did not find was that those “givens” were actually in existence in this contract performance. Indeed, BIA produced a substantial body of evidence probative of the fact that some of the delays, especially those in 1983, were HCJ’s responsibility. BIA put on extensive evidence of the level of HCJ’s manpower aimed at showing that, especially during the early periods of performance, the contractor had insufficient personnel to complete the job in 75 days. It introduced evidence of alleged shut-downs, including the early November event that culminated in Mr. Sandy Jones’ removal from the site, and of days not worked. It contended that some of the absences were for the purpose of working on a different contract. It introduced evidence that HCJ was using improper or impractical construction techniques and that there were occasions when an HCJ official complained about having no work to do because of problems for which BIA was responsible which were followed by a BIA official’s pointing out substantial amounts of work to do which the complaining HCJ official then conceded. Also, there is a persistent undercurrent throughout the record to the effect that HCJ, in its frustration over what it believed was BIA incompetence and intransigence, became so uncooperative and impatient that its attitude detracted from its own efficiency. Although HCJ presented at least some rebuttal to many of these points and on other points as well, the BIA evidence is substantial and reliable and based thereon, we find that a significant number of the delays encountered was HCJ’s responsibility.

The trouble we have with HCJ’s theory would be inconsequential if it had presented evidence alternatively on which we could make delay duration findings, but it did not.

The principal vehicle of HCJ proof on quantum was its Exh. M compiled by its CPA witness Mr. Winter who testified about it extensively. Although Mr. Winter admittedly had no personal knowledge of the legal and factual underpinnings of the document, HCJ has been thorough in explaining that there are administrative record entries on which Mr. Winter relied in compiling the multi-

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1 See especially the testimony of the COR (David Holmes) at Tr. 644-88.

2 In the course of his testimony the COR read the following passage from paragraph 13 of the Daily Construction Report for Oct. 13, 1983 (AF, Tab 36): “Dave Holmes asked Mr. Jones why they were filling the road lane-by-lane instead of completing the road for each lift. Mr. Jones stated he didn’t know, but the rest will be filled on both lanes each lift” (Tr. 682).

3 For instance, Mr. Montoya, the supervisor civil engineering technician, testified about a meeting with Mr. Harvey Jones in late November 1983. He recalled that Mr. Harvey Jones had complained that pipestaking was incomplete and, “So again, on the 30th, we went through the project, and I showed him where all our pipes were staked out. I showed him five pipes on Line B that were ready to be installed, three on Line C, and two on Line A. And he admitted to me, he says, ‘I didn’t think you were that far ahead of me’ ” (Tr. 1087). Mr. Montoya recollected a similar incident at Tr. 1087; see also Tr. 640.
schedule exhibit. The problem is that those entries are no less conclusory in character than the entries in the exhibit, and we had no detailed testimony on which to rely to ascertain that they were reasonable and connected to the BIA-caused delay. As an example of the difficulty we had in this endeavor, we note that the project was accepted as substantially complete on May 25, 1984. We also know that there was a more than minor amount of punch list-type, cleanup work to be done on the project. An understanding of the extent of the remaining work, however, has been insufficiently aided by the parties for it to be immediately apparent why 256 hours of equipment time, totalling well over $28,000 in costs was necessary between August 20, and September 14, 1984, as shown on page 0355m-p 3 of the exhibit. Another example relates to a controversy over a BIA request for an estimate on the placement of certain rip-rap which would have been an extra to the contract. HCJ contends that it related to BIA that it could not provide an estimate without a plan or design and that BIA's failure to provide such “resulted in 8 weeks of standby time” starting in late May 1984. (Referenced on the second page of App. Exh. M.) HCJ did not make a showing sufficient for us to conclude that this was a matter reasonably connected to the BIA delay that it should be included in the case as constituted under HCJ’s theory. It is also unclear whether and how much this issue actually affected the amount of HCJ’s demand in the appeal, although the exhibit page referenced above does have entries for the period in question that total over $21,000 in “delay” and at least $17,000 in “standby” for equipment. A related problem can be observed when the HCJ case’s scheme on entitlement is compared with its scheme on quantum. The various subissues on entitlement ("Basecourse," “Unclassified Excavation and Borrow,” etc.) all conclude with a very precise amount of recovery demanded, implying because the principal theory is delay, that HCJ had done a calculation of just how much delay each of the subissues’ proof accounted for, but when it endeavored to prove quantum, HCJ in essence merely proved all of its costs beyond a certain date. Its lack of argument on “Cumulative Impact and Additional Costs” when juxtaposed with its substantial entitlement proof and argument on the other sub-issues and the latter's precise damage figures causes us to contemplate whether HCJ included the “Cumulative Impact” category as a catch-all to account for the difference between total costs and the presumably identifiable delay costs demanded under the other categories. It thus forces us also to contemplate whether there are some overlapping items in the quantum total or whether the nearly $74,000 demand under the “Cumulative Impact” category could be related to HCJ-caused delay.

In any event, it is the appellant’s burden to prove its quantum with precision if it expects us to grant its appeal in the amount demanded and in these circumstances we cannot conclude that HCJ has done so.
On the other hand, our analysis under the Entitlement section resulted in findings in HCJ's favor in nearly every particular. Regardless of BIA's adducing substantial evidence on nearly every item and that we were thus forced to find facts on the basis of preponderance, the findings taken as a whole establish that BIA's effort was seriously substandard. Moreover, the evidence also establishes that the contract's administration was something other than model in nature. The various Government personnel failed to clear utilities before start of work. The CO admitted that he was aware of substantial Government deficiencies in the field and of contractor complaints about them but he did nothing to rectify the situation. BIA never wrote a final decision on any of the five claims submitted. In the field BIA contract administrators were often intransigent on the principal issues about which HCJ complained, including borrow excavation, density proctors, staking, and ditch design. This intransigence went so far, in one instance, that BIA failed to relax its standards for measuring compaction even after one official, prompted by the complaints to recheck the assumptions, determined that indeed the standards were too high. The field and administration inadequacies taken as a whole create a picture of such serious misfeasance that we find it difficult to sympathize with BIA's objections to the all-costs HCJ approach, especially where we rejected its principal defense, that it was blameless, and where its secondary defense, that HCJ was responsible for delays, though marginally successful, was unaccompanied by any proof of the precise extent thereof.

Nevertheless, that lack of sympathy and the difficulty a contractor of HCJ's type and character has in precisely tracking all of its costs do not establish an excuse, of course, for HCJ's failure to prove quantum reasonably precisely and with reasonable connection to its entitlement case. That failure is aggravated by HCJ's inclusion in its demand of what appear possibly to be expenses that are not sufficiently related to the delays attributed to BIA and expenses that are overlapping on others. Of even greater importance is the clear proof that HCJ was responsible for some of its delays. Still, BIA certainly caused HCJ additional expense. HCJ's demand for $509,376.65, which includes amounts for prompt payment interest and "additional costs," which we have already treated, is in an amount well in excess of the contract amount even as amended for extra work.

As has previously been noted, the claim as presented was for all costs incurred by HCJ after the 75-calendar day period shown in the Construction Schedule submitted by HCJ for completion of the contract work (i.e., not later than by November 26, 1983). From an early date claims presented on a total cost basis have been disfavored. One of the principal reasons for that lack of favor is present here as

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6 The fact that HCJ has been unable to show that it could have completed the contract work within such period does not mean that the contractor is entitled to no relief. See John A. Johnson Contracting Corp. v. United States, 132 Ct. Cl. 645, 656 (1953); Paul C. Helmick Co., IBCA-39 (Oct. 31, 1956), 63 I.D. 365, 365, 56-2 BCA ¶ 1096 at 2777 (Board not precluded from deciding a claim upon the basis of a theory not advanced by the parties).
the foregoing has demonstrated. It is that in the usual case at least some (and sometimes, perhaps, all) of the costs for which claim is being made have no relationship to the compensable event or events (here failure to remove utility lines, staking errors, improper testing methods, design problems) on which the claim or claims are founded. See Montgomery-Macri Co., IBCA-59 and IBCA-72 (June 28, 1963), 70 I.D. 242, 264-65, 1963 BCA ¶ 3819 at 19,016-17.

Where, as is the case here, entitlement has been found but the amount as to equitable adjustment cannot be determined with any degree of mathematical precision, this Board has resorted to what has aptly been described as the jury verdict approach. See Central Colorado Contractors, Inc., IBCA-1203-8-78 (Mar. 25, 1983), 90 I.D. 109, 145, 83-1 BCA ¶ 16,405 at 81,573. Taking into account the various factors to which we have adverted and bearing in mind that HCJ has the burden of proving not only the validity but the quantum of its claims (Montgomery Macri Co., supra, 70 I.D. at 263, 1963 BCA ¶ 33,819 at 19,015), the Board finds that the equitable adjustment to which appellant is entitled for the claims asserted under IBCA-2150, IBCA-2151, and IBCA-2152 is in the aggregate amount of $250,000.

Summary

The appeal in IBCA-2070 is denied. The appeal in IBCA-2153 is sustained in part in the amount of $456.45. The appeal in IBCA-2467 is sustained in part in the amount of $4,449. The appeals in IBCA-2150, IBCA-2151, and IBCA-2152 are collectively sustained in part in the amount of $250,000, for a total amount for all appeals of $254,905.45, plus interest computed in accordance with the Contract Disputes Act of 1978. All of the appeals are denied in all other respects. The claim for attorney fees is dismissed as premature. 5 U.S.C. § 504.

WILLIAM F. McGRAGW
Administrative Judge

I CONCUR:

RUSSELL C. LYNCH
Chief Administrative Judge
MELVIN HELIT v. GOLD FIELDS MINING CORP.

113 IBLA 299

Appeals from separate decisions of the California State Office, Bureau of Land Management, dismissing private contests of unpatented millsites (CA CA 22514, 22515, and 22762); rejecting in whole or in part notices of location of placer mining claims (CA MC 196854 through 196860); and dismissing protest of application for patent of millsites (CA CA 20913).

Decision dismissing contests affirmed in part and affirmed in part as modified; decision dismissing protests affirmed.

1. Administrative Procedure: Standing--Rules of Practice: Appeals: Standing to Appeal
Standing to appeal requires that an appellant be both a party to the decision appealed from and adversely affected by the decision. To be adversely affected, an appellant must have a legally cognizable interest in the land at issue.

2. Res Judicata--Rules of Practice: Appeals: Effect of
Under the doctrine of administrative finality, the administrative counterpart of the doctrine of res judicata, when a party has had an opportunity to obtain review within the Department and no appeal was taken, or an appeal was taken and the decision was affirmed, the decision may not be reconsidered in later proceedings except upon a showing of compelling legal or equitable reasons, such as violations of basic rights of the parties or the need to prevent an injustice.

A final decision by the Department after a contest hearing holding land to be either mineral or nonmineral in character is res judicata and conclusive between the parties regarding the status of the land at the date of the hearing, but does not preclude further consideration of the character of the land based on subsequent exploration and development.

4. Contests and Protests: Generally--Mining Claims: Contests--Rules of Practice: Private Contests
A contest complaint is required to contain a statement in clear and concise language of the facts constituting the grounds of the contest. A party seeking a hearing as to the mineral character of land which has been subject to a prior Departmental hearing must make a distinct showing of development made since the prior hearing, such as, if supported by the evidence at the hearing applied for, would clearly demonstrate that since such prior hearing mineral has been discovered in such quantities, and by such thorough work on the premises, as to overcome the effect of the previous judgment as to the character of the land.

5. Contests and Protests: Generally--Mining Claims: Contests--Rules of Practice: Private Contests
An affidavit by a contest complainant is not a substitute for an affidavit of a witness corroborating the factual allegations of the complaint as required by 43 CFR 4.450-4(c).
In the absence of an affidavit of a corroborating witness, a private contest complaint is properly dismissed.

6. Administrative Authority: Generally--Administrative Procedure: Adjudication--Contests and Protests: Generally--Mining Claims: Contests

Although 30 U.S.C. §§ 29, 30 (1982), do not authorize the Department to rule on the merits of an adverse claim, it is within the Department's authority to determine whether a document presents an adverse claim within the meaning of the statutes. The issue whether land is mineral or nonmineral in character is within the exclusive jurisdiction of the Department of the Interior and for this reason a conflict between mineral and nonmineral claimants does not raise an "adverse claim" within the meaning of the term in the statutes.

7. Mining Claims: Generally--Mining Claims: Patent

A patent may be issued to a corporation organized under the laws of the United States or any state or territory irrespective of the ownership of the stock of the corporation by persons, corporations, or associations who are not citizens of the United States.


When a mineral locator has filed a location certificate with BLM within 90 days of the date of the location of the claim as required by 43 U.S.C. § 1744(b) (1982), it is error for BLM to later reject the recordation of the claim. BLM's decision cannot change the fact the locator has complied with the statute. The fact the claim has been recorded with BLM, however, does not establish its validity.

APPEARANCES: Melvin Helit, Oceanside, California, pro se; William R. Marsh, Esq., and James M. King, Esq., Denver, Colorado, for Gold Fields Mining Corp.

OPINION BY ADMINISTRATIVE JUDGE GRANT

INTERIOR BOARD OF LAND APPEALS

Melvin Helit has appealed two decisions of the California State Office, Bureau of Land Management (BLM). BLM's first decision (appeal docketed as IBLA 88-665), dated August 12, 1988, dismissed three private contests filed by Helit (CA CA 22514, 22515, 22762) against 101 millsite claims held by Gold Fields Mining Corp. (Gold Fields). The contests were predicated on conflicts with appellant's CABLE 27 through 34 placer mining claims (CA MC 196266 and CA MC 196854 through CA MC 196860). BLM's second decision (appeal docketed as IBLA 88-666), dated August 16, 1988, dismissed Helit's protest against Gold Fields' mineral patent application for the millsites (CA CA 20913). The appeals have been consolidated because they concern the same parties, lands, and conflicting mining claims and millsites.

BLM dismissed the contest complaints on two grounds. First, BLM determined they did not meet the requirements of 43 CFR 4.450-1 which allows contests to be initiated "for any reason not shown by the records of the Bureau of Land Management." BLM found that the
"factors upon which the allegations are based are shown by the records of the Bureau of Land Management" because the lands involved were the subject of a previous contest brought by Gold Fields against Helit and other parties (CA 19053 and CA 19054). A hearing had been held and Administrative Law Judge Michael Morehouse had ruled that the land was nonmineral in character and that Helit's claims were invalid (Decision at 1-2). Because BLM found the issues raised by appellant's contest complaints had been resolved in the prior proceeding, BLM concluded they were "barred by the doctrines of res judicata or administrative finality and collateral estoppel" (Decision at 2). BLM also rejected the contest complaints because they were not accompanied by statements of witnesses corroborating the allegations as required by regulation. See 43 CFR 4.450-4(c).

In addition to dismissing the contests, BLM determined that "[a]ll but one of the placer mining claims involved in the existing contest complaints appear to be relocations of placer mining claims declared invalid by Judge Morehouse in the previous proceeding." (Decision at 2.) For this reason BLM rejected the notices of location Helit had filed for recordation with BLM under section 314(b) of the Federal Land Policy and Management Act of 1976 (FLPMA), 43 U.S.C. § 1744(b) (1982), for the C-ABLE 28, 29, 31, and 34 claims "as to those portions situated within the lands involved in a previous court proceeding." Id. The decision also rejected, in their entirety, the notices of location Helit had filed for recordation with BLM for the C-ABLE 30, 32, and 33 placer mining claims.

BLM's second decision addressed a "Statement of Adverse Claim" Helit had filed with BLM during the 60-day period following publication of notice of Gold Fields' patent application. See 30 U.S.C. §§ 29, 30 (1982). BLM determined that the document was properly treated as a protest because the essential issue raised in a conflict between placer and millsite locations is whether or not the land is mineral in character. BLM dismissed the protest because it found the issue had been resolved in Judge Morehouse's decision in the previous contest and could not be relitigated.

Appellant's notice of appeal and statement of reasons for appeal of the dismissal of the contests lists certain matters which he asserts are reasons for invalidation of the millsite claims not shown by BLM records. Appellant contends that Gold Fields has not established a right to patent because it is a foreign corporation; that Gold Fields has not established rights senior to appellant; that Gold Fields trespassed in locating the millsite claims; and that Gold Fields has not established that the lands at issue are nonmineral in character. Appellant's arguments are set forth in the text of two documents which are incorporated by reference. One is a copy of a notice of appeal of Judge Morehouse's decision and an accompanying statement of reasons. The other is titled "Summary of Transcript of Proceedings/San Diego,
California/January 20, 1987/Volumes 1 - 5/and Comments"
(Summary) and was apparently prepared as part of the prior appeal of
Judge Morehouse's decision. Appellant also asserts that the required
statements of corroborating witnesses consist of his personal affidavits
contained in the contest complaints. Appellant further contends that
the C-ABLE claims at issue are not relocations.

Gold Fields requested and received an extension of time to file an
answer to await issuance of a decision in related cases docketed before
the Board as IBLA 88-524 and IBLA 89-130, cases involving the same
parties and related issues. Some of the same placer claims are at issue
in this appeal. Subsequently, Helit initiated a quiet title action in the
U.S. District Court for the Southern District of California and the time
for filing an answer with the Board was further extended pending
issuance of a decision on a motion for summary judgment filed by Gold
Fields in the court action. A decision in the consolidated appeals IBLA
88-524 and 89-130 was issued by the Board on August 10, 1989. Melvin
Helit, 110 IBLA 144 (1989). A decision on the motion for summary
judgment was issued by the court on November 9, 1989.2

On December 11, 1989, the Board received from appellant a motion
for expedited consideration. By order dated December 21, 1989, the
Board granted the motion.

In its answer to appellant’s statement of reasons, Gold Fields asserts
that appellant’s contest complaints are barred by the doctrine of res
judicata or its administrative counterpart, the doctrine of
administrative finality. This contention is based on the fact that
appellant’s placer claims, upon which standing to contest the millsites
is predicated, embrace the same ground which Judge Morehouse found
to be nonmineral in character in the contest proceeding to which
appellant was a party. Gold Fields asserts that the contest decision has
become final and was found to be binding on the parties by the
U.S. District Court in its order of summary judgment dated
November 9, 1989. Gold Fields further argues that the appeals should
be dismissed due to appellant’s lack of standing. It asserts that,
because appellant’s C-ABLE 27 through 34 placer claims include the
same land declared nonmineral in character by Judge Morehouse’s
decision, the claims were “void ab initio because mining claims may be
located only on ground that is mineral in character” (Answer at 6). As
a result, Gold Fields argues, under the rules of standing stated in Scott
Burnham, 100 IBLA 94, 94 I.D. 429 (1987), Scott Burnham (On
Reconsideration), 102 IBLA 363 (1988), and In re Pacific Coast
Molybdenum Co., 68 IBLA 325 (1982), Helit lacks an interest in the
land sufficient to give him standing to appeal (Answer at 7-8).

[1] Standing to appeal requires that an appellant establish that he
was a party to the decision appealed from and, further, that he is

1 The appeal was dismissed by order of this Board by order dated Oct. 22, 1987, due to failure to timely file the
notice of appeal in the proper office.
2 On Dec. 21, 1989, appellant filed documents showing that a notice of appeal to the Ninth Circuit had been filed in
the district court on Dec. 8, 1989.
adversely affected by the decision. *In re Pacific Coast Molybdenum Co.*, *supra* at 331; see 43 CFR 4.410(a). To be adversely affected, an appellant must have a legally recognizable interest in the land at issue. *Scott Burnham*, *supra* at 119-20, 94 I.D. at 443.

Gold Fields' argument as to standing is based upon Judge Morehouse's decision. This was also the basis of the BLM decisions on appeal. Consideration of Gold Fields' argument requires analysis of the scope and effect of Judge Morehouse's decision.

The private contest heard by Judge Morehouse was filed by Gold Fields as the holder of millsite claims against Helit's conflicting placer claims identified as the C-ABLE 13, 14, 15, 23, 24, 25, and 26. For the purpose of his decision, Judge Morehouse identified the land at issue as "contestant's [Gold Fields'] millsites in the SE¼ NW¼ and S¼ NE¼ of Section 7, S¼ N¼ of Section 8, SE¼ of Section 8 and NE¼ of Section 17" (Contest Decision at 3). The sections are in partially surveyed T.13 S., R. 19 E., San Bernardino Meridian, Imperial County, California. Because one area involved conflicting locations by three parties, the Judge divided the land at issue into east and west areas. Based on his review of the evidence, Judge Morehouse concluded that Gold Fields had "carried its burden in showing the land within the east and west conflict areas is nonmineral in character," adding that "the weight of the evidence in support of this conclusion is overwhelming, and there is little or no credible evidence to the contrary." (Contest Decision at 15.) He further concluded that "the seven contested placer claims which are the subject of these consolidated proceedings are found to be invalid." (Contest Decision at 16.)

The location notices for the C-ABLE 28 through 34 placer mining claims show that they were located July 19, 1987, 3 days prior to the issuance of Judge Morehouse's decision. Each location notice states that the claim consists of 80 acres and identifies the quarter section within which each claim is located. Amended notices of location for the C-ABLE 29 and 30 which were filed with BLM June 15, 1988, do not indicate a change in either the size or position of the claims. The location notice for the C-ABLE 27 states that it was located June 28, 1987, and consists of the S¼ of the NE¼ of sec. 7.

Maps submitted with the notice of location of the claims when recorded with BLM and with the contest complaints and adverse claim show the positions of the claims within the quarter sections identified in the location notices. A comparison of these maps with a map filed with the location notice for the C-ABLE 27 (CA 196266) confirms the similarity of the claims before us with those previously before Judge Morehouse. The C-ABLE 28 which occupies the S¼ NW¼ of sec. 7 appears to be identical to the C-ABLE 15. The C-ABLE 29 and 30 in the S¼ N¼ of sec. 8 appear to be identical to the C-ABLE 13 and 14. The C-ABLE 31 and 32 in the SE¼ of sec. 8 appear to be identical to the C-
ABLE 23 and 24. The C-ABLE 33 and 34 in the NE4¼ of sec. 17 appear to be identical to the C-ABLE 25 and 26. Only the C-ABLE 27 does not correspond to a C-ABLE claim adjudicated in the decision; however, the land it occupies, the S½ NE¼ of sec. 7, is embraced in Gold Fields' millsites which were the basis of the contest before Judge Morehouse and this land was the subject of adjudication in the decision. Thus, Gold Fields is correct that appellant's claims encompass the same land Judge Morehouse found to be nonmineral in character.

[2] Gold Fields is also correct that Judge Morehouse's decision has become final. By order of this Board dated October 22, 1987, the appeal of the decision was dismissed because it was not timely filed in the proper office and the decision became final for the Department. Melvin Helit, supra at 150. Under the doctrine of administrative finality--the administrative counterpart of the doctrine of res judicata—when a party has had an opportunity to obtain review within the Department and no appeal was taken, or an appeal was taken and the decision was affirmed, the decision may not be reconsidered in later proceedings except upon a showing of compelling legal or equitable reasons, such as violations of basic rights of the parties or the need to prevent an injustice. Lloyd D. Hayes, 108 IBLA 189, 192-93 (1989); Turner Brothers, Inc. v. OSMRE, 102 IBLA 111, 120-21 (1988). No such showing has been made by appellant. The finality of Judge Morehouse's decision was recognized by the order of the district court. Melvin Helit v. GFMC Exploration-California, Inc., No. 88-1100-JLI(CM), slip op. at 2 (S.D. Cal. Nov. 9, 1989).

[3] The specific issue posed by this appeal is the effect of the Administrative Law Judge's decision on appellant's subsequent claims located in 1987. A number of cases have dealt with the effect of a contest decision on a subsequent challenge to the mineral character of a tract of public land. As a general matter, the Department has followed the rule that "decision by the Department holding a tract of land to be either mineral or nonmineral in character will be considered conclusive up to the period covered by the hearing, but will not preclude further consideration of the character of the land based on subsequent exploration and development." Shire v. Page, 57 I.D. 252, 259-60 (1941). In Shire the Department held that "[i]n view of the previous judgment and the evidence as to the character and general formation upon which said judgment was based, the failure to supply concrete factual data supporting mere general allegations is not deemed sufficient" to justify reopening the question of the mineral character of the land. 57 I.D. at 260.4

The case of Gorda Gold Mining Co. v. Bauman, 52 I.D. 519 (1928), involved a petition for reconsideration of a Departmental decision

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3 The C-ABLE 28 occupies the S¼ NW¼ of sec. 7, of which only the eastern quarter-quarter section was adjudicated in Judge Morehouse's decision, apparently because Gold Fields did not have millsites in the western quarter-quarter section.

4 The Shire decision explicitly found a lack of privity between the former contestant and subsequent mining claimant and, hence, the absence of res judicata. 57 I.D. at 260.
rendered after a hearing finding mining claims in conflict with a homestead entry to be valid and directing a survey to segregate the claims and cancellation of the homestead entry as to the lands. The Department held the issue of the character of the land at the date of the hearing to be res judicata and declined to order any further inquiry, noting that petitioner had failed to show that exploration and development subsequent to the hearing had shown the land to be nonmineral. 52 L.D. at 521. The case of Bailey v. Molson Gold Mining Co., 43 L.D. 502 (1914), like the case at issue here, involved an appeal from dismissal of a protest against a mineral patent application. The decision stated that, as between two private parties invoking a private contest proceeding before the Department, the determination of their respective rights in a tract of land would generally be regarded as res judicata of all facts essential to support such a judgment (i.e., the mineral character of the land), but because the Department is not bound to accept such a determination of the character of the land, “such a judgment does not bar further inquiry as to the character of the tract.” 43 L.D. at 503. The decision noted the Department had since adjudicated the land to be mineral in character and held that the issue should not be readjudicated “except upon a protest which sets up definite and specific facts which if established at a hearing would clearly show the land to be nonmineral.” 43 L.D. at 504.

Similarly, the Department has held that a finding regarding the mineral character of land after a contest hearing between a mineral locator and nonmineral claimants at which evidence was taken could not be overcome by the mere allegation that the land contained no valuable mineral. “To secure a hearing to challenge the prior finding, it was necessary for the agricultural applicants to allege that exploration and development subsequent to the former hearing or trial had shown the land to be non-mineral or that the former decision was based upon fraud or mistake such as would justify further inquiry into the character of the land.” Coleman v. McKenzie, 28 L.D. 348, 353, review denied, 29 L.D. 251, 359 (1899).

Thus, a hearing in a private contest at which evidence is taken leading to a final Departmental decision with respect to the mineral character of the land at issue is binding as res judicata between the parties to the contest as to the status of the lands at the date of the hearing. However, under Departmental case precedent, this would not preclude a showing that exploration and development since the time of the hearing have disclosed a mineral discovery sufficient to support new claim locations. In the absence of a showing of substantial evidence of mineral discovery not previously disclosed, the filing of new locations for the same ground which was the subject of a prior contest

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5 The district court found the Administrative Law Judge's decision to be res judicata between the parties regarding the mineral character of the land at issue. Slip op. at 2-3.
hearing which resulted in a finding that the land was nonmineral in character would leave the locator vulnerable to a charge that the claims were not located or held in good faith. See United States v. Prowell, 52 IBLA 256, 260 (1981). In the present case, the new placer claims were located within six months after the hearing but prior to the issuance of Judge Morehouse's decision. The district court ruled Helit could not avoid the effect of the decision "simply by relocating new claims on this land after invalidation of their prior claims." Slip op. at 3.

The contest hearing was held January 20-23, 1987. The C-ABLE 27 through 34 placer mining claims were located June 28 and July 19, 1987. While the finality of the decision precludes appellant from challenging the decision or raising any issue addressed by it, he is not precluded from asserting that evidence derived from subsequent exploration and development shows the land to be mineral in character. Thus, Judge Morehouse's decision does not necessitate a conclusion that the locations at issue were invalid because the land was nonmineral. Nor does the decision preclude the Department from rejecting the patent application for some or all of the millsites because it determines that the land is mineral in character. See Marvel Mining Co. v. Sinclair Oil & Gas Co., 75 I.D. 407, 423 (1968); United States v. United States Borax Co., 58 I.D. 426, 430 (1943). Hence, we conclude that appellant has standing to appeal the BLM decisions.

With respect to the decision of BLM dismissing appellant's contest complaints, we find the decision must be affirmed. Presumably, as with other private contestants, appellant's purpose was to obtain a declaration that Gold Fields' conflicting millsites are invalid, thereby eliminating the conflict and allowing Helit and his co-locators unfettered use of the ground. See 2 American Law of Mining § 50.01 (2d ed. 1984). Appellant is allowed to file a private contest action because such a procedure assists the Secretary of the Interior in carrying out his duties to protect the interests of the government and the public in public lands, in that by such method there may be called to the attention of the Bureau of Land Management invalid claims to title or interest in public lands, the invalidity of which does not appear on the records of the Bureau of Land Management and of which the Bureau may be without knowledge.

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8 The district court cited United States v. Allen, 578 F.2d 226 (9th Cir. 1978), which addressed whether a party may, under the guise of repeated locations of invalid mining claims, use public lands primarily for residential purposes. The court held that the appellant had confused the right to explore with the right to reside and permanently occupy the land and that exploration without discovery does not confer a right to obstruct surface use. 578 F.2d at 287-88.

7 We recognize that our analysis varies from that of the district court. The court first declined to review the contest decision and Helit's allegations as to the evidence at the hearing on the grounds it lacked jurisdiction due to Helit's failure to exhaust administrative remedies as a result of his untimely appeal. As discussed in our opinion, we reach the same result based on the doctrine of administrative finality. The court dismissed Helit's other claims for relief because it found the C-ABLE 27 through 34 placer mining claims "cover the same ground as was the subject of the private contest decision," and that the decision "precludes further litigation of the same issue by plaintiffs against Gold Fields in this court or in any other forum under the doctrine of res judicata. Robi v. Five Platters, Inc., 888 F.2d 318, 321 (9th Cir. 1989)" (Slip op. at 2-3). We agree. The court also stated that the contest decision had "conclusively resolved the status of the land described therein as between Gold Fields and plaintiffs." Id. at 3. Here our analysis differs. As analyzed in the Departmental decisions discussed above, the issue litigated and decided was the mineral character of the land as of the date of the hearing.
Duguid v. Best, 291 F.2d 235, 242 (9th Cir. 1961). For the same reason, however, a private contest complaint must assert the invalidity of a claim based on a “reason not shown by the records of the Bureau of Land Management.” 43 CFR 450-1.

[4] Pursuant to our analysis in this decision, we find that BLM was required to dismiss the complaints for a slightly different reason than stated in its decision. A contest complaint is required to contain “[a] statement in clear and concise language of the facts constituting the grounds of contest.” 43 CFR 4.450-4(a)(4). Consistent with the rule of Shire v. Page, supra, a party seeking a hearing as to the mineral character of land which has been subject to a prior Departmental hearing must make

a distinct showing of development made since the prior hearing, such as, if supported by the evidence at the hearing applied for, would clearly demonstrate that since such prior hearing mineral has been discovered in such quantities, and by such thorough work on the premises, as to overcome the effect of the previous judgment as to the character of the land.

Mackall v. Goodsell, 24 L.D. 553, 556 (1897). Appellant’s complaints fail to contain any clear and concise statement of the facts which would show that, since the prior contest, a mineral deposit has been discovered in such quantity and of sufficient quality as to overcome the decision that the land is nonmineral in character. This is a fatal shortcoming, since, in the absence of such information, the nonmineral character of the land is res judicata between appellant and Gold Fields as the district court held.

[5] BLM also rejected the contest petitions because statements of witnesses corroborating the allegations of the complaints did not accompany the documents as required by 43 CFR 4.450-4(c). In reply, appellant refers to pages of the complaints where the “statement of witness” may be found. We have examined these pages as well as the rest of the complaints. The only documents we find are affidavits by the appellant, Melvin Helit.

The regulation requires that statements of witnesses corroborate the factual allegations of the complaint. The purpose of the requirement is to assure there is evidence of the truth of the facts alleged, thereby preventing “the allowance of unjustifiable attacks against entries, thus relieving the Land Department of the consideration of speculative and unwarranted contests and entryman from the trouble and expense attendant on the defense thereof.” Nemnich v. Colyar, 47 L.D. 5, 7 (1919). The complainant is not a corroborating witness and his affidavits cannot confirm the facts alleged in the complaint. Winegeart v. Price, 74 IBLA 373, 380-81, 90 I.D. 338, 342 (1983). They serve only to confirm that the allegations of the complaints were made under oath, as required by the regulations. See 43 CFR 4.450-4(a). The regulations allow summary dismissal of a complaint when it fails to meet the requirements of the regulations. 43 CFR 4.450-5(a). Accordingly, BLM

Regarding appellant's adverse claim which was treated by BLM as a protest and dismissed, we note that Gold Fields was required to post and publish notice of its application for patent to the millsites. 30 U.S.C. § 29 (1982). Appellant filed a "Statement of Adverse Claim" with BLM on July 1, 1988, within the 60 days allowed by the statute. The statutes providing for adverse claims require BLM to stay "all proceedings, except the publication of notice and making and filing of the affidavit thereof, * * * until the controversy shall have been settled or decided by a court of competent jurisdiction, or the adverse claim waived." Id. § 30; see 43 CFR 3871.4. The party filing the adverse claim is required, "within thirty days after filing his claim, to commence proceedings in a court of competent jurisdiction, to determine the question of the right of possession, and prosecute the same with reasonable diligence to final judgment" and the statute provides that failure to do so "shall be a waiver of his adverse claim." 30 U.S.C. § 30 (1982).

[6] Although the statutes providing for adverse claims do not authorize the Department to rule on their merits, John R. Meadows, 43 IBLA 35, 37 (1979), it is within the Department's authority to determine whether a document presents an adverse claim within the meaning of the statutes. Thomas v. Elling, 25 L.D. 495, 497 (1897). If the document does not present an adverse claim such as is contemplated by the statutes, BLM may take other appropriate action or, if a judicial suit has been filed, the Department may choose to await the result. Brown Land Co. v. The Cleveland-Cliffs Iron Co., 17 IBLA 368, 378, 81 I.D. 619, 623 (1974).

Appellant's "Statement of Adverse Claim" asserted that he was "a co-owner of the possessory right and title" to mining claims "on which valuable mineral deposits" had been discovered. BLM determined that because the issue presented in a conflict such as this between placer locations and millsite claims is the mineral character of the land, appellant's statement could be treated as a protest. BLM was correct. The issue whether land is mineral or nonmineral in character is within the exclusive jurisdiction of the Department of the Interior and for this reason a conflict between mineral and nonmineral claimants does not raise an "adverse claim" as the term is used in 30 U.S.C. §§ 29, 30 (1982). See In Re Pacific Coast Molybdenum Co., supra at 329-30; Low v. Katalla Co., 40 L.D. 534, 538-40 (1912); Grand Canyon Railway Co. v. Cameron, 35 L.D. 495, 496-97 (1907). Since the "adverse claim" did not itself constitute a contest, BLM properly treated it as a protest.8

8 "Where the elements of a contest are not present, any objection raised by any person to any action proposed to be taken in any proceeding before the Bureau will be deemed to be a protest and such action thereon will be taken as is deemed to be appropriate in the circumstances." 43 CFR 4.450-2; see 43 CFR 3872.1.
We also affirm the dismissal of appellant’s protest for failure to state any basis upon which the protest could be upheld by BLM. Appellant has challenged the right of Gold Fields to hold the millsite claims, contending that allowing a domestic corporation to hold mining claims when it is a subsidiary of a foreign corporation is contrary to the original purposes of the citizenship provisions of the Lode Law of 1866 (Act of July 26, 1866, ch. 262, 14 Stat. 251) and the Mining Law of 1872 (Act of May 10, 1872, ch. 152, 17 Stat. 91).

[7] Appellant contends that the statutes’ citizenship provisions have been misinterpreted and misapplied. As noted in In re Pacific Coast Molybdenum Co., 75 IBLA 16, 38, 90 I.D. 352, 365 (1983), since at least 1899 the practice of the Department of the Interior has been to issue patents to a corporation organized under the laws of the United States or any state or territory irrespective of the ownership of stock of the corporation by persons, corporations, or associations who are not citizens of the United States. See Clark’s Pocket Quartz Mine, 27 L.D. 351 (1898). The regulations provide that the citizenship of a corporation is established by filing a certified copy of its charter or certificate of incorporation. 43 CFR 3862.2-1. On several occasions the Department has considered the issue and each time found insufficient reason to change the rule. Melvin Helit, supra at 152-53; In re Pacific Coast Molybdenum Co., 75 IBLA at 37-39, 90 I.D. at 364-65; Solicitor’s Opinion, M-36738 (July 16, 1968); Instructions, 51 L.D. 62 (1925).

It is indisputable that the Department’s construction of the provision allows aliens, as well as foreign corporations, to locate and hold mining claims by forming a corporation under the laws of a state or territory. See 1 American Law of Mining § 31.04[3] (2d ed. 1984). Appellant has “failed to show why this consistent interpretation, stretching over nearly a century of adjudication, should be abandoned at this late date.” In re Pacific Coast Molybdenum Co., 75 IBLA at 37-39, 90 I.D. at 365; followed Melvin Helit, supra at 152-53. We reaffirm our prior rulings in this respect.

Finally, we must consider BLM’s rejection, in whole or in part, of the recordation of all but one of the notices of location for the placer claims because they “appear to be relocations of placer mining claims declared invalid by Judge Morehouse in the previous proceeding” (Decision at 2). Appellant was required to file the claims with BLM within 90 days of the date of their location by section 314(b) of FLPMA. 43 U.S.C. § 1744(b) (1982). Failure to file a claim as required by the statute is deemed to conclusively constitute an abandonment of the claim. 43 U.S.C. § 1744(c) (1982); United States v. Locke, 471 U.S. 84 (1985). The consequence of BLM’s rejection of appellant’s location notices is that appellant would not have complied with the statute and his claims would be void for that reason.

[8] The location notices are datestamped as having been received by BLM September 15 and 28, 1987. A comparison of these dates with the
dates of location shows that they were filed within the time allowed by the statute. Thus, appellant complied with the law. BLM's decision cannot change the fact. Add-Ventures, Ltd., 95 IBLA 44, 50 (1986); see John D. Ketscher, 32 IBLA 235, 238 (1977). The reason stated by BLM for rejecting the location notices suggests that its conclusion was actually that the claims were invalid because they could not be located on the land addressed by Judge Morehouse's decision. If so, a decision finding the claims null and void ab initio for this reason would have been the appropriate course of action.

The fact the locations remain on file with BLM does not give appellant any rights he does not have by virtue of their validity or invalidity otherwise under the mining laws. Add-Ventures, Ltd., supra at 48; see John D. Ketscher, supra. If BLM determines that Gold Fields' millsite locations are proper and in compliance with the law, upon issuance of a patent, appellant's claims will become nullities because there is no longer any Federal land to which they can attach as locations under the mining laws. Scott Burnham, supra at 116, 94 I.D. at 441. Accordingly, the decision dismissing appellant's contest complaints is affirmed as modified to delete the rejection of the recordation of appellant's claims.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision dismissing appellant's protest is affirmed and the decision dismissing appellant's contests is affirmed in part and affirmed in part as modified.

C. RANDALL GRANT, JR.
Administrative Judge

I CONCUR:

WM. PHILIP HORTON
Chief Administrative Judge

APPEAL OF NIKO CONTRACTING CO.

IBCA-2368

Decided: March 30, 1990

Contract No. CX-3000-6-0080, National Park Service.

Sustained.

Contracts: Construction and Operation: Drawings and Specifications--Contracts: Disputes and Remedies: Equitable Adjustments

* There is a longstanding rule that a mineral entry cannot be allowed for land within an existing entry so long as the latter remains of record and the prior entry must be removed before a mineral patent application can be processed. See Roos v. Altman (On Petition), 54 I.D. 47, 56-57 (1932); Walter G. Bryant, 58 I.D. 379 (1981). A BLM record of a mining location filed under 43 U.S.C. § 1744(b) (1982), is not an entry in the same sense of the term. See Scott Burnham, supra at 109-10, 94 I.D. at 437.
Where a contractor's estimate of screw fasteners required to comply with specified spacing is found to be correct and additional screws are required to make a Government approved plywood underlayerment for roofing membranes to lay flat, the added fasteners are found to be an additional contract requirement for which the contractor is compensated.

APPEARANCES: Louis Rabil, Attorney at Law, Washington, D.C., for Appellant; Alton E. Woods, Department Counsel, Washington, D.C., for the Government.

OPINION BY CHIEF ADMINISTRATIVE JUDGE LYNCH

INTERIOR BOARD OF CONTRACT APPEALS

Appellant, Niko Contracting Co. (Niko) was the successful bidder for a contract to install new roofs at the Harpers Ferry, West Virginia, Civilian Conservation Center. A contract was awarded on June 20, 1986, and a notice to proceed was issued on July 22, 1986, with work to commence by August 4, 1986. Appellant now claims in this appeal that compliance with the specifications required the use of 22,040 screws to secure the plywood underlayerment and that he had bid on the basis of a cushion of an additional 7,440 screws for a total of 29,480. Appellant claims that the Government required him to use 46,000 screws or 16,500 more than anticipated with an acquisition and installation cost totalling $14,373.59. The Government contends that appellant miscalculated the requirement for screws and that the Government did not instruct him to use more screws than required by the specifications. A hearing was held in Arlington, Virginia, on October 19, 1988.

Background

Within 2 weeks of commencing work, appellant requested permission to substitute an Olympic screw for the specified self-drilling screw, because the self-tapping screws received from the supplier were defective. The new screws were approved, but required the drilling of a pilot hole. Appellant contends that from the first day of installing the new plywood decking in the presence of two Government representatives, his workmen were asked to install added fasteners because the original steel deck was very flimsy and the new five-eighths inch plywood was not rigid enough to lie flat on its own. He alleges that the inspectors told them to install as many fasteners as needed to make sure that the new plywood deck was flat and smooth. The plywood tended to curl at the edges and more fasteners would be required to assure a level surface.

The roofs involved in this appeal were sheet metal roofs supported by purloins spaced equi-distant apart. Appellants work involved the placement of a plywood underlayerment fastened to the old metal roof to provide a flat stable surface for a single-ply membrane roofing
material. The specifications required that the plywood be fastened by screws through the sheet metal and the purloins. Two by four-inch sleepers were required to support the seams where plywood sheets met away from a purloin. The specifications called for securing the plywood underlayerment to the existing sheet metal and into the purloin with screws 12-inch O.C.

The Government contends that the claim was untimely presented by letter dated December 15, 1986, which was 4 months after the job had commenced, that added screws were needed because the plywood used was inferior and tended to curl at the edges, that it was necessary to assure the plywood base lay flat in order to secure the membrane manufacturer's 10-year warranty required by the contract, and that appellant grossly underestimated the number of screws required because the purloins were closer together than asserted by appellant.

Discussion and Findings

Respecting timeliness of the claim, the Government claims it was prejudiced by the tardy notice because the contracting officer could not then determine whether the claim had merit. Mr. Wilson was the Government's project supervisor and contracting officer's representative on the project. He testified that he was on the site about one-third of the time (Tr. 156), and that the need for more screws was raised with him on the job by appellant prior to the December letter (Tr. 149). He admitted that some 100 additional screws were requested to be put in to make the edges lie flat (Tr. 151). He testified that he told appellant that "all I wanted you to do is put down enough screws so we can qualify for the ten year warranty, which means we have to hold down the plywood so that the warranty would be valid." He attributed the problem to a poor quality of plywood which curled up more than normal and would require more screws to hold it down (Tr. 150). Additionally, he testified that the engineer writing the technical specifications, Mr. Fillsuth, expressed the opinion that more fasteners should be put down and came to Mr. Wilson about four times urging more fasteners (Tr. 153-56). Mr. Wilson's recollection that only about 100 added screws were ordered is hardly consistent with the concerns he expressed about the quality of the plywood requiring more fasteners and the engineer's urging that more fasteners be put down. He concedes that he had actual notice of appellant's contention that more screws were being used than required by the specifications. He was at the site more time than any other witness and could observe the work as it progressed. As representative of the contracting officer, he could be expected to report on his observations. That he did so is evident in several changes ordered to strengthen and improve the roofs. For example, the sleepers were changed from 2 by 2-inch material to 2 by 4-inch material and added sleepers were ordered by Modification 1 at his recommendation. With Mr. Wilson supervising on the site and knowledgeable that more screws were being used, the Government had actual notice of appellant's claim and the opportunity to challenge its
merit by an on-site inspection. Therefore, we cannot perceive that there was prejudice in receiving the formal claim letter in December 1986.

The Government's contention that the problem of added fasteners were required because of inferior plywood is undermined by the fact that the plywood was specified by the Government as to thickness, and after delivery, received the Government's approval as required by the contract. Originally, the specifications had required plywood of only one-half-inch thickness. This was changed to five-eighths-inch thickness prior to the bids. Either by specifying a thicker plywood, or by rejecting the plywood delivered to the site, the Government had the opportunity to avoid the difficulty of curling plywood which the parties seem to agree was a contributing cause of requiring a greater number of fasteners. Having specified the spacing of the fasteners and approving the plywood to be used, the Government can hardly contend that appellant was responsible for varying the spacing of the fasteners to compensate for the choice of plywood.

Similarly, although it is understandable that a flat base of plywood was essential to assure a valid manufacturer's warranty on the membrane, the Government chose to specify the spacing of the fasteners. By specifying the spacing, the Government determined that this minimum spacing would fulfill the requirements of the contract. Entitled only to fasteners at the specified spacing, the contract cannot be interpreted to require the number of fasteners necessary to make the plywood base lie flat.

The most contested issue in this appeal is whether appellant miscalculated the number of fasteners required to do the job. This issue revolves around the parties differing views on the distance between the purloins. Appellant claims that he measured the distance between the purloins in estimating the job and found them to be 4 to 5 feet apart. The Government contends that the purloins were actually only 2 feet apart and presented a calculation showing that the number of fasteners required by the contract was 51,088 rather than the 29,480 calculated by appellant (Exh. Y). Underpinning the Government's calculation is Exhibit AA, which is page 297 of a reference work entitled "Architectural Graphics Standard." Appellant challenges this exhibit on the grounds that it portrays wood framing with roof supports spaced at 2-foot intervals, whereas steel construction permits roof purloins to be more widely spaced.

It is curious that Mr. Wilson did not recall the spacing of the purloins at the worksite. The difference between 2 and 4 feet is so pronounced that it could hardly go unnoticed. Neither did either party have photographs of the underside of the completed roof to provide the needed proof of the purloin spacing. However, appellant's Exhibits 12 and 13 are photographs of the work in progress on November 17, 1986, and show the plywood sheets placed with the 8-foot dimension placed
across the purloins. Appellant testified respecting these photographs that after placement of the sheets of plywood, a chalkline was snapped along the length of the purloin to mark the location of the purloin in red chalk in order that screws could be properly placed through the plywood and into the purloin (Tr. 171-75). No more than two red chalklines appear on the 8-foot length of any sheet of plywood. While no measurements appear on the photographs to aid in determining the distance between the red lines, it is clear that a greater portion of the 8 feet is uninterrupted by a red line than remains of the sheet on either side of the two red lines. These two photographs, together with the explanation of the reason for placement of the red chalklines, are convincing evidence that the purloins were spaced more than 2 feet apart. Therefore, we find that appellant's calculation of the quantity of screws required to comply with the specified spacing of fasteners was correct. It follows and we find that the additional fasteners required to make the approved plywood underlayerment lay flat were an addition to the contract requirements.

Appellant's quantum claim is based on the material cost of the added screws plus labor, overhead, and profit based on an average of 2 minutes to install 16,500 more screws than required. The labor cost for installing the added screws is $10,544.87. Adding the material cost of $817.65 plus 15-percent G&A and 10-percent profit totals $14,373.59. In accord with the principle that the actual cost of added work attributable to the Government is compensable, we allow the entire amount. The added cost for drilling for the specified number of screws was absorbed by appellant and not included in the claim.

Conclusion

Having found appellant's calculation of the screws required by the contract to be correct and that the additional screws were an addition to the contract requirements in order to make the plywood underlayerment lay flat, we find for appellant in the amount of $14,373.59 plus interest computed in accordance with the requirements of the Contract Disputes Act of 1978.

Russell C. Lynch
Chief Administrative Judge

I concur:

William F. McGraw
Administrative Judge
ALVIN R. PLATZ ET AL.

114 IBLA 8

Appeal from a decision of the Folsom Resource Area Manager, Bureau of Land Management, denying application for motorized access across public land located in the North Fork American River Wild River Corridor. CA CA-20525.

Reversed and remanded.


In denying a right-of-way authorizing motorized access to private property across lands included in a wild and scenic river area, BLM acted contrary to sec. 12(b) of the Wild and Scenic Rivers Act, 16 U.S.C. § 1283(b) (1982), and the implementing regulations at 43 CFR 8351.2-1, since the record established that appellants and their predecessors have historically used motorized vehicles in reaching their property.


OPINION BY ADMINISTRATIVE JUDGE IRWIN

INTERIOR BOARD OF LAND APPEALS

At the direction of the Chief Administrative Judge, exercising his responsibility for the internal management and administration of the Board, 43 CFR 4.2(c), this appeal has been granted expedited consideration because the matter has previously been before the Board.

Appellants, Al Platz and his partners in the Gold Ring Placer Mine Properties partnership, originally appealed the July 21, 1987, decision of the Area Manager, Folsom Resource Area, Bureau of Land Management (BLM), that denied them access by motor vehicle to their property lying within the boundaries of the corridor along the North Fork American River, which is designated as a wild river under the Wild and Scenic Rivers Act (WSRA). See 16 U.S.C. § 1274(a)(21) (1982). BLM's decision denied such access because "motorized land and water vehicles [were] prohibited within the wild river boundary" by the North Fork American River Management and Development Plan (Management Plan). We set that decision aside by order dated June 29, 1988, and remanded the case for readjudication because

[the statement of reasons [submitted by appellants] raises significant questions whether BLM considered the provisions of applicable statutes and regulations, i.e., 16 U.S.C. 1283(b) (1982), 16 U.S.C. 3210(b) (1982), and 43 CFR 8351.2-1(b)(2), in making the decision. We have examined the case record forwarded by BLM and conclude that the record does not reflect that BLM's adjudication of this case was guided by applicable law.
We note that 43 CFR 8351.2-1, which was promulgated after the completion of the Management and Development Plan that BLM found was controlling in this case, provides that the authorized officer may issue orders which close or restrict the use of lands and water surfaces within the boundaries of any component of the National Wild and Scenic River System but that such orders may exempt owners or lessees of property within the boundaries of the designated wild and scenic river area. 43 CFR 8351.2-1(b)(2).

BLM met with appellants in August 1988 and, as agreed, they filed an application for a right-of-way "for motorized vehicle access (trail bikes) on existing trail to private property" the following month.

The Area Manager's March 21, 1989, decision granted "pedestrian and equestrian use of the existing trail * * * across the public land for the reasons stated [in pages 2-4 of the decision] above" and offered appellants a right-of-way grant for 10 years (Decision at 5). The decision recited that the provisions referred to in the Board's June 29, 1988, order had been "specifically considered in this decision-making" and contained brief discussions of the applicability of those provisions.

Appellants filed a notice of appeal from BLM's March 21, 1989, decision on April 21, 1989. On May 15, 1989, they requested an extension of time until July 14, 1989, in which to file a statement of reasons (SOR), which was duly granted. Appellants' SOR was timely filed. BLM's response, filed August 21, 1989, was a one-page declaration of the Area Manager that he had not discussed the case during a November 1988 visit to the Board.

As previously noted, appellants' property is a former placer mining claim, patented in 1879, which they purchased in 1983. It is surrounded by public lands within the boundary of the North Fork American River, which is classified as a wild river under the Wild and Scenic Rivers Act. 16 U.S.C. § 1274(a)(21) (1982); 45 FR 58635 (Sept. 4, 1980); see Attachment 2, January 31, 1989, Land Report. BLM's March 21, 1989, decision incorporated verbatim the analysis contained in its January 31, 1989, Land Report.

In considering "what constitutes appropriate access for the reasonable use and enjoyment of the subject property" under section 1323(b) of the Alaska National Interest Lands Conservation Act (ANILCA), BLM reasoned as follows: (1) access to the property over the existing steep trail has historically been by foot or horse; (2) appellants use the property for recreation, not residence; (3) motorized access would be inconsistent with management of the wild river corridor; and (4) horseback access is adequate for recreational use of the property. 2

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1 Wild river areas are "[t]hose rivers or sections of rivers that are free of impoundments and generally inaccessible except by trail, with watersheds or shorelines essentially primitive and waters unpolluted. These represent vestiges of primitive America." 16 U.S.C. § 1273(b)(1) (1982).
2 In its decision BLM considered it "clear" that it is "obligated to provide access to the Platz property" under sec. 1323(b) of ANILCA, which provides: "Notwithstanding any other provision of law, and subject to such terms and conditions as the Secretary of interior may prescribe, the Secretary shall provide such access to nonfederally owned land surrounded by public lands managed by the Secretary under the Federal Land Policy and Management Act of 1976 (43 U.S.C. 1701-82) as the Secretary deems adequate to secure to the owner the reasonable use and enjoyment thereof: Provided, That such owner comply with rules and regulations applicable to access across public lands." 16 U.S.C. § 3210(b) (1982).
BLM's January 31, 1989, Land Report contains the following passages, quoted in the decision, that indicate the information upon which it based its decision:

The property is located in the bottom of the North Fork American River Canyon near Green Valley. To the south of the canyon, where access to Mr. Platz property is possible, the elevation drops 2,000 feet in about 12 miles. This area is remote and undeveloped; no roads have been constructed into this portion of the canyon. Access to the property has always been by the Green Valley Trail. The Green Valley Trail has, for over one hundred years, provided access along a narrow, steep and winding trail to the river.

The Green Valley Trail never evolved into a road simply because the terrain precludes a road.

Since historic access to the Platz property was by trail and because even miners found it more reasonable to skid equipment down into the canyon than to try to build a road, access must be confined to forms of access commensurate with the capability of the Green Valley Trail. Previous access has apparently been adequate for construction and maintenance of a cabin and for conducting mining operations. In fact, the cabin on the Platz property has been used and enjoyed for decades by pedestrian and equestrian access. As far as is known, equestrian travel was the preferred method of access.

BLM's decision states that it "specifically considered" section 12(b) of the WSRA, 16 U.S.C. § 1283(b) (1982), and 43 CFR 8351.2-1. BLM concluded that its decision was consistent with section 12(b) of the WSRA, which provides that "[n]othing in this section shall be construed to abrogate any existing rights, privileges, or contracts affecting Federal lands held by any private party without the consent of said party." BLM reasoned as follows:

Non-motorized access has been the principal access means historically, at the time of passage of the Act, and at the date of purchase of the private parcel by the grantee.

According to BLM, its decision grants appellants "a mode of access which will meet [their] needs for transportation and packing in supplies, a mode commensurate with the reasonable use and enjoyment of a remote recreation site" (Decision at 2).

Appellants assert that sec. 1323(b) of ANILCA applies nationwide, citing the Board's decision in Utah Wilderness Ass'n, 80 IBLA 64, 91 I.D. 165 (1984), involving BLM's dismissal of a protest filed by Utah Wilderness Ass'n (Utah Wilderness) against the issuance of a road right-of-way to Shell Oil Co. (Shell). In affirming BLM's decision, the Board concluded that "Shell has a right of access to the state land in section 36 by virtue of section 1323(b) of ANILCA." 80 IBLA at 77, 91 I.D. at 173. The Board based its decision in part upon Montana Wilderness Ass'n v. U.S. Forest Service, 655 F.2d 951 (9th Cir. 1981), in which the U.S. Court of Appeals for the Ninth Circuit held that sec. 1323(a) of ANILCA applies nationwide. 655 F.2d at 957.

The right-of-way in question in Utah Wilderness Ass'n expired by its own terms on the same day the Board issued its decision. Utah Wilderness filed an action in the U.S. District Court for the District of Utah, asking that the matter be remanded to the Board with instructions to reverse the BLM decision, or to require BLM to analyze the proposed right-of-way under the standards of sec. 603(c) of FLPMA, 43 U.S.C. § 1732(c) (1982), rather than under sec. 1323(b) of ANILCA. Shell moved to dismiss Utah Wilderness' claims as moot. The District Court concluded that "a thorough review of the record and careful consideration, the court concludes that proper resolution of the plaintiff's claims calls for dismissal of this action as moot but with an order directing the IBIA to vacate its opinion upholding the grant of the right-of-way." Utah Wilderness Ass'n v. Clark, No. C84-0472J, memo. op. at 6 (D. Utah, Dec. 16, 1985).

Consequently, this Board issued an order on Feb. 26, 1986, vacating its decision in Utah Wilderness Ass'n, supra. Because the District Court did not address whether the Board was correct in applying sec. 1323(b) of ANILCA to public lands situated in Utah, but rather ordered the Board to vacate its decision to that effect, there is no Board precedent on the scope of sec. 1323(b). Because we decide in this case that appellants' right of access is secured by sec. 12(b) of the WSRA, we need not address whether such access would be secured by sec. 1323(b) of ANILCA as an independent matter.
Because no *legal* access to the subject private parcel across public lands has ever been established under the Federal Land Policy and Management Act (FLPMA), pursuant to 43 CFR 2800, no specific rights of access, other than "casual use," have existed. Therefore, no existing rights, privileges or contracts, affecting public lands were abrogated since none existed. [Italics in original.]

(Decision at 5).

In addition, BLM stated that appellants were not entitled to an exemption under 43 CFR 8351.2-1 from the prohibition against motorized vehicle use within the boundaries of the North Fork American River, as embodied in the Management Plan. In BLM's opinion,

[b]ecause motorized vehicle use within the Wild River boundary is specifically prohibited in the management and development plan adopted to meet the intent of Congress for Wild Rivers, and a lesser degree of access than motorized will meet the grantee's needs, an exemption from the motorized use restriction is not indicated.

(Decision at 5).

In their SOR, appellants emphasize that "BLM now apparently acknowledges that pedestrian access is inadequate to ensure 'the reasonable use and enjoyment' of the property" (SOR at 11). In appellants' view, pedestrian access would not enable them to "carry supplies or materials to make the type of improvements to the cabins and associated facilities that BLM has authorized. * * * Nor can the owners go to and from the cabin rapidly in the event of a medical or other emergency." *Id.* at 11-12. Thus, argue appellants, "[t]he remaining question is whether the BLM Decision or Record can support a conclusion of access via mules or horses is adequate to ensure the reasonable use of the property." *Id.*

According to appellants, answering that question must take into account the fact that appellants "have the right to use trail bikes on the Green Valley Trail for the first two miles of the trail. The Forest Service has recently reissued a trail use permit authorizing that use." *Id.*; SOR, Exh. L. The portion of the trail at issue is the one-half mile from the river corridor boundary to appellants' cabin. Appellants place their right-of-way application into the following perspective:

The owners do not wish to install a road or to widen the trail by one inch. They do not ask that the trail be opened for recreational vehicle use. Nor do the considerations that might apply to recreational use limit BLM's duty to provide access for private property owners. The owners' use of the last one-half mile segment of the trail will be minimal. They estimate that the total number of round-trips on this section will be approximately one each per month (Declaration of Platz, ¶ 15), which amounts to about eight hours per year of trail use. [Italics in original; footnote omitted.]

(SOR at 12-13).

A BLM decision to grant or deny an application for a right-of-way is generally an exercise of the discretion granted to the Secretary under section 501 of the Federal Land Policy and Management Act of 1976 (FLPMA), 43 U.S.C. § 1761 (1982). As an appeals board acting on behalf of the Secretary, we have "plenary authority to review de novo all official actions and to decide appeals from such actions on the basis
of a preponderance of the evidence in cases involving substantive rights, or on the basis of public policy or public interest in cases involving the exercise of discretion" unless "the scope of appellate review by or on behalf of the Secretary [has been diminished or constrained] by the Secretary himself in a duly promulgated regulation, or by the Congress through enacted law." United States Fish & Wildlife Service, 72 IBLA 218, 220-21 (1983). When we review a BLM decision granting or denying an application for a right-of-way, we look to see whether the record shows the decision to be a reasoned analysis of the factors involved, made in due regard for the public interest, and no sufficient reason is shown to disturb the decision. Dwane Thompson, 88 IBLA 31, 35 (1985); Nelbro Packing Co., 63 IBLA 176, 185 (1982); Stanley S. Leach, 35 IBLA 53, 55 (1978); Jack M. Vaughan, 25 BLA 303, 304 (1976). In this case we conclude that a preponderance of the evidence establishes that a complete ban on motorized access deprived appellants of their existing rights, contrary to section 12(b) of the WSRA.

[1] Section 10(a) of the WSRA, 16 U.S.C. § 1281(a) (1982), provides, with reference to the administration of the “national wild and scenic rivers system,” that “[m]anagement plans for any such component may establish varying degrees of intensity for its protection and development, based on the special attributes of the area.” In addition, section 12(a) provides:

The Secretary of the Interior, the Secretary of Agriculture, and the head of any other Federal department or agency having jurisdiction over any lands which include, border upon, or are adjacent to, any river included within the National Wild and Scenic Rivers System * * * shall take such action respecting management policies, regulations, contracts, plans, affecting such lands, following November 10, 1978, as may be necessary to protect such rivers in accordance with the purposes of this chapter.

However, as noted, section 12(b) of the WSRA, 16 U.S.C. § 1283(b) (1982), provides that “[n]othing in this section shall be construed to abrogate any existing rights, privileges, or contracts affecting Federal lands held by any private party without the consent of said party.” (Italics added.)

We find that BLM’s decision denying appellants’ access to their private property by trail bike in this case amounts to an abrogation of “existing rights” within the meaning of section 12(b) of the WSRA. Platz and his wife purchased the property, which was patented under the mining laws in 1879, from a Mr. Goddard in 1983, and thereafter conveyed it to a partnership consisting of themselves and three other couples (SOR (Platz Declaration at 1-2)). As noted by BLM, the Green Valley Trail has provided access to the subject property for over 100 years (Decision at 3).

BLM states that "[a]s far as is known, equestrian travel was the preferred method of access" to appellants’ property, and that its decision "does not diminish any rights previously granted since none
exists” (Decision at 4-5). In the Land Report upon which BLM based its decision, BLM states that “[h]istorically, access to the private parcel has been non-motorized, using the existing trail” (Land Report at 2).

BLM’s assessment of the historical means of access to the Platz property may be accurate when viewed as a century-long matter. However, our concern under section 12(b) of the WSRA relates to appellants’ “existing rights.” Platz asserts that he has “first-hand knowledge of the use of the property and the access route to the property over the last thirty years, as does each of the partners, as they visited the property regularly in that period prior to having bought it” (SOR (Declaration of Platz at 2)). He states that “[d]uring the time [he] visited the property when Mr. Goddard was the owner, [he] routinely used a motorbike to come and go,” and that “[t]here were never any complaints from either the Forest Service or BLM.” Id. at 4. He states that Goddard’s predecessor, who owned the property for at least 15 years, “used a modified motorcycle, or ‘tote-goat.’” Id. Further, Milan Jones, who was lessee of the property when Platz bought it from Goddard, “used a three-wheel trail bike for access to the property.” Id. at 5; SOR, Exh. R (Letter from Milan Jones dated May 9, 1989). The case file contains other letters supporting the claim that various types of motorized vehicles have been used to gain access to the Platz property since at least 1960 (SOR, Exhs. S and T), and that the Green River Trail is too steep in places for equestrian access (SOR, Exh. U).

The record does not support BLM’s conclusion that equestrian access to the Platz property will necessarily be less damaging to the Green River Trail than access by motorized vehicle. In the environmental assessment (EA) prepared in conjunction with the Land Report, BLM states that “[b]ecause portions of the subject trail consists [sic] of excessively steep pitches (25% - 30%), an attempt to maintain traction on these sections would result in severe rutting of the trail surface” (EA at 8). BLM indicates that “[t]he construction of water bars at proper intervals per BLM standards would aid in removing runoff water and would help provide erosion control in the steep rutted sections of the trail.” Id. at 9. However, with regard to equestrian access, BLM states that “[s]ome damage to the trail surface would result from saddle or pack horse use, especially during wet soil conditions.” Id. at 11. Again, BLM would condition the right-of-way grant for equestrian access upon the “installation of water bars at proper intervals, per BLM standards.” Id. at 11-12.

Platz counters BLM’s conclusion that motorized vehicles will cause more damage to the terrain than horses, stating that “because the trail is only two-feet wide, horses do damage to surrounding vegetation, and cause erosion to a greater extent than the trail bikes with low pressure, wide wheels and low gearing that we use on the trail” (SOR (Platz Declaration at 4)).

Assuming, arguendo, that BLM is correct in its conclusion that trail bike use of the Green River Trail will cause more damage than
equestrian access, we remain unpersuaded that such additional damage, which in any event would not appear to be significantly greater, justifies denying appellants the mode of access to their property which has been, according to the record, the primary mode of access for nearly the last three decades. Relevant to our conclusion on this issue is the EA prepared by the Forest Service (FS) subsequent to the joint FS/BLM decision dated January 11, 1984, wherein FS and BLM determined to allow Platz to use motorized transportation from the trailhead to the wild river boundary, but not along the remaining half mile to the Platz property. In this EA, FS considered three alternatives for use of the portion of the Green River Trail under its jurisdiction: (1) construct and reconstruct a standard hiking trail with an 18- to 24-inch trail tread for the entire trail length, allowing Platz to operate a trail bike thereon; (2) construct the trail with a trail tread width of 48 inches to the wild river boundary, again allowing Platz motorized access; and (3) no action. In adopting the second alternative, FS stated:

While foot or horse travel is one form of access, it is difficult for [Platz] to use and enjoy his property to the extent possible without a more sophisticated form of travel. Mr. Platz has been allowed to operate a trail bike on the trail for two years and has assisted with trail maintenance; therefore, off-road vehicle use will not be a new development. A 48" trail would not detract from wilderness character.

(ES EA at 3). On June 29, 1989, FS issued a "use permit" allowing appellants to use motorcycles on the Green Valley Trail from the trailhead up to the wild river boundary, subject to conditions relating to maintenance and repairs to the trail. 9 We think the FS approach will sufficiently protect the values along the remaining half mile from the wild river boundary to the Platz property.

Our review suggests that BLM's reliance upon the Management Plan is overstated. In its decision, BLM stated that "[i]n this case, the management plan prohibits motorized equipment. The purpose of this prohibition is to preserve the sense of remoteness and solitude consistent with a wild river" (Decision at 4). We find that the Management Plan does not expressly or necessarily, in all cases, prohibit the use of motorized equipment in the North Fork American River corridor. BLM's assertion that all motorized access has been prohibited within the management boundaries is explicitly contradicted by the Land Report. The Land Report states:

If motorized use within the Wild River Corridor were authorized by this action, the precedent would be set for owners of all private inholdings within a Wild River Corridor to acquire motorized access. To date, only those motorized uses that existed at the time of Wild River designation have been "grandfathered in." [Italics added.]

9 We do note that in a letter dated Feb. 9, 1989, the Forest Supervisor informed the BLM Area Manager that: "Based on the discussion of facts contained in your documents, I concur with and fully support, your proposed decision to not allow motorized access within the Wild North Fork American River corridor."
(Land Report at 16). To the extent, therefore, that we have concluded that trail bike access to the Platz property was a use "existing" at the time of wild river designation, the theoretical basis for BLM's decision is severely eroded. Even assuming that such use was prohibited, we interpret the Management Plan as reflecting the concern in sec. 12(b) of the WSRA that "existing rights, privileges or contracts" of private parties not be abrogated. In this case, it would be improper to invoke the prohibition mentioned in the Management Plan, since, in our view, that prohibition would constitute an abrogation of appellants' "existing rights," i.e., the use of motorized access to their property.

The Management Plan (SOR, Exh. F) contains a section entitled "Management Guidelines" which addresses the subject of transportation in the North Fork American River corridor:

Transportation. Motorized land and water vehicles and suction dredges will be prohibited within the wild river boundary. Trails in close proximity (parallel) to the river will not be expanded without determination of the need for additional access. Trail bridges will be allowed across the river where they are needed and are comparable with the natural character of the area.

Access to private lands and valid mining claims existing prior to January 1975 shall be controlled to cause the least adverse effect on the wild river environment. [Italics added.]

(Management Plan at 9-10).

We find merit in appellants' view that "[i]t is clear that landowners entitled to access are on a different footing than others who wish to enter the corridor solely on the basis of their status as members of the public" (SOR at 17).4 This "different footing," as appellants point out, is reflected in the regulations at 43 CFR 8351.2-1, which implement the WSRA. Those regulations provide, in pertinent part:

(a) The authorized officer may issue written orders which close or restrict the use of the lands and water surface administered by the Bureau of Land Management within the boundary of any component of the National Wild and Scenic River System when necessary to carry out the intent of the Wild and Scenic Rivers Act. Each order shall:

(1) Describe the lands, road, trail, or waterway to which the order applies;
(2) Specify the time during which the closure or restriction applies;
(3) State each prohibition which is applied; and
(4) Be posted in accordance with paragraph (d) of this section.

(b) A written order may exempt any of the following persons from any of the prohibitions contained in the order:

(1) Persons with written permission authorizing the otherwise prohibited act or omission. The authorized officer may include in any written permission such conditions considered necessary for the protection of a person, or the lands or water surface and resources or improvements located thereon.

(2) Owners or lessees of property within the boundaries of the designated wild and scenic river area. [Italics added.]

4 The concern with the rights of private landowners is reflected in other provisions of the Management Plan. For example, although "[t]he management of private land within the River Management Zone will be compatible with wild classification," the Management Plan at pages 4-5 further provides: "The cost to landowners to meet this need was recognized in the Wild and Scenic Rivers Act and provisions made for monetary compensation through purchase of land in fee or of scenic easements. * * * The landowner will be paid a fee to compensate him for property rights granted to the government. Reimbursement will be based on the present value of the property--determined by a professional real estate appraiser--and the value of property rights granted to the government." [Italics in original].

Further, the initial paragraph of the Management Guidelines states that the "guidelines which involve restrictions of private land will be in effect only when the right to make these restrictions has been purchased." Id. at 5.
As with the Management Plan, the provisions of this regulation do not expressly prohibit the use of motorized vehicles in a wild and scenic rivers corridor. We agree that such use may be prohibited, as a general matter, provided that BLM complies with the procedures set forth in the regulations. However, we think the regulations contain procedures designed to protect the "existing rights" of private landowners who will be affected by the prohibition. Specifically, with regard to private property access, we note that in the preamble to the final rule found at 43 CFR 8351.2-1, BLM responded to the comment that it "cannot restrict uses of or close private lands, water inholdings or valid rights of access in wild and scenic areas," by saying that it "is not attempting to restrict uses of or close private lands or rights," and that "[s]ection 8351.2-1(a) has been rewritten to make this clear." 45 FR 51740 (Aug. 4, 1980).

Even if we were to agree that BLM has the authority to proscribe, in all cases, motorized access to private property in the North Fork American River corridor, we would have to conclude that under the regulations it has failed to accomplish that objective. Subsection (a) of 43 CFR 8351.2-1 provides that BLM "may issue written orders which close or restrict the use of the lands and water surfaces administered" by BLM. We interpret this provision to mean that if BLM wishes to close or restrict the use of certain lands or water surfaces, it must issue such a written order. Under 43 CFR 8351.2-1(a)(1)-(3), this order must include a description of the affected lands, road, trail, or waterway; state the time during which the closure or restriction applies; and state the prohibition which applies.

As noted, the regulations do not expressly preclude the use of motorized vehicles in a wild and scenic rivers corridor. Subsection (e) of 43 CFR 8351.2-1 provides:

When provided by a written order, the following are prohibited:
(1) Going onto or being upon land or water surface;
(2) Camping;
(3) Hiking;
(4) Building, maintaining, attending or using a fire;
(5) Improper disposal of garbage, trash or human waste;
(6) Disorderly conduct; and
(7) Other acts that the authorized officer determines to be detrimental to the public lands or other values of a wild and scenic river area. [Italics added.]

We interpret this regulation to mean that if BLM wishes to prohibit the use of motorized vehicles in the North Fork American River corridor, it may do so on the basis that it constitutes an "other act" which is detrimental to the area.

Assuming that BLM has issued a written order specifically prohibiting the use of a motorized vehicle in a wild and scenic river area, subsection (b) of 43 CFR 8351.2-1 provides that certain persons may be exempted from the prohibition by written order, among them "[p]ersons with written permission authorizing the otherwise
prohibited act or omission,” and “[o]wners or lessees of property within the boundaries of the designated wild and scenic river area.” This provision answers BLM’s concern that granting to appellants the right of access to their property by means of motorized vehicle will open up the area to motorized vehicle use by the public at large. See Land Report at 16. Assuming BLM has issued a written order specifying a prohibition and has posted it in accordance with 43 CFR 8351.2-1, a person must possess an order of exemption from that prohibition, or risk the penalties described at subsection (f) of the regulation.

We note that there is no indication in the case file that BLM has issued a written order or orders prohibiting the use of motorized vehicles in the North Fork American River corridor. BLM perhaps assumed that the adoption and publication of the Management Plan in the Federal Register complied with the written order requirement of 43 CFR 8351.2-1. We reject that notion. Subsection (a)(4) requires that a written order be posted in accordance with 43 CFR 8351.2-1(d), which provides:

Posting is accomplished by:

(1) Placing a copy of an order in each local office having jurisdiction over the lands affected by the order; and

(2) Displaying each order near and/or within the affected wild and scenic river area in such locations and manner as to reasonably bring the prohibitions contained in the order to the attention of the public.

A basic reason why BLM must adhere to this “posting” requirement relates to the penalties BLM may impose when a person violates a prohibition established in the written order. Subsection (f) of 43 CFR 8351.2-1 provides that “[a]ny person convicted of violating any prohibition established in accordance with this section shall be punished by a fine of not to exceed $500 or by imprisonment for a period not to exceed 6 months, or both, and shall be adjudged to pay all costs of the proceedings.” Publication of the Management Plan in the Federal Register, even if it contained a binding prohibition against all use of motorized vehicles in the North Fork American River area, would not accomplish “posting” and its objectives as defined in the regulations.

In light of BLM’s intention to prohibit motorized vehicle use in the North Fork American River corridor, it should issue a written order to that effect which complies with the content and posting requirements of the regulation, and upon issuing appellants’ right-of-way for trail bike access to their property, exempt them by written permission from the prohibition.5

5 We do not imply that appellants’ right-of-way to their property is unconditional. 43 CFR 8351.2-1(b)(1) authorizes the inclusion in any written permission of “such conditions considered necessary for the protection of a person, or the lands or water surface and resources or improvements thereon.” Further, a right-of-way is required under sec. 505 of FLPMA, 43 U.S.C. § 1765 (1982), to contain terms and conditions which will, inter alia, “minimize damage to scenic and esthetic values and fish and wildlife habitat and otherwise protect the environment.” The implementing regulations provide that BLM shall impose stipulations which shall include, inter alia, “[r]equirements for restoration, revegetation and curtailment of erosion of the surface of the land, or any other rehabilitation measure determined necessary,” and “[r]equirements designed to control or prevent damage to scenic, esthetic, cultural and environmental values (including damage to fish and wildlife habitat), damage to Federal property and hazards to public health and
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 reversed and remanded for action consistent with this opinion.

I CONCUR:

JAMES L. BURSKI
Administrative Judge

WILL A. IRWIN
Administrative Judge
Appeals from decisions of the Montana State Office, Bureau of Land Management, cancelling overriding royalty interests and requiring repayment of overriding royalties. M-32324(ND) et al.

Decisions reversed; requests for attorneys’ fees denied.

1. Administrative Procedure: Generally--Appeals: Generally--Rules of Practice: Appeals: Failure to Appeal
Where a decision by BLM cancelling an overriding royalty interest and requiring reimbursement of moneys previously received from that interest is delivered to the last address of record of the holder of the interest, and where no appeal is filed by him, BLM’s decision cancelling his interest becomes final for him.

Where the record fails to establish that a copy of a BLM decision cancelling an overriding royalty interest and requiring reimbursement of moneys previously received from that interest was received by the interest holder, by a qualified representative of her estate, or by her heirs, a failure to appeal does not render BLM’s decision final.

3. Oil and Gas Leases: Applications: Sole Party in Interest
Where the record establishes that a firm filed DECs prepared and signed by its employees, and that the employee/applicants were required by verbal agreement, as a condition of their employment, to sell their leases to parties as directed by the firm, the firm had a claim to an advantage or benefit from a lease within the meaning of 43 CFR 3100.0-5 (1978). Thus, the firm held an “interest” in its employees’ DECs, and, where that interest was not disclosed at the time the DECs were filed as required by 43 CFR 3102.7 (1978), they should have been rejected.

4. Oil and Gas Leases: Applications: Sole Party in Interest
Where the record fails to show that there was any enforceable agreement between a lease filing firm and nonemployees under which the nonemployees were bound to transfer any leases they acquired as directed by the firm and shows instead that the method for acquiring leases developed by the firm rested solely on the fact that the nonemployees enlisted to sign DECs were friends and relatives of the employees or principals of the firm and, thus, could be expected to sell any subsequently acquired lease to the firm by ties of loyalty, the firm held no “interest” in the DECs it filed on behalf of the nonemployees, since it had no means to enforce such expectation. Such claims of loyalty amounted merely to a hope or expectancy that a successful applicant would sell the lease to the firm.

5. Oil and Gas Leases: Cancellation--Oil and Gas Leases: Overriding Royalties
Under 43 CFR 3108.3 (1987), BLM lacks the power to administratively cancel any oil and gas lease or interest therein that is in production.

Cancellation of overriding royalty interests in an oil and gas lease and the requirement to repay overriding royalties does not constitute an adversary adjudication under sec.
DECISIONS OF THE DEPARTMENT OF THE INTERIOR


OPINION BY ADMINISTRATIVE JUDGE HUGHES

INTERIOR BOARD OF LAND APPEALS

Jase O. Norsworthy and others (appellants) have appealed from decisions of the Acting State Director, Montana State Office, Bureau of Land Management (BLM), dated September 11, and October 20, 1987, cancelling their overriding royalty interests in eight noncompetitive oil and gas leases and requiring them to repay any overriding royalties already received by them in connection with those interests.

BACKGROUND

The eight leases involved here arose from the filing of simultaneous oil and gas lease drawing entry cards (DECs) for eight parcels by various individuals between August 19, 1975, and December 20, 1977, in simultaneous noncompetitive oil and gas lease drawings conducted by BLM. None of the cards disclosed the existence of other parties in interest, but each instead represented that the applicant was the sole party in interest. Eight leases were issued, effective between November 1, 1975, and March 1, 1978, to the applicants after submission by them of acceptable oil and gas lease offers.\footnote{The winning DECs were filed by: Menno L. Bargen (M-32324 (ND)), June A. Larsen (M-32753 (ND) Acq.), Melvin P. Hoiness (M-32760 (ND) Acq.), June M. Heller (M-34187 (ND) Acq.), Dorothy Van Wagoner (Lenehan) (M-34446 (ND)), Deborah C. Reger (M-34449 (ND) Acq.), James R. Reger (M-37404 (SD)), and Karen A. Rintoul (M-39449). Since the simultaneous oil and gas lease drawings involved herein, that system for issuing Federal oil and gas leases has been abolished as a result of passage by Congress of sec. 5102 of the Federal Onshore Oil and Gas Leasing Reform Act of 1987 (Reform Act), P.L. No. 100-203, 101 Stat. 1310-256 (1987).}
These leases were then assigned from the original lessees either separately to the Patrick Petroleum Corp. of Michigan (PPCM) or, in most cases, jointly to PPCM and the Williams Exploration Co. (WEC). As part of these first assignments, the original eight lessees each retained a 1-percent overriding royalty interest in any production from the lease. Subsequently, overriding royalty interests in these eight leases were assigned back from PPCM and WEC to Jase O. Norsworthy, James W. Reger, Langdon G. Williams, Vincent T. Larsen, or Dennis C. Rehrig (Norsworthy et al.). Norsworthy et al. were closely associated with the NRG Co. (NRG), which was the entity that evidently filed the eight DECs involved here, as well as hundreds of others, in BLM's simultaneous noncompetitive oil and gas lease drawing system between 1975 and 1980. Significantly, the eight applicants in these cases were all related in some way to NRG, either through employment or as relatives or friends of NRG principals, employees, or associates. BLM ruled in its September 1987 decision that NRG had engaged in "multi-filing practices and sole party in interest violations" from January 1975 through February 1980. Although BLM left the leases intact, it cancelled the overriding royalty interests in these leases held by the eight original lessees and by Norsworthy et al., except those held by Larsen. BLM explained that there was "insufficient evidence to allege [Larsen's] involvement * * * in fraudulent activities." Some of the overriding royalty interests originally held by Norsworthy et al. had been reconveyed to others. BLM's October 1987 decision cancelled these interests.

The eight oil and gas leases involved herein have at all relevant times been considered to be producing leases either due to production from wells drilled in the leased land or as a result of production attributable to the leases under communitization agreements.

The factual basis for BLM's decisions was provided by a criminal investigation, begun in January 1980 in conjunction with the Justice Department, into the activities of PPCM, WEC, and NRG with respect to the acquisition of interests in 63 noncompetitive oil and gas leases (including the eight leases involved herein) issued by BLM under the simultaneous oil and gas leasing system between January 1975 and February 1980. As a result of that investigation, it was concluded that PPCM and NRG had manipulated the system in order to increase their chances of acquiring oil and gas leases or interests therein, thus

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2 Norsworthy, Reger, Williams, and Larsen received interests in all eight leases. Rehrig received interests in only three.

3 There is some doubt as to whether NRG completed the DECs for all of these eight applicants. For example, the DEC of Karen A. Rintoul (M-39449) appears to have been completely filled out, including parcel number, in her handwriting. In view of our holdings herein, it is unnecessary to resolve this question.

4 BLM evidently left the leases intact under the terms of a settlement agreement executed in June 1985 between the United States and PPCM and WEC; discussed below. The cancelled overriding royalty interests in each lease are set out in Appendix A.
violating the Departmental regulations prohibiting multiple filings and requiring disclosure of other parties in interest.

The results of the investigation were submitted to a Federal grand jury, which returned criminal indictments against NRG.6 A criminal information was filed against NRG in January 1983, and the criminal proceedings were docketed as United States v. NRG Co., Crim. No. CR-83-1-GF (D. Mont.). In Information, Crim. No. CR-83-1-GF, NRG was accused as follows:

[Between March and September 1978, NRG] knowingly and willfully and unlawfully did make and cause to be made false, fictitious and fraudulent statements and representations to the United States Department of the Interior in a material matter; that is, [NRG] prepared, caused to be prepared, filed and caused to be filed Drawing Entry Cards in the names of offerors who were NRG COMPANY employees, which Drawing Entry Cards stated that said offeror was the sole party in interest, which statement [NRG] well knew was false, in that said offeror was not the sole party in interest but that defendant NRG COMPANY possessed an interest in the lease if the offeror's card was selected as the winner. [Italics supplied.]

Significantly, the information cited NRG only for criminal acts in connection with the filing of 12 DECs in the names of offerors who were NRG employees. None of these filings is involved in the present case.

Contemporaneous with the filing of the criminal information, NRG and the U.S. Attorney gave notice to the court of a plea agreement. Under this agreement, NRG agreed only to “plead guilty to each of twelve counts of violation of 18 U.S.C. § 1001 as charged in an Information, Crim. No. CR-83-1-GF.” NRG was eventually fined by the district court in accordance with the plea agreement. In this plea agreement, the United States agreed to bring no further criminal charges related to NRG’s participation in the simultaneous oil and gas leasing system during the years 1975 to 1980. However, the plea agreement provided that it would not prevent, prejudice, or preclude the right of the United States to pursue civil remedies against NRG or its officers or employees thereof, nor prevent, prejudice, or preclude the right of the Department of the Interior and/or BLM to pursue administrative remedies against NRG or its officers or employees.

Filed along with the criminal information and plea agreement was an Offer of Proof setting out the factual background of the criminal action. As BLM relies on this offer of proof as the basis for the decisions under appeal, it is appropriate to set it out in full:

On December 30, 1974, [PPCM] entered into a joint venture agreement with [WEC], providing for the exploration and acquisition of lands in an area of Montana, North Dakota and South Dakota known generally as the Williston Basin. Under the joint venture agreement [PPCM] and [WEC] shared equally the costs associated with the exploration, acquisition and development of property in the Williston Basin that was thought to have potential oil and gas deposits.

Commencing in January 1975, [NRG] was engaged to acquire property in the Williston Basin on behalf of the joint venture. The costs associated with this land acquisition program were borne equally by [PPCM] and [WEC]. Much of the property acquired by the

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6 PPCM was also indicted for similar infractions.
April 17, 1990

Joint venture consisted of mineral rights purchased from private landowners; in addition, considerable acreage was obtained in the Federal Simultaneous Oil and Gas Leasing Program.

From May 1975 to 1979, [PPCM] detailed an employee to Billings, Montana to monitor the joint venture land acquisition program. The [PPCM] employee used an office in the [NRG] offices and was in daily contact with the NRG principals and employees.

The method employed by the [NRG] and [PPCM] in an effort to acquire leases in the Federal Simultaneous Program operated as follows:

[PPCM and WEC] would examine the listing of all federal lands in Montana, South Dakota and North Dakota to be offered for lease in the monthly federal lottery and would notify NRG of the parcels of interest. The NRG office manager would coordinate the filing of drawing entry cards on parcels the joint venture had determined to try to acquire. The office manager arranged to have NRG employees – clerical and professional – sign cards in their own names as offeror, and return the cards [to] him. He then inserted the appropriate parcel numbers and date, and filed the cards with the Billings office of the [BLM]. Employees were told that NRG was affording them the opportunity to file lottery cards. The NRG office manager advised the employees that the payment of the ten dollar filing fee per card, and the selection of parcels, would be taken care of by NRG. Employees were told to fill in only their name, address, social security number, and sign the card. Employees were told that if a card bearing their name was drawn as the winner in a monthly lottery, NRG would pay the yearly rental payment. Employees were told that NRG would purchase a winning lease from them for 25 cents an acre (later raised to 50 cents, then a dollar an acre), together with a 1% overriding royalty on any oil or gas production. Spouses of NRG employees also signed cards on the same terms. Numerous blank cards – sometimes hundreds at a time – were provided to NRG employees to be signed. [PPCM’s] employee in Billings also signed cards, as did his wife. The NRG principals, Jase O. Norsworthy and James W. Reger, also signed cards, along with their spouses and children. Similarly, their in-laws, relatives, neighbors, business acquaintances, and friends also signed cards. NRG’s filing program was explained to these individuals substantially as it was to the NRG employees. NRG paid all filing fees, as well as rental payments on winning leases. NRG was reimbursed by the [PPCM-WEC] joint venture.

In similar fashion, friends, employees and business associates of U. E. Patrick, President of [PPCM], signed cards. The signed cards were transmitted to NRG at Billings, Montana, for designation of parcel numbers, payment of filing fees, and filing.

In this manner, NRG was able to obtain thousands of cards signed in blank by dozens of individuals. These signed cards were kept in a filing cabinet in the NRG office. When needed for filing, the office manager would select these presigned cards, affix the appropriate parcel number, date the card, and file in the monthly lottery. Depending on the desirability of a particular parcel, up to 100 different cards might be filed on a parcel; only one card signed by any given individual was filed for any one parcel. In some months, dozens of different parcels were filed on by NRG using this system.

Each entry card had to be accompanied by a ten dollar filing fee. NRG obtained from First Bank Billings a cashier’s check, made payable to BLM, for the amount of the filing fees for a particular filer, listing the filer as remitter. Thus, if NRG used cards signed by an employee to file on fifty different parcels in a monthly drawing, a cashier’s check in the amount of $500 would be obtained, listing the employee as remitter. On some parcels, individuals filing on behalf of NRG represented in excess of 70% of all cards entered on that parcel. None of the cards ever contained any entry in the blank requesting the identity of any other party having an interest in the offer.

NRG, [PPCM, and WEC] initiated this filing program immediately after commencement of the [PPCM-WEC] joint venture in January, 1975. It continued up until February 1980, at which time BLM abruptly suspended the lottery program. Sixty-three leases were initially acquired by NRG in this fashion, and were subsequently assigned to [WEC and PPCM or PPCM].
In spite of this effort, NRG was not successful in acquiring all the parcels in the Williston Basin that were sought in the federal lottery. In some instances, NRG was authorized by [PPCM] and [WEC] to approach the winner of certain parcels with an offer up to 25 dollars an acre, together with a 3% overriding royalty, in an effort to acquire the lease.

The cost to acquire Williston Basin acreage won by individuals filing in the federal lottery for the period January 1975 through September 1979 averaged $4.96 per acre. The cost to acquire Williston Basin acreage that had to be purchased from other parties was considerably higher. For example, as of November, 1978, the cost to [PPCM-WEC] for acquiring leases through the federal filing program averaged $4.63 per acre, while acreage that had to be purchased averaged $13.10 per acre.

Almost without exception, in the five years that the above-described federal filing plan was in operation, every person filing through NRG sold leases they won to NRG, with subsequent partial assignments made to [PPCM and WEC]. Only one NRG employee, Leila Heidema, chose to sell the lease to another oil company. She received $12.50 per acre and a 5% overriding royalty. She was confronted by an NRG principal and the office manager, both of whom told her that she had "betrayed" them. Her office keys were taken from her by the office manager who told her that "we can no longer trust you." She was fired several months later. Following this incident most employees of NRG were not given cards to sign for approximately a year thereafter. When employees were subsequently given cards to sign, they were reminded of Leila Heidema.

The offer of proof ended by listing the 63 parcels acquired by NRG and PPCM pursuant to this filing program, including the eight parcels at issue here.

The offer of proof thus established that applicants to whom a lease was awarded were not required by written agreement to transfer their leases as directed by NRG or to reimburse it for its efforts in preparing and filing their DECs.6

On June 14, 1985, PPCM, WEC, and the United States entered into a settlement agreement in order to resolve civil claims of the United States arising from alleged violations of Departmental regulations governing the simultaneous oil and gas leasing system, which violations resulted in the acquisition of noncompetitive oil and gas leases by PPCM and WEC. Under that agreement, PPCM and WEC, without admitting any wrongdoing, agreed to relinquish to the United States any and all interests held either separately or jointly by them in 41 nonproducing noncompetitive oil and gas leases and to pay the United States $3.01 million, as well as unspecified amounts of additional royalties, in connection with 11 producing noncompetitive oil and gas leases, including the eight leases involved herein. These royalties were to be calculated as if the leases had been issued pursuant to competitive bidding.

In return, PPCM and WEC were allowed to keep the 11 producing leases, and the United States agreed to execute releases in favor of PPCM and WEC, which releases would be effective upon payment of the $3.01 million in full. The United States agreed to release PPCM and WEC from liability and to refrain from instituting any civil or

6 The absence of any proof that an applicant assisted by NRG was required by written agreement to reimburse NRG from the proceeds of the lease, either in terms of a direct payment from or a commission on any sale of a subsequently acquired lease procured by NRG, distinguishes this case from the long line of cases represented by Raymond G. Albrecht, 92 IBLA 235, 93 I.D. 258 (1986).
administrative action of any kind against them as to any and all claims that the United States might have in connection with acquisition of any interest in any of the leases. However, the releases further provided:

This Release shall not release or discharge from liability the NRG Company, any employee of the NRG Company, including Jase O. Norsworthy, James W. Reger, Vincent T. Larsen, Dennis C. Rehrig, and Langdon G. Williams, or the original lessees of the [11 producing] leases * * *, as to whom the United States expressly reserves its rights.

In its September 1987 decision, BLM stated that, in cancelling the overriding royalty interests, it was acting pursuant to the Secretary’s general authority under the Mineral Leasing Act (MLA) recognized in Boesche v. Udall, 373 U.S. 472 (1963). BLM, with the exception of those interests held by Vincent T. Larsen, cancelled “any and all overriding royalty interests [in the subject oil and gas leases] acquired, retained or assigned * * * by the original lessees, the NRG Company, its officers or employees, their heirs, assignees or successors in interest.” BLM did so because, based on the criminal investigation, it had determined that such leases and interests were “fraudulently acquired in violation of the multi-filing regulation, 43 CFR 3112.5-2 [(1978)], and the sole party in interest regulation, 43 CFR 3102.7 [(1978)].” In an attachment to the September 1987 BLM decision, BLM identified 13 individuals as the current holders of overriding royalty interests in the subject oil and gas leases.

In addition to cancellation of the overriding royalty interests of 12 of those individuals, BLM required them (or their heirs, successors, or assigns) to repay it “any and all monies” that they had previously received with respect to the cancelled interests. Finally, BLM stated that “[t]he recovered monies and the cancelled interests will be offered by competitive sale under the provisions of 43 CFR 3120.1(d).” Ten of the identified holders of cancelled overriding royalty interests appealed from this first decision.

In conjunction with cancellation of the overriding royalty interests and the requirement to repay overriding royalties, by letter dated September 11, 1987, BLM contacted various parties who were either operators of the subject oil and gas leases or payors with respect to the overriding royalty interests cancelled in the September 1987 BLM decision and directed them to immediately place all future overriding royalties accruing with respect to the cancelled interests into interest-
bearing escrow accounts and to submit, within 60 days of receipt of the letter, a detailed accounting of all overriding royalties already paid to the holders of the overriding royalty interests or their heirs, successors, or assigns. The record indicates that this was done.

On October 20, 1987, apparently as a result of information provided by the operators/payors, BLM issued a decision identifying 16 other individuals (either acting on their own behalf or as trustees) and trusts as “successor holders” of overriding royalty interests cancelled in the September 1987 BLM decision. BLM stated that it regarded such individuals and trusts as parties to the September 1987 BLM decision and thereby also cancelled their overriding royalty interests and required them to repay to BLM any overriding royalties already paid to them. BLM’s October 1987 decision generated notices of appeal from the successors to the holders of the cancelled overriding royalty interests.9

[1] No appeal was filed by Menno L. Bargen, although the record establishes that a copy of BLM’s September 1987 decision was received at his last address of record on September 15, 1987. In the absence of a timely appeal, BLM’s decision cancelling Bargen’s interest in lease M-32324(ND) became final. However, BLM’s decision was timely appealed insofar as it cancelled other overriding royalties in this lease.

[2] Neither was an appeal filed by June M. Heller (lease M-34187(ND) Acq.). However, the record indicates that there were problems in serving her. BLM first sent a copy of its September 1987 decision to her address in Sun City, Arizona, which was returned with the notation that the addressee had moved and left no address. BLM sent a second copy to the “Trustee of the Heller Revocable Trust,” in Phoenix, Arizona, but it was returned for the same reason. A third copy was received by one Betty Hartmann, an apparent stranger to the dispute, on October 19, 1987.

We are left to speculate that Heller, who the record shows was at an advanced age when the lease was issued in 1976, might have died or become institutionalized, and that Hartmann is somehow associated with Heller’s estate. In these circumstances, we are unable to conclude that Heller’s interests, or those of her heirs, have been protected by providing due notice of BLM’s adverse decision. Accordingly, the decision cancelling her interest in lease M-34187(ND) Acq. cannot be considered final. In any event, as discussed below, we conclude that BLM improperly cancelled overriding royalty interests in that lease.

8 The successors to these interests who appealed from the October 1987 decision are: A. G. Bowen, Jr.; Margaret L. Jones; Emily Norsworthy; Margaret Norsworthy, Trustee, Norsworthy Family Trust No. 1; Margaret Reger Trust, First Trust Co. of Montana, J. W. Reger-Margaret Reger Trust; J. R. Reger Trust, First Trust Co. of Montana, J. W. Reger-J. R. Reger Trust; S. L. Reger Trust, First Trust Company of Montana; J. W. Reger-S. L. Reger Trust; Abbie Reger; Langdon Williams, Trustee; Margaret Ryan Trust, First Trust Co. of Montana, J. Reger-Margaret R. Ryan Trust; Forest Bowen; Theodore Williams; Trustee for David Williams, Michael Williams and Ted Williams; Joyce Williams; Dorothy VanArsdale; and Clinch Gray Norsworthy III.

9 We note that, in view of our decision reversing BLM’s cancellation of the other interests here, BLM may wish to consider whether it would work an injustice not to reconsider its decision concerning Bargen’s interest. See Texasgulf, Inc., 114 IBLA 66 (1980), and Walter Van Norman, Jr., 114 IBLA 56, 61 (1980) (Hughes, A.J., concurring).
APPLICATION OF DEPARTMENTAL REGULATIONS

Underlying all of the questions presented by these appeals is whether the leases in which appellants hold overriding royalty interests were acquired in violation of applicable Departmental regulations governing the simultaneous oil and gas leasing system.

Departmental Regulations

In its September 1987 decision, BLM stated that the subject leases were acquired in violation of 43 CFR 3112.5-2 (1978) and 43 CFR 3102.7 (1978) in effect at the time the DECs were filed. Departmental regulation 43 CFR 3112.5-2 (1978) provided:

> Where an agent or broker files an offer to lease for the same lands in behalf of more than one offeror under an agreement that, if a lease issues to any of such offerors, the agent or broker will participate in any proceeds derived from such lease, the agent or broker obtains thereby a greater probability of success in obtaining a share in the proceeds of the lease and all such offers filed by such agent or broker will * * * be rejected.

Additionally, Departmental regulation 43 CFR 3102.7 (1978), in conjunction with 43 CFR 3112.3-1 (1978), required that an offeror either submit a "signed statement * * * that he is the sole party in interest in the offer and the lease, if issued," or, if he is not the sole party in interest, "set forth the names of the other interested parties." An "interest" in a lease was defined by 43 CFR 3100.0-5 (1978) as including

any claim or any prospective or future claim to an advantage or benefit from a lease, and any participation or any defined or undefined share in any increments, issues, or profits which may be derived from or which may accrue in any manner from the lease based upon or pursuant to any agreement or understanding existing at the time when the offer is filed.

NRG Employees

[3] BLM's conclusion in its September 1987 decision that violations of these regulations occurred is largely based on the joint BLM/Department of Justice investigation and the guilty pleas of NRG and PPCM. BLM also stated that the violations were established both by the provision of the January 1983 plea agreement (leaving BLM free to pursue administrative remedies against NRG or its officers and employees) and by the provision of the June 1985 settlement agreement (actually contained in the attached general releases) that

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In the present case, the leases were actually not purchased from the successful drawees by NRG but rather, as arranged by NRG, by either PPCM or PPCM and WEC jointly. Pursuant to an agreement or understanding with NRG, an overriding royalty interest was then assigned to Jase O. Norsworthy and James W. Reger, the principals of NRG, and others. See Letter from NRG to PPCM, dated Dec. 13, 1974 (Exh. 3 attached to SOR of Langdon G. Williams et al.). Thus, PPCM or PPCM and WEC, as well as NRG, could be viewed as having an interest in any lease which might be issued in response to the subject DECs if the applicants were effectively required to sell their leases through NRG either to PPCM or PPCM and WEC.

In this regard, PPCM also pled guilty to having undisclosed interests in the DECs filed by NRG on behalf of its employees. U.S. v. Patrick Petroleum Corp., Crim. No. 82-4-BL6. Thus, the guilty pleas of both NRG and PPCM are equally relevant. However, for simplicity's sake, we shall refer only to the former.
NRG, its employees, and the original lessees of the eight leases involved herein were not released from liability. These provisions, however, merely constituted a reservation by the United States of its rights to pursue further actions against NRG and others and do not establish that these parties had engaged in any wrongdoing.

First examining the guilty plea, we note that NRG pleaded guilty only to preparing and filing (or causing to be prepared and filed) 12 DECs on behalf of its employees, which failed to disclose its status as another party in interest. None of the subject drawing entry cards formed the basis for the guilty plea, so that this plea cannot be viewed as an admission by NRG that it had an interest in any of the subject cards. The matter was, therefore, not conclusively determined by the criminal judgment. See United States v. Podell, 572 F.2d 31, 35 (2d Cir. 1978).

Nevertheless, the guilty plea is strong evidence that NRG did have an interest in the DECs of its employees. NRG's guilty plea, considered in light of the undisputed evidence contained in other documentation growing out of the criminal investigation, shows that NRG believed that, as a result of the filing method engineered by NRG, it had interests in the cards it prepared and filed (or caused to be prepared and filed) on behalf of its employees. There is no evidence that the circumstances with respect to which NRG pled guilty are any different from the circumstances under which it prepared and filed or caused to be prepared and filed other DECs for its employees.

The facts determined by BLM's investigation fully corroborate this impression. The record establishes that both NRG and its employees in whose names the cards were filed fully expected that NRG would arrange for PPCM or PPCM and WEC to purchase any lease issued to them. The evidence well supports the conclusion that the employee/applicants were required by verbal agreement, as a condition of their employment, to sell their leases to parties as directed by NRG under the terms described above. Employee/applicants had no realistic option of selling their leases to someone other than the purchaser selected by NRG. That is clearly borne out by the instance of an applicant who was assisted by NRG in preparing and filing a DEC and who did not sell her subsequently awarded lease as directed by NRG. That applicant was an employee of NRG who, according to her unchallenged statement, was harassed and eventually fired under questionable circumstances precisely because she chose not to sell her lease to NRG. See Statement of Leila M. Heidema (BLM Answer, Attachment 4 to Putsche Affidavit).

The experience of the fired employee was evidently related to other employees, thus conveying the unspoken but clear message that they too would be fired should they choose not to sell any awarded lease to

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12 After reviewing all of the evidence of the investigation proferred in the record, including the Dec. 16, 1987, affidavit of the BLM special agent who participated in the investigation and all attachments to the affidavit submitted with BLM's answer, we agree with BLM's representation that this offer of proof presents a complete picture of the results of that investigation.
NRG. The extent to which NRG laid claim to any lease acquired as a result of a DEC prepared and filed by it on behalf of an employee is evident in the following passage from the statement of Leila M. Heidema (BLM's Answer, Attachment 4 to Putsche Affidavit): "I dutifully called Don Jones [NRG office manager] at home [and] told him the good news, 'One of my cards [was] picked,' Don saying, 'You mean one of Norsworthy [and] Reger's cards [was] picked.'" (Italics in original.)

More directly, the record contains an undisputed statement by Valerie A. Williams that, around May 1978, the NRG office manager convened a meeting of female employees to reinstitute the filing of DECs by them. The office manager allegedly advised that if a parcel was won, NRG "expected it because of their investment," presumably in putting up the filing fee and advance rental. Also, the statement of Cynthia C. Curnow, an NRG employee from 1966 to 1978, relating that employees were "allowed to keep" overriding royalty interests, strongly suggests that NRG considered that the employees had no option but to transfer ownership of any leases that they won.

We hold that, in this system of filing DECs in its employees' names, NRG had created more than an option in an employee/applicant to sell any lease won to PPCM or PPCM and WEC, but rather a "claim" by it to an advantage or benefit from a lease within the meaning of 43 CFR 3100.0-5 (1978).

Lease M-34446(ND) was won by an NRG employee, Dorothy Van Wagoner. NRG held an interest in Van Wagoner's DEC that was not disclosed at the time the DEC was filed as required by 43 CFR 3102.7 (1978), in conjunction with 43 CFR 3112.3-1 (1978). Therefore, the DEC should have been rejected.

As discussed below, BLM lacked authority to administratively cancel interests in the lease, even though it was improvidently issued. Nevertheless, our determination that the regulations were violated may be relevant to any subsequent attempts to cancel these interests, either judicially or administratively.

There is some question as to whether Karen A. Rintoul, lease M-39449, was also an employee of NRG at the time her DEC was filed. It appears from one reference in the record that she was (BLM Answer, Exh. 4 at 4), but Rintoul convincingly argues that she was not (Statement of Reasons (SOR) of Rintoul at 8). BLM has not rebutted Rintoul's showing on appeal that she was not an employee, and we conclude that she was not.

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13 Van Wagoner has apparently married, as she has appeared under the name Dorothy Van Wagoner Lenehan.
14 We note generally that, although BLM cited the multiple-filing regulation, 43 CFR 3112.5-2 (1978), there is nothing in the record conclusively establishing that NRG filed more than one DEC on any of the eight parcels at issue here. There are general indications that NRG routinely made multiple filings. In view of our holding that NRG had an "interest" in its employee's DEC that was not disclosed in violation of 43 CFR 3102.7 (1978), it is unnecessary to consider whether these general indications provide a sufficient factual basis for determining whether a violation of 43 CFR 3112.5-2 (1978) also occurred.
Nonemployees

[4] Turning to the DECs of nonemployees of NRG, we note that NRG has never admitted that there was any impropriety with its filing of DECs on their behalf. As discussed above, its guilty plea was limited to situations involving the filing of DECs on behalf of its employees, which, we have held, did violate the regulations. Reviewing the other information in the administrative record, we are unable to determine that there was any means by which NRG could force a nonemployee/applicant to transfer a lease as it directed. If there were agreements between NRG and the nonemployee/applicants under which NRG could seek redress for a recalcitrant applicant, they are not shown in the record. Insofar as there is information in the record, it tends to show the contrary. See SOR of Hoiness at 2-7.

Nevertheless, the fact that all of these leases were assigned in such a manner as to grant identical overriding royalty interests to Norsworthy and Reger, officers of NRG, creates the impression that their DECs were filed for the undisclosed benefit of NRG, which, as a broker, would participate in the proceeds derived from the lease. In this regard, the Board has held that, where (1) rental is paid by a third party other than the applicant; (2) the applicant used the third party's address on the DEC; (3) the third party corresponded with BLM on the applicant's behalf; and (4) the third party was engaged in seeking to acquire oil and gas leases on Federal lands, there is a presumption that the DEC was filed for the undisclosed benefit of the third party, and that the mere assertion on appeal by the applicant that the lease would be hers and in her name only is insufficient to overturn BLM's decision rejecting applicant's offer for violating the sole party in interest disclosure requirement. Audrey Jean Boston, 67 IBLA 117, 119 (1982); Lynda Bagley Doye, 65 IBLA 340, 344 (1982).

At most, only two of these circumstances described in Boston and Doye are demonstrated by the record here, in that NRG, which was engaged in seeking to acquire oil and gas leases, paid the rental on some of these leases. Significantly, unlike in those cases, the applicants here used their own addresses on their DECs, thus ensuring that other parties who wished to purchase any lease that was "won" could contact the applicants directly, without the need to go through NRG. We do not find that the circumstances here justify a presumption that there was an undisclosed interest.

We do find that the record shows that the method for acquiring leases developed by NRG rested on the fact that the nonemployees enlisted to sign DECs were friends and relatives of the employees or

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15 In 1979, the regulations governing simultaneous noncompetitive leasing were substantially revised, largely to deal with "abuses" of "filing services." See 44 FR 56176 (Sept. 28, 1979). In the preamble to these amendments, the Department noted that "some services have advanced the first year's rental and obtained leases which have then been assigned without their clients' knowledge." Id. (Italics added). Changes were made to ensure that applicants would be more directly involved in the process of marketing any leases that they "won."

In this case, the fact that these eight applicants each used an address other than NRG's ostensibly prevented a similar abuse here, as any winning applicant would, at least, have been aware that he or she had "won" a lease and could have been contacted directly by prospective purchasers of the lease.
principals of NRG and, thus, could be expected to sell any subsequently acquired lease to NRG by ties of loyalty.

We note initially that the filing of DECs by family members for similar parcels is not, by itself, impermissible. BLM has previously held, with our tacit approval, that nothing in the regulations applicable in 1978 prohibited family members from filing on the same parcels. See Lillian Sweet, 37 IBLA 25, 27 (1978). A limited exception to this rule was announced by the Board, as obiter dictum, in Farrell L. Lines, Trustee, 40 IBLA 91, 96-97 (1979), to the effect that minor children of a family unit have an "interest" in oil and gas lease offers filed by their parents, such that the prohibition against multiple filings would be violated if both the parent and minor child filed applications for the same parcel. In that case, multiple offers were filed by trustees on behalf of several minor children of a parent, as well as by the parent himself. In the instant case, although at least one child (James R. Reger, son of James W. Reger) filed a DEC, it does not appear that he was a minor, as it was filed in his own name. In the absence of a showing that the children were minors at the time their DECs were filed, and that DECs were also filed by their parents on particular parcels, we see no need to consider whether the Lines rule applies here.

The determinative question is whether such claims of loyalty amount to a "claim" to an advantage or benefit from a lease under 43 CFR 3100.0-5 (1978), or merely a hope or expectancy that the applicant would sell the lease to NRG. A hope or expectation does not amount to an interest in a lease within the meaning of 43 CFR 3100.0-5 (1978), even where the filing service selects the parcel, submits the DEC, and pays the filing fee and first year's rental. D. E. Pack, 30 IBLA 230, 232-33 (1977); John V. Steffens, 74 I.D. 46, 53 (1967). The following excerpt from Steffens is illustrative of the rationale for concluding that the filing service does not have an interest in a potential lease in such circumstances:

"The most that Central Southwest obtained under the arrangement, as far as the record shows, was a calculated likelihood that a successful client would feel a sense of duty to give Central Southwest the first opportunity to obtain an assignment of a lease which, coupled with Central Southwest's direct means of communication with the client, would give it a practical advantage over competitors in securing an interest in the client's lease. Undoubtedly, Central Southwest could bring an action to recover the amount of the rental payment advanced to a client, but we see no basis upon which it could successfully assert a claim of interest in a lease in the event a client elected not to accept its offer to purchase the lease. Thus, while we recognize the advantage obtained by Central Southwest, we are unable to conclude that this expectancy constitutes an "interest" within the meaning of 43 CFR 3100.0-5(a)."

The Board held that the trust arrangement for the minor children gave a contingent remainder interest to the parents that was sufficient to qualify as an "interest." Thus, the Board's observation that the general concern of a minor child in the relative wealth or interest of his family constituted a "beneficial interest" that must be disclosed stands as dictum.

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16 The Board held that the trust arrangement for the minor children gave a contingent remainder interest to the parents that was sufficient to qualify as an "interest." Thus, the Board's observation that the general concern of a minor child in the relative wealth or interest of his family constituted a "beneficial interest" that must be disclosed stands as dictum.
The question remains, if the successful nonemployee/applicants were not forced to sell their leases to NRG, why did they do so, when they could possibly have sold them to other parties on more favorable terms? In this regard, we find the circumstances surrounding June M. Heller's participation instructive. Mrs. Heller, the octogenarian grandmother of the wife of an NRG employee, signed DECs for NRG whenever she was visiting her daughter in California (who also had evidently been enlisted to sign cards for filing by NRG). When asked by a Government investigator why she did not negotiate the assignment terms before assigning her lease to NRG, she stated that she regarded the lease as a "gift," because "it didn't cost her anything." While Mrs. Heller seems to have been guided by a sense of gratitude toward NRG, there was nothing preventing her from promoting the sale of the lease on her own. What could NRG have done to force Mrs. Heller to do its bidding on the lease? There is nothing to show that there was any agreement between them, or between NRG and any other nonemployee. While it is arguably likely that Mrs. Heller was guided by a sense of loyalty to her granddaughter and that she would have been swayed by a threat to the employment of her granddaughter's spouse, it is equally possible that she would not.

We regard this sense of moral obligation as too imprecise and amorphous to be counted as an "interest," as that term is defined in the applicable regulation. We see NRG's decision to put up money for nonemployees under these circumstances as a gamble on the possibility that feelings of gratitude and loyalty would overcome more pragmatic considerations. While this gamble evidently paid off repeatedly, admittedly resulting in an "advantage" for NRG, we are unable to conclude that taking it amounted to a violation of Departmental regulations. See John V. Steffens, supra at 53.

Additionally, we note, as to the DEC of Melvin P. Hoiness, that his uncontradicted statement convinces us that he was not bound by any pre-existing agreement to convey lease M-32760 as directed by NRG. To the contrary, the record shows that Hoiness made a conscious decision to assign his lease to NRG, after he had won the lease and after considering a competing offer to purchase. Hoiness indicated that, instead of attempting to assert any rights in acquiring the lease, NRG left the decision up to him.

BLM argues on appeal that the present case is similar to H. J. Enevoldsen, 44 IBLA 70, 86 I.D. 643 (1979), aff'd, Enevoldsen v. Andrus, Civ. No. 80-0047B (D. Wyo. June 24, 1981), wherein the Board concluded that a third party, which had prepared and filed DECs on behalf of others, had an interest in any subsequently issued lease because there was a verbal agreement that the third party would have

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17 We accept for the sake of argument the general statement in the offer of proof that other parties offered the applicants more favorable terms for their lease interests.
either the "first opportunity to make an offer to purchase the lease [from the applicant]," commonly known as the first right to buy, or the "right to match any other offer made by a third person to [the applicant]," commonly known as the right of first refusal. Id. at 90, 86 I.D. at 653. We concluded that such a right, enforceable against the applicant, was a prospective "claim" to an advantage or benefit from a lease, and was therefore an "interest" within the meaning of 43 CFR 3100.0-5 (1978). Although the applicant could chose not to sell, should he decide to do so, he was required first to allow the third party either to offer to purchase the lease or to match another offer for the lease. This arrangement, we held, created an "interest" in any subsequently acquired lease, which interest was required to be disclosed.

However, in concluding that either a first right to buy or a right of first refusal constituted an interest in a lease under Departmental regulations, we expressly distinguished an "option in the lessee to sell to the agent filing service," stating:

In [the latter] situation, there is no restraint on alienation of the lease. The lessee may sell to anyone and the agent has no claim against him if he chooses to sell to someone else, without exercising the option to sell to the agent. Under * * * a right of first refusal * * *, however, the lessee is restricted in his rights to the lease because he cannot alienate any interest in the lease without complying first with his arrangement with [the agent filing service].

Id. Unlike Enevoldsen, there is no evidence that the present case involved an agreement establishing either a first right to buy or a right of first refusal.

In these circumstances, we cannot determine that prelease violations of either 43 CFR 3102.7 (1978) (requiring disclosure of other parties in interest) or 43 CFR 3112.5-2 (1978) (prohibiting multiple filing of DECs by an agent or broker under an agreement allowing him to participate in the proceeds of any lease issued) occurred as to the DECs of nonemployees of NRG. Neither NRG nor PPCM had a cognizable "interest" in the DECs of nonemployees of NRG, as there were no enforceable agreements with nonemployees allowing NRG or PPCM to participate in the proceeds of leases issued to them. Accordingly, we reverse BLM's decisions to the extent that DECs were filed by parties who were not employees of NRG.

Apart from the lease held by Van Wagoner (Lenehan), the leases involved herein were issued to nonemployees of NRG. Accordingly, BLM's decisions as to the following leases are hereby reversed: M-32760(ND) Acq. (Melvin P. Hoiness); M-32753 (ND) Acq. (June A. Larsen); M-34187(ND) Acq. (June M. Heller); M-37404 (SD) (James R. Reger); M-34449(ND) Acq. (Deborah C. Reger); and M-39449 (Karen A. Rintoul). BLM's decision concerning lease M-32324 (ND) (Menno L. Bargen) is reversed insofar as it cancelled interests held by Norsworthy, Reger, and Williams.
We hold below that BLM lacked authority to administratively cancel these leases. However, the issue of the validity of the DECs is nevertheless significant, as it is possible that BLM might seek judicial cancellation or attempt to justify administrative cancellation under the 1988 regulations. As the obtaining of the above leases involved no cognizable pre-lease improprieties established by the present record, BLM may not pursue cancellation as to these interests.

**ADMINISTRATIVE CANCELLATION OF OVERRIDING ROYALTY INTERESTS**

[5] Appellants challenge BLM’s authority to cancel their overriding royalty interests. In doing so, BLM relied on *Boesche v. Udall*, supra, in which the Supreme Court considered the question of whether the Secretary of the Interior had the authority to administratively cancel a “lease of public lands issued under the provisions of the Mineral Leasing Act * * * * in circumstances where such lease was granted in violation of the Act and regulations promulgated thereunder.” *Id.* at 473. The Court concluded that, “under his general powers of management over the public lands,” the Secretary has traditionally possessed the authority to administratively cancel a lease “for invalidity at its inception,” *i.e.*, where a breach of the Act or its implementing regulations occurred *prior* to issuance of the lease, and that this authority was not withdrawn by the MLA, either as originally enacted or as subsequently amended. *Id.* at 476.

*Boesche* concerned a nonproducing lease, and the Supreme Court was careful to note that it sanctioned “no broader rule than is called for by the exigencies of the general situation and the circumstances of this particular case.” *Id.* at 485. Nevertheless, *Boesche* may be read as suggesting that the Department has broad administrative authority to cancel MLA leases for pre-lease violations without regard to whether the lease is in production. BLM was evidently guided by such reading in reaching its decision in the instant appeal.

However, this Board has consistently held that, whatever the Secretary’s inherent authority might be, the Secretary has restricted that authority by promulgating a regulation that requires the initiation of judicial proceedings to cancel a producing lease. *E.g.*, *James W. Smith*, 6 IBLA 318, 79 I.D. 439 (1972); *Naartex Consulting Corp.*, 48 IBLA 166 (1980), *appeal dismissed, Naartex Consulting Corp. v. Watt*, 542 F.Supp. 1196 (D.D.C. 1982), *aff’d*, 722 F.2d 779 (D.C. Cir. 1983), *cert. denied*, 467 U.S. 1210 (1984); *Suzanne Walsh*, 98 IBLA 363 (1987). *Smith* and its progeny held that the Department, through its regulations, had interpreted section 27(h)(1) of the MLA, 30 U.S.C. § 184(h)(1) (1982), to require judicial action to cancel any interest in a lease in production, regardless of whether the underlying violation was pre- or post-lease.¹⁸

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¹⁸ By so doing, the Board itself elected to read sec. 27(h)(1) to apply to any violation of the MLA, rather than (as suggested by the Supreme Court in *Boesche*, supra at 480) merely to any violation of the acreage limitation provisions.
Indeed, Departmental regulations have consistently left no room to doubt that judicial action is required to cancel a producing lease. For example, 43 CFR 3108.3 (1972), considered by the Board in *Smith*, supra at 324, 79 I.D. at 442, provided: "Judicial Proceedings. Leases known to contain valuable deposits of oil or gas may be cancelled only by judicial proceedings in the manner provided in sections 27 and 31 of the Act." (Italics added.) No distinction between pre- or post-lease violations could be discerned from this regulation, either from its express terms or by implication. The Board, holding that it was bound to follow this regulation, declined in *Smith* to sanction administrative cancellation of any producing oil and gas lease.

The cancellation regulation was amended on May 23, 1980, 45 FR 35163, but it was recodified virtually verbatim as 43 CFR 3108.3(b) (1981): "A lease known to contain valuable deposits of oil or gas may be canceled only by judicial proceedings in the manner provided in sections 27 and 31 of the Act." Again, there was no doubt that judicial action was necessary to cancel a producing lease.

The cancellation regulation was amended and expanded again on July 22, 1983, 48 FR 33662. As codified, the amended regulation contained three subsections, 43 CFR 3108.3(a)-(c) (1984). Subsection 3108.3(a) contained language relating to section 31 of the MLA authorizing cancellation for post-lease violations, both administratively and judicially, depending on whether the lands covered by the lease were known to contain valuable deposits of oil or gas. Subsection 3108.3(b) contained a broad statement that "(l)ease shall be subject to cancellation if improperly issued," giving the impression that leases could be generally cancelled by the Department for improprieties in issuance (including pre-lease violations). However, this impression was countered by subsection 3108.3(c), which repeated the old rule that "(l)ease for lands known to contain valuable deposits of oil or gas may be cancelled only by judicial proceedings in the manner provided in sections 27 and 31 of the Act." The language of subsection 3108.3(c) was identical to that previously construed in *Smith* as limiting Departmental authority to administratively cancel producing leases.

Despite the inclusion of the more liberal 43 CFR 3108.3(b) (1984), in *Suzanne Walsh*, supra, we expressly held that subsection 43 CFR 3108.3(c) (1984) continued the prohibition against administrative cancellation of producing oil and gas leases, including those leases not in production but merely covering lands known to contain valuable deposits of oil or gas:

In *James W. Smith*, the Board concluded en banc that this regulation, which is longstanding, constitutes an administratively imposed limitation on the Secretary's
traditional authority to cancel oil and gas leases which were improvidently issued, and that the Department is bound by that regulation. Thus, the Department cannot administratively cancel appellant's lease even though it covers land which is not subject to Federal oil and gas leasing if it is determined that the lands leased are "known to contain valuable deposits of oil or gas." [Citations omitted.]

98 IBLA at 371. In *Walsh* we remanded the case to BLM with instructions to refer the matter to the Department of Justice for initiation of judicial proceedings to cancel the lease.

It is the 1983 version of the cancellation regulation that was in effect in 1987 when BLM issued these decisions. 43 CFR 3108.3 (1987). It is undisputed that all the leases involved in the case are producing leases. Based on the Board precedents discussed above, there is no doubt that, at the time its decisions were issued, BLM lacked authority to cancel these leases administratively. Accordingly, its decisions must be reversed *in toto* for this reason.

BLM attempts to deflect the applicability of 43 CFR 3108.3(c) (1987), requiring judicial cancellation, by arguing that this section applies only to "leases" rather than "interests in leases." We do not believe that such a distinction can be made. Even though 43 CFR 3108.3(c) speaks of "leases" being cancelled, the reference in the regulations to section 27 of the MLA necessitates the conclusion that the regulation also encompasses "interests in leases." Section 27(h)(1) of the MLA provides for an election where an interest in a lease is owned or controlled in violation of any of the provisions of the MLA: the lease may be cancelled, the interests forfeited, or the person owning the interest may be compelled to dispose of the interest, "in any appropriate proceeding instituted by the Attorney General." Therefore, where a regulation provides that a lease may be cancelled only by judicial proceedings in the manner provided in section 27, the option of cancellation of the lease, forfeiture of the interest, or compelling disposition of the interest is available to the Attorney General. Thus, 43 CFR 3108.3(c) (1987), like section 27, addresses cancellation of both leases and interests in leases.

We are not unmindful that the cancellation regulation was amended in 1988, following issuance of BLM's decisions here. 53 FR 22822 (June 17, 1988). At that time, BLM announced its intention to reconsider the general question of the Department's authority to cancel leases administratively:

> As a result of [BLM's] review of the comments on [the cancellation provisions] and a review of the language of the proposed rulemaking and the cancellation provisions of the law, it has been determined that the proposed rulemaking did not clearly implement the [Department's] oil and gas lease cancellation authority. The final rulemaking has,

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19 Sec. 5104 of the Reform Act, P.L. 100-203, 101 Stat. 1330-259 (1987), amended sec. 31 of the MLA to clarify when the Department could cancel a lease for post-lease violations without instituting judicial proceedings. Specifically, sec. 5104 provides that this authority exists "unless or until the leasehold contains a well capable of production of oil or gas in paying quantities, or [unless and until] the lease is committed to an approved cooperative or unit plan or communitization agreement." This section merely clarified sec. 31 of the MLA, which had provided more broadly that the Secretary's authority to cancel a lease for post-lease violations existed "unless or until the land covered by any such lease is known to contain valuable deposits of oil or gas." The 1988 amendment of 43 CFR 3108.3 (1978) added the Reform Act's clarification that cancellation for post-lease violations could not be accomplished administratively when either actual or allotted production had occurred previously. 53 FR 22822 (June 17, 1988).
therefore, been revised by adding a separate paragraph setting out the authority in section 31(b) of the [MLA] for breach of the lease, another paragraph setting out the judicial cancellation authority in section 31(a) of the [MLA] for breach of the lease, and a separate paragraph setting out the judicial authority in section 27(h)(1) of [the MLA] for interests held in violation of the Act.

53 FR 22823 (June 17, 1988). BLM has not had an opportunity to address how these changes affect its authority to cancel leases administratively.20 Thus, the interests of efficient adjudication would best be served if BLM makes the initial determination on this question, and, on remand, it is free to consider the question of whether interests in lease M-34446(ND) may be cancelled administratively. Any adverse decision would, of course, be subject to appeal.

In view of our reversal of BLM's decisions, it is unnecessary to address other questions that may significantly affect the outcome of any subsequent proceeding. These questions are best addressed in the context of a specific appeal from any future adverse decision.

ATTORNEY'S FEES AND EXPENSES

[6] Appellants contend that they are entitled to recover attorneys' fees and expenses incurred by them in order to maintain the instant appeals, pursuant to section 203(a)(1) of the Equal Access to Justice Act (EAJA), as amended, 5 U.S.C. § 504 (Supp. IV 1986).

Section 203(a)(1) of the EAJA provides for the award of attorneys' fees and expenses to the prevailing party in an "adversary adjudication" except where the position of the agency was substantially justified or special circumstances make an award unjust. 5 U.S.C. § 505 (Supp. IV 1986). However, despite the fact that appellants are prevailing parties in this case, it is clear they are not entitled to recover attorneys' fees and expenses under any circumstances. As construed by the Board, section 203(a)(1) of the EAJA is only applicable in the case of adjudications "required by statute [5 U.S.C. § 554 (1982)] to be determined on the record after"

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20 We note that, far from liberalizing BLM's cancellation authority to include producing leases, 43 CFR 3108.3(c) (1988) has been changed in a way which calls into question BLM's authority to administratively cancel any lease (producing or nonproducing). This provision now effectively states, "If any interest in any lease is owned or controlled in violation of any of the provisions of the act, the lease may be canceled only by judicial proceedings in the manner provided by section 27(h)(1) of the [MLA]." No mention is made of whether the lease is in production or is known to contain valuable deposits of oil or gas. This provision thus plainly appears to limit BLM's authority to cancel leases for any violation of the MLA to judicial proceedings, regardless of whether the lease is in production. We note that the regulation is more restrictive than the statute in that the statute states that action may be taken in any appropriate proceeding instituted by the Attorney General, while the regulation states that action may only be taken by judicial proceedings. This action is possibly explained if one reads sec. 27(h)(1) as applying only to acreage limitations, as suggested by the Supreme Court in Boesche, supra at 480. However, both the Board (James W. Smith, supra at 823 n.4, 79 I.D. at 442 n.4) and BLM (preamble to 1988 rulemaking, 53 FR 22823 (June 17, 1988)) have rejected this narrow reading of the statute. Nor would the cancellation authority apparently be saved by the inclusion of the more liberal 43 CFR 3108.3(d) (1988), stating "[l]ease shall be subject to cancellation if improperly issued." As discussed above, in Suzanne Walsh, supra, we expressly held that subsec. 43 CFR 3108.3(c) (1984) continued the prohibition against administrative cancellation of producing oil and gas leases, notwithstanding the presence of 43 CFR 3108.3(d) (1988) (then codified as 43 CFR 3108.3(b) (1984)). As noted above, the applicability of 43 CFR 3108.3(c) has been significantly expanded by the 1988 rulemaking.
opportunity for an agency hearing." BLM v. Ericsson, 98 IBLA 258, 261-62 (1987); see Cavin v. United States, 19 Cl. Ct. 198 (1989). The present proceeding falls within the purview of the MLA and the Mineral Leasing Act for Acquired Lands. Nothing in those Acts requires that administrative adjudication under the Acts be conducted on the record after opportunity for a hearing. Thus, we conclude that appellants are not entitled to recover attorneys' fees and expenses and hereby deny their requests.

Accordingly, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decisions appealed from are reversed, and appellants' requests for attorneys' fees are denied.

DAVID L. HUGHES
Administrative Judge

I CONCUR:

BRUCE R. HARRIS
Administrative Judge
## APPENDIX A

<table>
<thead>
<tr>
<th>Oil and Gas Lease</th>
<th>Original Lessee</th>
<th>Holders of Overriding Royalty Interests</th>
<th>Percentage Amounts of Overriding Royalty Interests</th>
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NGC ENERGY CO., MONO POWER CO.

114 IBLA 141

Appeal from a decision of the Colorado State Office, Bureau of Land Management, upholding a prior decision finding that drainage had occurred from lands within oil and gas lease C-17540, and providing for the assessment of compensatory royalties.

Vacated in part, reversed in part.

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

Compensatory royalties accrue after the passage of a reasonable time following the date the lessee knew or should have known that drainage was occurring. In a common lessee context, the lessee who drills the offending well is in the best position to know that drainage is occurring. In such case BLM need not assume the initial burden of showing that the lessee knew that a reasonably prudent operator should have known that drainage was occurring, as the common lessee is presumed to have knowledge of the drainage upon first production from its offending well. This presumption is rebuttable by the common lessee, who bears the ultimate burden of persuasion as to the date he had notice that drainage was occurring.

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

Under the usual statement of the standard for prudent operation, the lessee is not obligated to drill an offset well unless there is a sufficient quantity of oil or gas to pay a reasonable profit to the lessee over and above the cost of drilling the well. The prudent operator standard applies to situations in which a leased Federal tract is being drained by a well operated by a common lessee. In such cases, BLM has the burden of establishing that the leased Federal tract is being drained by the common lessee's non-Federal well, but need not prove as a part of its cause of action that a protective well would be economic. The burden of producing evidence and the ultimate burden of persuasion on this issue rest with the common lessee.

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

No breach of a lessee's duty to prevent drainage will occur if the cost of drilling and operating an offset well is greater than the value of the recovered oil and/or gas. However, if a lessee can make a reasonable profit by drilling the well, he has a duty to prevent drainage by drilling a well. The prudent operator test is applied looking to the reasonably anticipatable recovery from the offset well, rather than the oil and/or gas which would be lost if the well were not drilled.

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

An oil and gas lessee is generally required to take such actions as would be prudent to protect his lessor from unnecessary losses due to drainage. The scope of this responsibility is not limited to drilling an offset well, but embraces all other actions a prudent operator might consider. Thus, if a prudent operator would unitize, it follows that a failure to do so would constitute a breach of the duty to protect the lessor from unnecessary loss due to drainage.
The concept of a duty to unitize is thoroughly compatible with the prudent operator standard governing a lessee’s conduct and the viability of unitization is a factor to be considered when determining whether a lessee has discharged his duty to protect the leased premises from drainage. However, the lessee may always demonstrate that a prudent operator would not have formed a unit, that the lessee had unsuccessfully attempted to establish a unit, or that the costs of unitization would not leave him a profit.

When an offset well would not now be, and never would have been, profitable there is no legally defensible basis for requiring unitization. To require unitization in such cases ignores economics and simple practicalities. Quite apart from any theoretical difficulties in justifying unitization, the unitization of a producing property with a property that could not profitably be produced is virtually impossible. The operating and nonoperating interest owners of the producing property have no practical or economic reason for consenting to such unitization.


OPINION BY ADMINISTRATIVE JUDGE MULLEN

INTERIOR BOARD OF LAND APPEALS

NGC Energy Co. (NGC) and Mono Power Co. (Mono) have appealed from a May 5, 1988, decision of the Colorado State Office, Bureau of Land Management (BLM), upholding a prior decision that drainage had occurred from land within Federal oil and gas lease C-17540, and providing for the assessment of compensatory royalties.¹

A brief history of lease C-17540 provides the necessary background for this appeal. Effective July 1, 1969, BLM issued lease C-8929 encompassing the SW¼, sec. 15, the N½ NW¼, sec. 28, and the N½ N½, sec. 29, T. 1 N., R. 103 W., sixth principal meridian, Rio Blanco County, Colorado, for a term of 10 years. Effective January 3, 1973, a portion of the land subject to lease C-8929 (i.e., the N½ NW¼, sec. 28) was committed to the Bantu Ridge Unit, and the uncommitted remainder was segregated and assigned serial number C-17540. A portion of the land subject to lease C-17540 was then committed to the Taiga Mountain Unit effective November 7, 1978, the uncommitted acreage was again segregated, and the new lease was assigned a new serial number. Following this second unitization and segregation, lease C-17540 embraced 160 acres in the N½ N½, sec. 29, T. 1 N., R. 103 W., sixth principal meridian. Production under the unit extended the term of lease C-17540 beyond the end of its original term.

¹ In its answer to NGC's statement of reasons, BLM admits error in its decision holding NGC liable for drainage. NGC was not a common lessee and did not have notice of the alleged drainage until 2 months prior to lease expiration. See Consolidation Coal Co., 87 IBLA 296, 301 (1986), finding that, when two or more lessees have an undivided interest in a lease, they hold the lease as tenants in common and there is no agency relationship between them. Therefore, notice to one lessee does not bind another lessee unless the notified lessee has the authority to act for the other. We therefore vacate BLM's liability determination as to NGC and will not specifically address the issues NGC raised on appeal.
As a result of development drilling in sec. 20, T. 1 N., R. 103 W. (which was not within the Taiga Mountain Unit), BLM placed the acreage subject to lease C-17540 in an undefined addition to an undefined known geologic structure (KGS), effective December 29, 1982. Effective June 23, 1984, when the Taiga Mountain Unit automatically contracted, lease C-17540 was eliminated from that unit. The term of lease C-17540 was extended for 2 years from the date of elimination pursuant to 43 CFR 3107.4, and expired on June 23, 1986.

At all relevant times Coseka Resources (USA) Ltd. (Coseka) owned an undivided 50-percent interest, Mono owned an undivided 25-percent interest, and NGC owned the remaining undivided 25-percent interest in lease C-17540. Coseka was the operator of the lease. Coseka and Mono also held interests in a lease of adjacent fee lands in sec. 20, T. 1 N., R. 103 W., sixth principal meridian. On December 29, 1982, Coseka completed the Coseka 3-20-1N-103 Coors (3-20 Coors) well as a producing gas well in the SE 1/4 SW 1/4 of sec. 20, within its fee lease.

By letter dated April 25, 1986, BLM notified lessees that it was conducting a statewide review of areas in which Federal leases might be drained by offset producing wells, including possible drainage of lease C-17540 by the 3-20 Coors well. After noting that the lease and regulations required lessees to protect the lease from drainage, BLM stated that, if lessees believed that drainage was not occurring or that an economic well could not be drilled, they should submit data supporting their position. Coseka responded by letter dated June 4, 1986, stating that, because most of lease C-17540 was in a separate fault block from the 3-20 Coors well, it was not being drained by that well. Coseka did admit that a portion of the lease, located in the NW 1/4 NW 1/4, sec. 29, fell within the same fault block and could be drained by the well, but stated that well spacing closer than 160 acres could not be justified, given the then current gas prices.

By letter dated July 31, 1987, BLM informed lessees that, based on preliminary geologic and engineering reviews, it had determined that the lease was subject to possible drainage by the 3-20 Coors well. While recognizing that the lease had expired, BLM reminded lessees that, during the term of the lease, they had a duty to protect the lease land from drainage. BLM indicated that, if the lessees could not demonstrate that drainage had not occurred, using detailed engineering or geologic data, they would be assessed compensatory royalties from the date of first production from the 3-20 Coors well until the date of expiration of lease C-17540.

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2 NGC's interest was originally held by Pacific Transmission Supply Co. (PTS). Effective Nov. 1, 1980, PTS assigned its interest to Natural Gas Corp. of California (an affiliate of NGC). This interest was reconveyed to PTS, effective Nov. 1, 1985. NGC obtained PTS' interest through merger.

3 The successful completion of this well apparently triggered BLM's decision to include lands subject to lease C-17540 in the undefined KGS. See text supra.

4 This letter superseded a July 23, 1987, letter. When the first letter was written, the author assumed that the lease was still in existence and requested plans for drilling a protective well.
In a response dated September 21, 1987, Coseka submitted additional engineering and geologic data in support of its position that, at the most, minimal drainage had occurred, and that it would have been uneconomic to drill a protective well. Coseka explained its rationale for defining the extent of the reservoir and indicated that two wells, the 3-20 Coors and the Coseka 9-20-1N-103 Federal (located in the SE^¼ NE^¼, sec. 20, T. 1 N., R. 103 W.), were producing from the reservoir. Coseka concluded that the majority of lease C-17540 was nonproductive, and that the small quantity of hydrocarbons contained in the portion of the lease subject to possible drainage was insufficient to warrant an offset well.

By decision dated March 18, 1988, BLM determined that drainage had occurred from lease C-17540 and assessed compensatory royalty based upon 18.8 percent of production from the 3-20 Coors well between December 1982 and June 23, 1986. BLM did not specifically state the basis for its decision. However, a final geologic report dated March 3, 1988, and a final engineering report dated March 9, 1988, appear to be the foundation for its determination.

The final geologic report dated March 3, 1988, was prepared by BLM based on Coseka's data. The drafters of this report agreed with the Coseka findings that: (1) only the NW^¼ NW'A of sec. 29 was capable of containing producible hydrocarbons, and (2) it was not economically feasible to drill a well on the lease. Having reached these conclusions, the author of the final geologic report concluded that compensatory royalties should be assessed.

The final engineering report dated March 9, 1988, also relied on data supplied by Coseka. In computing the drainage factor, the author of that report determined that the 3-20 Coors well would drain 53.1 acres of the reservoir, and that 10 of those acres were within lease C-17540. Based upon these findings, the drainage factor was determined to be 18.8 percent of the 3-20 Coors production.

Coseka, Mono, and NGC all sought state director review (SDR) of the BLM decision. Mono and NGC argued that the duty to protect against drainage did not arise until a reasonable time after BLM notification that drainage was occurring, and that BLM first notified them of the drainage in April 1986, less than 2 months prior to lease expiration. They contended that they had no obligation to drill a protective well or pay compensatory royalty because the lease expired before the passage of a reasonable time after BLM's notice. They further asserted that no compensatory royalty was due because a protective well would not have been economically justified, citing Board decisions holding that the prudent operator rule applies to Federal drainage cases. The prudent operator rule provides that a lessee is not required to drill a protective well or pay compensatory royalty if the protective well is not economically justified. NGC submitted an additional analysis.

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*The report found that the Coseka 9-20-1N-103 Federal well drained 121 acres of the same reservoir.*
demonstrating that the drilling of a protective well on the lease at any
time after December 1982 would not have been profitable.\(^6\)

Coseka’s SDR submission included the arguments raised by Mono
and NGC. In addition it argued that BLM’s drainage determination
was improper because BLM provided no geologic or engineering data to
contradict Coseka’s evidence that only a small amount of drainage was
occurring from the Federal lease, and no evidence that the drainage
was sufficient to justify the assessment of compensatory royalties.
Coseka further stated that it was operating under the protection of the
U.S. Bankruptcy Code, and any assessment for compensatory royalty
against it had been discharged because BLM had received notification
and failed to file a claim.

In the May 5, 1988, decision, the State Director upheld the prior
decision as to Mono and NGC, but found that Coseka’s bankruptcy and
subsequent reorganization precluded assessment of compensatory
royalties against it. He identified two issues (in addition to the
bankruptcy issue) raised in the SDR requests: (1) the notice
requirement; and (2) the economic viability of a protective well. He
found that the Board decisions cited by Mono and NGC were not
controlling because they did not involve common ownership of the
offending well and the drained Federal lease, and concluded that
"IBLA never intended to require an economic test in cases involving
common ownership." The State Director also determined that, in the
common lessee context, "since the operator of the offending well is also
a lessee of the offset tract, notification of the drainage situation is not
necessary. The lessee has obviously been aware of the offset from the
beginning, therefore notification is irrelevant in the case of common
ownership."

The State Director agreed with the allegation that BLM had offered
no contradictory evidence to refute lessees’ data, stating that BLM had
"no contention with Coseka’s interpretation of the reservoir limits or
with well performance," and acknowledged that the 18.8-percent
drainage factor "was calculated using the drainage area as determined
by volumetric analysis of the 3-20 Coors well and the bounded reservoir
area under lease [C-17540]. The parameters utilized in this analysis
were those which Coseka supplied."\(^7\) He further found that payment
of compensatory royalties beyond the expiration date of the lease could
extend the lease for as long as the offending well continued to produce
and lessees tendered the compensatory royalties.

In its statement of reasons for appeal, Mono again asserts that, even
though it is a common lessee, it is entitled to notification by BLM that

\(^6\) In a separate submission, Coseka also provided further technical information bolstering its conclusion that the
lessees would incur substantial losses if they were to drill a protective well on the Federal lease.

\(^7\) In the Final Engineering Report prepared for the SDR, BLM found that, in determining the volume per acre-foot
of both the 3-20 Coors well and the Coseka 9-20-1N-103 Federal well, Coseka had incorrectly applied the recovery factor
twice, and, therefore, Coseka’s calculations were invalid. The State Director’s decision does not mention Coseka’s error
on this point.
drainage is occurring before incurring a duty to protect the lease against that drainage, and that the assessment of compensatory royalties can commence only after the expiration of a reasonable time following such notification. It alleges that the applicable regulations mandate that it be afforded the opportunity to drill a protective well to prevent drainage, and that BLM must provide notice of drainage and allow a lessee a reasonable amount of time in which to drill a protective well before it can assess compensatory royalties. Mono argues that compensatory royalties cannot be assessed because BLM advised it that drainage might be occurring less than 2 months prior to lease expiration thereby depriving it of its option to drill.

Mono further argues that the prudent operator rule should apply in the common lessee context, and that BLM has failed to find that drilling a protective well would have been economic or in accordance with good oil field practices. Mono asserts that this conclusion is supported by the evidence submitted to BLM, which clearly demonstrates that drilling on lease C-17540 would not have been economically justified. Mono concludes that no compensatory royalty should be assessed in this case, or, alternatively, that the Board should refer the case for a hearing to determine the existence of drainage and, if drainage occurred, the date from which compensatory royalty should be assessed.

In its response, BLM concedes that it was never economically feasible to drill a protective well on lease C-17540, but argues that this fact does not preclude BLM from assessing compensatory royalties in the common lessee context. BLM contends that a common lessee has a duty to unitize a lease being drained with other leases, including the offending well, even if a prudent operator would not drill a protective well, citing Williams v. Humble Oil & Refining Co., 432 F.2d 165 (5th Cir. 1970), cert. denied, 402 U.S. 954 (1971), a case decided under Louisiana law, in support of this contention. It asserts that, in common lessee drainage cases, the question is not whether the lessee could have drilled a profitable offset well, but whether the lessee has taken all reasonable steps to prevent drainage. BLM argues that these steps include unitization, forced pooling, or obtaining administrative relief from spacing orders. According to BLM, the imposition of this duty to unitize is necessary to prevent fraudulent drainage by circumventing the prudent operator rule.

[1] The applicable regulations governing drainage and compensatory royalty, 43 CFR 3100.2-2 and 43 CFR 3162.2(a), provide in part, respectively:

Where lands in any leases are being drained of their oil or gas content by wells either on a Federal lease issued at a lower rate of royalty or on non-Federal lands, the lessee

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8 Mono notes the following additional facts. In this case the owners of the offending well and the Federal lease are not all the same. Mono owns a smaller interest in the 3-20 Coors well (20 percent before payout and 12.5 percent after payout) than it does in the Federal lease (25 percent). It argues that it would defy common sense to assume that it would deliberately drain production from under the Federal lease by producing from a well in which it owns a smaller interest.

9 This argument was raised for the first time in the BLM answer.
shall both drill and produce all wells necessary to protect the leased lands from drainage. In lieu of drilling necessary wells, the lessee may, with the consent of the authorized officer, pay compensatory royalty in the amount determined in accordance with 30 CFR 221.21.

(a) The lessee shall drill diligently and produce continuously from such wells as are necessary to protect the lessor from loss of royalty by reason of drainage. The authorized officer may assess compensatory royalty under which the lessee will pay a sum determined as adequate to compensate the lessor for the lessee's failure to drill and produce wells required to protect the lessor from loss through drainage by wells on adjacent lands.

In Atlantic Richfield Co., 105 IBLA 218, 95 I.D. 235 (1988), and Atlantic Richfield Co. (On Reconsideration), 110 IBLA 200, 96 I.D. 363 (1989), this Board considered the drainage issue in the context of a common lessee. In our initial decision we discussed the principle that compensatory royalties commence upon the passage of a reasonable time following notice to the lessee that drainage is occurring. We held:

In a common lessee context, the lessee who drills the offending well is in the best position to know that drainage is occurring. In such context, we find no reason for requiring BLM to assume the initial burden of going forward with evidence that the common lessee knew or that a reasonably prudent operator should have known that drainage was occurring. See Elliott v. Pure Oil Co., [10 Ill.2d 146, 139 N.E.2d 295 (1956)]. The common lessee shall be presumed to have knowledge of the drainage upon first production from its offending well. However, this presumption is rebuttable by the common lessee, who bears the ultimate burden of persuasion as to notice of drainage. Id. at 226, 95 I.D. at 240. See also Cordillera Corp., 111 IBLA 61, 65-66 (1989). Thus, contrary to Mono's assertion, BLM is not barred from assessing compensatory royalties by its failure to notify it of the possible drainage before April 1986.

[2] Under the usual statement of the prudent operator rule, even if drainage is occurring, the lessee is not required to drill an offset well unless there is a sufficient quantity of oil or gas to pay a reasonable profit to the lessee over and above the cost of drilling the well. Nola Grace Ptysynski, 63 IBLA 240, 247, 89 I.D. 208, 212 (1982).

In Atlantic Richfield Co., supra at 224-25, 226, 95 I.D. at 239, 240, we determined that the prudent operator standard applies when a leased Federal tract is being drained by a well operated by a common lessee. In that case we also refined our determination regarding the proper burdens of proof in the common lessee context. In such situations, BLM has the burden of establishing that the leased Federal tract is being drained by the common lessee's non-Federal well. However, it need not show, as a part of its cause of action, that a protective well would be economic. In the case of a common lessee, the burden of producing evidence and the ultimate burden of persuasion on this issue rest with the common lessee. Id. at 225, 95 I.D. at 239. See also Cordillera Corp., supra at 66.

[3] In Atlantic Richfield Co., supra, we also discussed the appropriate test of prudent operation to be applied in common lessee cases. We noted that, because the loss to the lessor is an economic loss, economics
should govern the duty to drill. We held that if the cost of drilling and operating an offset well is greater than the value of the recovered oil and/or gas, there would be no breach of a lessee's duty to prevent drainage. However, if a lessee can make a reasonable profit by drilling the well, the well should be drilled. We held that one must look to the reasonably anticipatable recovery from the offset well, rather than the oil and/or gas that would be lost if the well were not drilled when applying the prudent operator test. *Atlantic Richfield Co., supra* at 226-27, 95 I.D. at 240-41.

In *Atlantic Richfield Co., supra*, we also considered the extent to which the prudent operator rule is applicable to drainage by a common lessee. In that decision we held that the prudent operator rule limits the duty of a common lessee to protect Federal lands from drainage, i.e., a common lessee must pay compensatory royalty on oil and gas that it drained from a Federal lease only if the reserves recoverable by a protective well on the Federal lease are sufficient to pay a reasonable profit over and above the cost of drilling and operating the well.

[4] BLM concedes that it would not have been economically feasible to drill a protective well on lease C-17540, because a protective well would not have produced sufficient oil or gas to recover the costs of drilling. That question is no longer in issue. Nevertheless, BLM now asserts that Mono must pay compensatory royalty because Mono had a duty to unitize the Federal lease with the offending lease, even though it had no duty to drill an offset well. On appeal BLM argues that appellant's obligation to seek unitization arises from operation of the prudent operator rule. In other words, since lessees are generally required to take such actions as would be prudent to protect a lessor from unnecessary losses due to drainage, the scope of the lessee's responsibility cannot be limited to drilling an off-set well, but must embrace all other actions which a prudent operator might consider.

As a general proposition, we do not find this formulation objectionable. Certainly, if a lessee unitized a lease rather than drilling an offset well, one could hardly say that the lessee did not fulfill the lease obligations merely because the regulations do not expressly state that unitization is an option. See, e.g., *Cordillera Corp., supra* at 65-66. By the same token, the failure to expressly delineate a unitization option in the regulations should not preclude a finding that a prudent operator would have unitized the lease. It follows that, if a prudent operator would unitize, a failure to do so would constitute a breach of the duty to protect the lease against drainage. As previously noted, in *Nola Grace Ptasynski, supra*, this Board found the prudent operator rule applicable to Federal leases.

Notwithstanding the fact that a failure to unitize would constitute a breach of the lessee's duty to protect the lease against drainage if a prudent operator would unitize, BLM's assertion of a duty to unitize in the face of a clear showing that an offset well could not be economically drilled is fraught with both legal and practical difficulties. This is particularly true in the instant appeal. In the first
place, none of the court decisions BLM cites to this Board imposes a duty to unitize. The decision of the Fifth Circuit Court of Appeals in *Williams v. Humble Oil & Refining Co.*, supra, on which counsel seems to rely for the broad assertion that it is not “unreasonable to require a common lessee to unitize a lease being drained with others [Reply at 7],” establishes no such absolute duty. Rather, this decision recognizes that the viability of unitization is a factor to be considered when determining whether a lessee has discharged his prudent operator duty to protect against drainage. Thus, the court noted:

To require the lessee in certain circumstances to seek unitization will not place an unfair burden upon him. Indeed, the concept of a duty to unitize is thoroughly compatible with the “prudent administrator” standard governing his conduct with respect to other implied covenants. The lessee may always defend a suit based upon his failure to unitize by showing that a prudent operator would not have formed a unit or that he had attempted without success all reasonable means to establish a unit or that the costs of unitization would not leave him a profit. [Italics supplied.]

*Id.* at 174.

Thus, the Fifth Circuit expressly recognized that there was no absolute obligation to unitize, but that a lessee had the obligation to factor in the possibility of unitization when carrying out its duties as a prudent operator. When an offsetting well is shown to be profitable, it makes eminent good sense that prudent lessees would consider unitization as a viable and practical alternative to drilling the offset well. However, when an offset well would not now be, and never would have been, profitable, we find no legally defensible basis for requiring unitization. Such an approach ignores economics and simple practicalities.

In *Nola Grace Ptasynski*, supra at 251, 89 I.D. at 214-15, we addressed the economic basis of the prudent operator rule in the context of the obligation to drill an offset well to prevent drainage of leased lands:

If the recoverable oil underlying the land where drainage is occurring is insufficient to support the cost of recovery, no intelligent landowner would make out-of-pocket expenditures to drill a well. The oil lost through drainage is not an economic loss to the landowner, because its attempted recovery would actually cost the landowner money. Thus, while in some conceptual sense the landowner has lost the oil drained, there has been no economic loss occasioned by the drainage. The landowner is no worse off than he was before the offending well commenced to drain his meager reserves, and considerably better off then he would be if he tried to recover them by drilling an offset well. A lessee

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10 The decision in *Cook v. El Paso Natural Gas Co.*, 580 F.2d 978 (10th Cir. 1977), cited by BLM, is essentially premised on the conclusion that the prudent operator rule does not apply at all in the common lessee situation. Indeed, on this point, rather than following the rationale of the Fifth Circuit, as suggested by BLM counsel, it is directly contrary to *Williams v. Humble Oil & Refining Co.*, supra. In the *Williams* case, the requirement that a lessee consider unitization was directly derived from the prudent operator rule. The question of the applicability of the prudent operator rule in the common lessee situation was examined in *Atlantic Richfield Co. (On Reconsideration)*, supra. While *Cook* was not cited, the Board expressly rejected the theory that the prudent operator rule was inapplicable.

11 This prudent operator requirement should not be limited to a common lessee. It would apply to all drainage situations.
should not be obligated to pursue a course of economic folly which a prudent owner would forego. [Italics in original, footnote omitted.]

These same considerations apply to an analysis of unitization in lieu of drilling an uneconomic offset well. When the owner of the property being drained seeks to compel unitization in such a situation, that party seeks compensation for oil or gas which could not be profitably produced. In short, it would be an attempt to share in proceeds properly appertaining to its neighbor's property, at its neighbor's expense, and with none of the risk its neighbor assumed when drilling the well.

As a practical matter, it is difficult to see how unitization could be accomplished in the situation now before us. The operator of a producing well would not normally be disposed to unitize with an adjacent property merely to permit the adjacent property owner an opportunity to share in the proceeds from the producing well. Thus, the unitization addressed in Williams v. Humble Oil & Refining Co., supra, was forced, and not consensual. This fact was expressly recognized by the court at page 174 of that decision.

Nor would the protection of correlative rights apply if, as in this case, the drained mineral owner's ability to drill a protection well is constrained only by economic realities and not by legal impediments. Cf. Sinclair Oil & Gas Co. v. Bishop, 441 P.2d 436, 446-47 (Ok. 1967) (implying obligation to seek unitization where production from an existing well would result in waste in violation of state conservation statues). Nor is the prevention of the drilling of unnecessary wells implicated. Assuming rationality on the part of the drained mineral lessee, no additional wells would be drilled in any event.

The relationship of a lessee to the adjacent property owners will normally be of no consequence when considering the economics of unitization. The presence of a common lessee is relevant only because of the need to gain the consent of a specified percentage of the interest owners (operating and nonoperating) in the area to be unitized. This

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12 Forced pooling would not be an available option where, as in the instant case, the offending well was in one drilling unit and the land being drained in another.

13 While it is true that the adjacent mineral owner would be required to pay its aliquot share of production costs, it is also true that the owner of the drained mineral estate would not seek unitization if the owner expects that the allocated costs of production would be greater than the allocated share of the profits. If an absolute duty to unitize were applicable to both common and noncommon lessees, a situation could arise where an adjacent lessee would be required to unitize with land containing a nonprofitable well for the sole purpose of allowing his lessee to share in the royalty payments. See, e.g., Hardy, Drainage of Oil & Gas from Adjoining Tracts--A Further Development, 6 Nat. Res. J. 45, 57-58 (1966) (where an argument is made for precisely this result in the common lessee situation). Paradoxically, in this situation, the draining working interest owner would be happy to share his loss with the drained working interest owner. Such a result would, of course, be totally inconsistent with the entire prudent operator rule. That rule is clearly premised on the concept that the lessee should not be required to lose money solely for the purpose of permitting the lessee to obtain royalties.

14 To the extent that the leases involved may contain pooling clauses, it is possible that imposition of an obligation to unitize on a common lessee would give rise to an obligation to pool the royalty interest of the draining lease and thus the consent of the nonparticipating owners (generally required under both voluntary and forced unitization) would be obtained. Although such unitization might technically be deemed voluntary, it would occur only when a common lessee is forced to take action it would otherwise avoid. Moreover, it forces the common lessee to take actions with respect to the drained royalty owner's interests which might be deemed violative of its duty of fair dealing. See discussion in text infra.

15 Moreover, if legal impediments did exist, it seems difficult to justify forced unitization to protect correlative rights when the adjacent mineral owner would not drill a protective well if afforded the opportunity.

is the case for both voluntary and forced unitization. See generally Williams & Meyers, Oil & Gas Law § 913.5. Thus, quite apart from any theoretical difficulties in justifying unitization, it is virtually impossible to unitize a producing property with a property that could not be produced profitably under applicable spacing and drilling units. The operating and nonoperating interest owners of the producing property would have no practical or economic reason for consenting to such unitization.

In the “uncomplicated” common lessee situation, unitization would normally have no economic effect on the interests of the common lessee. The common lessee would still receive all net income less royalty payments. Indeed, the essential neutrality of unitization to the lessee’s economic interests in such cases has been expressly recognized and cited as supporting the imposition of the duty to seek unitization upon a common lessee. See Williams v. Humble Oil & Refining Co., supra at 174. However, this analysis conveniently overlooks the obvious fact that the benefits gained by the drained lessor are at the direct expense of the draining lessor. It could not be expected that a lessor of the draining parcel would favor unitization when faced with these economic realities.

It should be noted, however, that many oil and gas leases contain pooling clauses permitting the lessee to pool all mineral interests without the lessor’s consent. It might be argued, therefore, that in such situations, the common lessee would be obligated to utilize this provision to pool the nonworking interest of his lessor (unitize) to protect the adjacent land from drainage. See, e.g., Hardy, Drainage of Oil & Gas from Adjoining Tracts--A Further Development, 6 Nat. Res. J. 45, 55-56 (1966). However, to accept this premise one must ignore the lessee’s affirmative “fair dealing” obligation to the lessor of the draining land. See generally, Williams & Meyers, Oil & Gas Law § 420.2.

It does not take much imagination to envision a legal basis for a suit to enjoin a lessee from unitizing a producing lease with land which is not and was never capable of economic production, when a common lessee is seeking unitization for the sole purpose of avoiding a possible conflict with the lessor of the drained land. It is questionable whether this action represents a reasonable discharge of the common lessee’s obligation of “fair dealing” with the lessor of the productive tract. The lessor of the draining land obtains absolutely no benefit when a

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17 By using this phrase we expressly refer to a common lessee owning 100 percent of the operating interests in both tracts of land.

18 The one obvious exception would be when the drained parcel has a nonoperating interests burden which is greater than that existing on the draining parcel. Another exception would be when the common lessee owns the entire mineral estate in the draining parcel.

19 Admittedly, most pooling clauses expressly limit the amount of acreage with which the leased land may be pooled or unitized. See generally Williams & Meyers, Oil & Gas Law § 669.10. Thus, the discussion in the text assumes that this limitation would not be exceeded. If it is, the royalty interest owner’s consent would be needed—an unlikely event, as noted earlier in the text.
common lessee's actions are based on the desire to avoid the possibility of liability to the lessor of the drained land rather than rational economic considerations. This issue would arise only when two parcels of land happened to have a common lessee. Therefore, until policy considerations, not now apparent, are shown to militate against having a lessee control adjoining parcels, there appears to be absolutely no theoretical justification for imposing a general obligation on a common lessee which would not be imposed if the parcels had been leased by separate entities.  

All of the difficulties we have discussed are compounded when there are multiple lessees rather than a single common lessee holding the entire operating interests in both tracts. In this case, one party owned interests only in the drained tract, several entities held interests only in the draining tract, two parties owned interests in both tracts, and one of the two (Coseka, the operator under both leases) has since been discharged in bankruptcy of all further liability. Given the undisputed fact that an offsetting well would not be profitable, it is difficult to believe that there was even a remote possibility that unitization could have been effected by Mono.  

It may well be that the land which the United States leased has been, in some conceptual sense, drained of oil, but the United States has suffered no real economic loss as a result of that drainage. Such loss as might have occurred is simply damnnum absque injuria. See generally Phillips Petroleum Co. v. Millette, 72 So.2d 176, 189 (Miss. 1954) (Ethridge, J., dissenting) ("Since appellees could not have gained by the production of oil from their lands, they could not lose by its subterranean drainage"). Counsel for BLM seeks to have us award the Government what is essentially a windfall, merely because its lessee had also leased the adjacent tract. Such action is not justified.

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 vacated in part and reversed in part.

R. W. MULLEN  
Administrative Judge

I CONCUR:

JAMES L. BURSKI  
Administrative Judge

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20 This is not to say that there may not be a specific fact situation under which a common lessee should be held to a higher standard. Such special circumstance should be addressed if and when it arises. Clearly, no general rationale exists to justify such treatment in other than an exceptional case.

21 Coors Energy Co. owned an after-payout working interest of 33.5-percent in the producing fee lease. There would be no earthly reason for Coors to agree to unitization with the Federal tract and, therefore, no possible method to unitize the two leases under the Colorado statutes.
MICHIcAN EXPLORATION CO.

114 IBLA 177 Decided April 23, 1990

Appeal from a decision of the Eastern States Office, Bureau of Land Management, dismissing a protest of the survey of an island previously omitted from survey. ES 7050.

Affirmed.


An unsurveyed island, whether located in navigable or non-navigable waters, remains public domain, does not pass with the bed under the water to a state upon statehood or convey with a grant of riparian land, and may be surveyed and disposed of by the United States.

2. Boundaries--Conveyances: Exceptions--Navigable Waters--Patents of Public Lands--Surveys of Public Lands: Omitted Lands

A railroad patent to the State of Michigan describing “all of section one” does not convey an unsurveyed island within the meander lines of a lake, whether navigable or non-navigable, located within sec. 1, and the United States may properly survey such island.


OPINION BY ADMINISTRATIVE JUDGE FRAZIER

INTERIOR BOARD OF LAND APPEALS

Northern Michigan Exploration Co. (NOMECO) has appealed from a decision of the State Director, Eastern States Office, Bureau of Land Management (BLM), dated June 2, 1987, dismissing NOMECO’s protest of the survey of an island in Rennie Lake, T. 26 N., R. 10 W., Michigan Meridian, Michigan. The island at issue, designated as Tract 37 on BLM’s plat of survey, is not shown on prior plats of survey of the township or mentioned in the field notes of these early surveys. Prior surveys occurred in 1839, when the exterior boundaries and subdivisional lines of the township were originally surveyed, and in 1852 when the subdivisional lines were resurveyed.

In a Federal Register notice dated May 22, 1986, 51 FR 18844, BLM stated that its plat of survey had been accepted on May 2, 1986, and would be filed in the Eastern States Office on June 30, 1986. Interested parties seeking to protest BLM’s determination that Tract 37 was public land of the United States were directed to file such protest by June 30.
MICHIGAN EXPLORATION CO.

114 IBLA 177

Decided April 23, 1990

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A railroad patent to the State of Michigan describing "all of section one" does not convey an unsurveyed island within the meander lines of a lake, whether navigable or non-navigable, located within sec. 1, and the United States may properly survey such island.


OPINION BY ADMINISTRATIVE JUDGE FRAZIER

INTERIOR BOARD OF LAND APPEALS

Northern Michigan Exploration Co. (NOMECO) has appealed from a decision of the State Director, Eastern States Office, Bureau of Land Management (BLM), dated June 2, 1987, dismissing NOMECO's protest of the survey of an island in Rennie Lake, T. 26 N., R. 10 W., Michigan Meridian, Michigan. The island at issue, designated as Tract 37 on BLM's plat of survey, is not shown on prior plats of survey of the township or mentioned in the field notes of these early surveys. Prior surveys occurred in 1839, when the exterior boundaries and subdiisional lines of the township were originally surveyed, and in 1852 when the subdiisional lines were resurveyed.

In a Federal Register notice dated May 22, 1986, 51 FR 18844, BLM stated that its plat of survey had been accepted on May 2, 1986, and would be filed in the Eastern States Office on June 30, 1986. Interested parties seeking to protest BLM's determination that Tract 37 was public land of the United States were directed to file such protest by June 30.
Appellant NOMECO filed a timely protest, identifying itself as the lessee of a mineral interest owned by Mr. and Mrs. Wilbur Scheck. Appellant's protest cited *United States v. Chandler-Dunbar Water Power Co.*, 209 U.S. 447 (1908), for the proposition that a patentee of Government land bordering on a navigable waterway takes to the centerline of the waterway, including small unsurveyed islands like Tract 37, between the mainland and centerline. BLM's decision of June 2, 1987, responded that *Chandler-Dunbar* was distinguishable because the islands at issue there were regarded by the Supreme Court as part of the streambed.

BLM's decision offered additional facts which place its survey in historical context. Fractional sec. 1, the situs of Tract 37, is shown on the Department's 1853 plat of survey to be invaded by the waters of a meandered lake. The official acreage of sec. 1 is reported as 534.26 acres. As noted above, Tract 37 does not appear on this 1853 plat.

Instructions issued by the Surveyor General in 1850 for the States of Ohio, Indiana, and Michigan required deputy surveyors to meander "all lakes and deep ponds, of the area of forty acres and upwards; and all islands suitable for cultivation." C. Albert White, *A History of the Rectangular Survey System* 368 (italics supplied). Subsequent instructions in 1864 advised that survey of "small unsurveyed islands which were omitted when the adjacent lands were surveyed" was authorized if an applicant for survey paid the cost thereof; such islands are "usually of too little value to justify the Government in incurring the expense of survey." *Id.* at 503.

Current instructions set forth at section 3-122 of *The Manual of Instructions for the Survey of the Public Lands of the United States* (1973) provide:

> Even though the United States has parted with its title to the adjoining mainland, an island in a meandered body of water, navigable or nonnavigable, in continuous existence since the date of the admission of the State into the Union, and omitted from the original survey, remains public land of the United States. As such the island is subject to survey.

Pursuant to special instructions dated July 28, 1985, Cadastral Surveyor Anthony E. Carrow executed the survey of the island at issue. Carrow's plat of survey designated the island as Tract 37 and indicated its area as 0.80 acre. Field notes of this survey concluded that the island was in place "in 1839 when the township was subdivided, in 1837 when the State of Michigan was admitted into the Union and at all subsequent dates and is public land of the United States." 2

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1. Mr. Scheck also filed a protest, which stated, "I do claim, have record title, and have occupied" Tract 37 since purchasing the island in 1941 from H. J. Ullmann. Scheck maintained that his abstract of title shows that the Grand Rapids & Indiana R.R. Co. owned the property in 1891. The Schecks did not appeal the BLM decision denying their protest.

2. Appellant states that the evidence supporting the existence of Tract 37 in 1837 is inconclusive at best, but offers no contrary evidence. Appellant refers instead to cases that "establish a presumption that the surveys were accurate when made," which presumption must be overcome by the Government to prevail in its claim that the island was present when the early surveys were made.

BLM's evidence of the existence of the island in 1837 consists of the following:

Continued
In its statement of reasons, appellant states that "all of section one, containing five hundred and thirty-four acres and twenty-six hundredths of an acre" was conveyed by the United States to the State of Michigan by patent dated July 27, 1891. This conveyance was made pursuant to the Act of June 3, 1856, 11 Stat. 21, granting to the State every alternate section of land for six sections in width on each side of a railroad to be constructed. By Supplemental List No. 49, Michigan selected the "whole of section 1," T. 26 N., R. 10 W., as an indemnity selection in lieu of lands within the primary limits (i.e., 6 miles) of the railroad. Supplemental List No. 49 was approved and certified by the Secretary of the Interior on June 10, 1864.

Shortly after the enabling legislation of June 3, 1856, the Michigan State Legislature appears to have conveyed its interest in the lands described therein to the Grand Rapids & Indiana Railroad Co. This fact is gleaned from recitations in a warranty deed, recorded September 9, 1891, by which the Railroad, inter alia, conveyed to Jonathan Cobb and William W. Mitchell part of sec. 1. The record does not further reveal the chain of title from Cobb and Mitchell to H. J. Ullmann, grantor of the Schecks. When in 1941 the Schecks purchased the island from Ullmann, the island was very small, the water was high, and small shrubs grew upon the island, Scheck's protest states.

The island designated as Tract No. 37, consists of sandy loam rising gradually out of Rennie Lake to an elevation of 3 feet above the normal lake level.

The island does not fall within the meandered area of the original survey and is surrounded by shallow waters of the lake with a maximum depth of 2 to 3 feet. The lake level is variable depending upon the season and year. At the time of the survey, the lake level appeared to be approximately 1 foot above the normal lake level as evidenced by the escarpment and accompanying timber fringe growth. The nearest mainland bears Southwesterly, 3 cs. dist. over a channel depth of 3 feet. There is no evidence of the presence of old stumps in the channel.

There are no currents within the lake nor movements of silt laden waters and the island does not appear to have been formed by accretion or the depositing of silt. The island does not appear to have been uncovered since the 1839 original survey by any recession of the lake.

The timber species on the island are similar to that on the mainland and consist of white pine, red pine, jack pine, birch, and aspen with an understory of aspen, maple, pine, and oak. The size of trees range from 6 to 15 inches in diameter. A boring sample of a red pine, 15 inches diameter shows an approximate age of 45 years. There also appears to be a few large stump impressions on the island but no stumps were found.

"Local residents all stated that the island had been in existence within their knowledge of the area, the longest being approximately 30 years."

"A map prepared by the Michigan Department of Natural Resources from marginal survey and soundings by Michigan Emergency Conservation work in the winter of 1936-37, show the depths of Rennie Lake and indicate an island separate and distinct from the mainland in the same location as this island."

"From the general characteristics of the island, similar to the opposing mainland, and the lack of evidence that the island was formed by silting action or uncovered by the recession of the lake, it may be presumed that the island was in place in 1839 when the township was subdivided, in 1837 when the State of Michigan was admitted into the Union and at all subsequent dates and is public land of the United States."

"The only evidence of occupancy is an old campfire circle and a pit 5x3 foot square dug on the south side of the island down to the lake level." (Field notes of the Survey completed Sept. 6, 1985).

In light of the 1810 instructions of the Surveyor General, directing deputy surveyors to meander all islands suitable for cultivation, and in the absence of evidence adduced by appellant, we will not disturb BLM's finding that Tract 37 was in place in 1837 and at all subsequent dates.

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1 The island designated as Tract No. 37, consists of sandy loam rising gradually out of Rennie Lake to an elevation of 3 feet above the normal lake level.

2 The island does not fall within the meandered area of the original survey and is surrounded by shallow waters of the lake with a maximum depth of 2 to 3 feet. The lake level is variable depending upon the season and year. At the time of the survey, the lake level appeared to be approximately 1 foot above the normal lake level as evidenced by the escarpment and accompanying timber fringe growth. The nearest mainland bears Southwesterly, 3 cs. dist. over a channel depth of 3 feet. There is no evidence of the presence of old stumps in the channel.

3 There are no currents within the lake nor movements of silt laden waters and the island does not appear to have been formed by accretion or the depositing of silt. The island does not appear to have been uncovered since the 1839 original survey by any recession of the lake.

4 The island does not fall within the meandered area of the original survey and is surrounded by shallow waters of the lake with a maximum depth of 2 to 3 feet. The lake level is variable depending upon the season and year. At the time of the survey, the lake level appeared to be approximately 1 foot above the normal lake level as evidenced by the escarpment and accompanying timber fringe growth. The nearest mainland bears Southeasterly, 3 cs. dist. over a channel depth of 3 feet. There is no evidence of the presence of old stumps in the channel.

5 The island does not fall within the meandered area of the original survey and is surrounded by shallow waters of the lake with a maximum depth of 2 to 3 feet. The lake level is variable depending upon the season and year. At the time of the survey, the lake level appeared to be approximately 1 foot above the normal lake level as evidenced by the escarpment and accompanying timber fringe growth. The nearest mainland bears Southeasterly, 3 cs. dist. over a channel depth of 3 feet. There is no evidence of the presence of old stumps in the channel.

6 The island does not fall within the meandered area of the original survey and is surrounded by shallow waters of the lake with a maximum depth of 2 to 3 feet. The lake level is variable depending upon the season and year. At the time of the survey, the lake level appeared to be approximately 1 foot above the normal lake level as evidenced by the escarpment and accompanying timber fringe growth. The nearest mainland bears Southeasterly, 3 cs. dist. over a channel depth of 3 feet. There is no evidence of the presence of old stumps in the channel.
In its arguments on appeal, appellant refines its protest argument to state:

An analysis of the * * * cases leads to the conclusion that where an island is small and of little apparent value and where there is no indication that its omission from the government’s original survey was due to mistake or fraud on the part of the surveyor, the island will be deemed to have passed with a grant of the uplands. This conclusion is even more certain when the island is located in a non-navigable body of water.

(Statement of Reasons, July 29, 1987, at 6).

In support of this argument, appellant relies heavily upon four cases:


1. No determination of the navigability of Rennie Lake has been made by BLM. Such a determination is properly made on the basis of conditions in 1837 when Michigan was admitted to the Union, United States v. Oregon, 295 U.S. 1, 14, 15 (1935). Despite BLM’s reticence in making a navigability determination, appellant elsewhere assumes that Rennie Lake is non-navigable. See Statement of Reasons, supra at 6.

2. Butler was a suit to quiet title in an “island” of 2.56 acres that had been omitted from the original survey of lands riparian to the Grand River in Michigan. Plaintiff Butler was the successor-in-interest to Federal patentees of nearby riparian land; the Railroad held a Federal patent to the island at issue, which had been surveyed some 20 years after the original surveys were run.

Citing Hardin v. Jordan, 160 U.S. 371 (1895), the Supreme Court stated that grants by the United States of its public lands bounded on streams and other waters, made without reservation or restriction, are to be construed as to their effect according to the law of the state in which the land lies. Michigan law held that a grant of land bounded by a stream, whether navigable or not, carried with it the bed of the stream to the center of the thread thereof. 159 U.S. at 92-94. Affirming judgment in favor of Butler, the Court stated, “We have no doubt upon the evidence that the circumstances were such at the time of the survey as naturally induced the surveyor to decline to survey this particular spot as an island.” Id. at 95.

3. McBride involved a petition by a homesteader to survey a 22-acre island in the Platte River. The Department refused this petition relying on Butler, supra note 8, and held that survey and sale of the island was precluded by the fact that the adjacent banks of the river had been surveyed and sold. Looking to Nebraska law, the Supreme Court held that riparian proprietors are the owners of the bed of the stream to the center of the channel. The Court acknowledged that the Government, as original proprietor, has the right to survey and sell any lands, including islands in a river, but that if it omits to survey an island and thereafter refuses to do so, no citizen can override the Department, assume that the island ought to have been surveyed, and proceed to homestead it.

4. Chandler-Dunbar Water Power Co. claimed two islands in the navigable Sault St. Marie under a patent from the United States describing riparian land on the river St. Mary. In response to the company’s claim, the United States filed a bill in equity to remove this apparent cloud on the Federal title. The bill acknowledged that the bed of the river surrounding the islands passed to Michigan at the time of Statehood, but denied that the islands passed by the patent of neighboring lands. The Supreme Court found the islands to be unsurveyed and of little value and held that the Act offering Michigan admission to the Union did not except these islands from the acknowledged transfer to the State of the streambed surrounding them. If by the law of Michigan the bed of the river or strait would pass to a grantee of the uplands, the Court reasoned, it may be assumed that the islands passed along with the bed. Citing Butler, supra at note 8, the Court held that under Michigan law a grant of land bounded by a stream, whether navigable in fact or not, carries with it the bed of the stream to the center of the thread thereof. The claim of the United States was, accordingly, found to be without plausible ground.

5. Bourgeois was a suit for just compensation to recover the value of an island allegedly appropriated by the United States. Plaintiff claimed to be the successor-in-interest to a Federal patent (1866) of upland riparian to the non-navigable Jewell Lake in Michigan. The island at issue, 6.76 acres, was first surveyed in 1855, having been omitted from the 1846 plat of survey; the 1846 plat did, however, show a meandered Jewell Lake.

In seeking to determine whether the 1866 patent conveyed the island, the Court of Claims distinguished Federal cases involving navigable and non-navigable waters. From these cases, the court drew a further distinction between those involving islands and beds.

Finding no Federal or common law on point, the court fashioned a rule based on an analogy to non-navigable water bed cases. These cases held that when land bordering a non-navigable body of water is ceded, the beds pass (unless the intent of the grantor is expressly stated to the contrary) according to state law. Under Michigan law, the court stated, title to the beds passes to the shoreland owners. 545 F.2d at 731. The court, accordingly, held that plaintiff could recover just compensation from the United States upon proof of her title in the upland.

In concluding that cases involving non-navigable water beds were the best analogy to the dispute at hand, the court focused on accessibility to the island. Cases involving islands in navigable waters were rejected because the Government could with impunity cede title to shoreland while retaining access by the navigable water route. In Olive Wheeler, supra, the United States v. Chandler-Dunbar Water Power Co., supra, Bourgeois v. United States, supra, the Board addressed the Bourgeois analysis. Citing Emma S. Peterson, 39 I.D. 585 (1911), which held that an unsurveyed island, whether located in navigable or non-navigable waters, remains public land, the Board stated that it was not persuaded by Bourgeois that there should be a different rule for non-navigable waters. The Board also stated, “It is not the case, as the court in Bourgeois assumed, that such an island
evidence there "left it uncertain whether the so-called island was more than 'a low sand bar, covered a good part of the year with water.'"

Scott v. Lattig, 227 U.S. 229, 244 (1913). The "conformation" involved in Butler contrasts vividly with the fast lands identified by BLM as Tract 37. 159 U.S. at 95.

McBride is also easily distinguished because the Government was not a party to that case. As such, the Supreme Court held: "N]othing we have said is to be construed as a determination of the power of the Government to order a survey of this island or of the rights which would result in case it did make such survey." 197 U.S. at 515.

Chandler-Dunbar involved islands that were "little more than rocks rising very slightly above the level of the water." Id. at 451. Though the acreage of these islands (one island contained "a small fraction of an acre" and the other "a little more than an acre") is similar to that in Tract 37, the Court's citation to Butler and its failure to distinguish United States v. Mission Rock Co., 189 U.S. 391 (1903), lead to the conclusion that the islands were regarded as indistinguishable from the bed of the navigable river surrounding them. Tract 37 does not fit such a description.

Bourgeois offers faint support for appellant's position because that case relied upon a theory of access to hold that "if the intent of the grantor is ambiguous and the Government grants shoreland along non-navigable waters, it also passes title to islands according to the law of the state in which the property is located." 545 F.2d at 731. Key to this decision by the U.S. Court of Claims was the notion that if the Government has not reserved an easement in any of the Federal patents of riparian upland, it would have absolutely no way to use an island in a non-navigable lake. No access existing in favor of the Government, title to the island should pass according to state law, the court reasons. Such a view, however, overlooks the Government’s power to obtain access by eminent domain. Leo Sheep Co. v. United States, 440 U.S. 668, 680 (1979).

[1] In Scott v. Lattig, supra, Mr. Justice Van Devanter set forth the law applicable to the instant facts. Although Scott involved an omitted island in a navigable river, we have previously held in R. A. Mikelson,
26 IBLA 1, 9 (1976), that Scott applies also to non-navigable bodies of water. Accord, Olive Wheeler, 108 IBLA at 296; Emma Peterson, 39 L.D. at 567. We reiterate that conclusion here and offer our reasons infra. As noted above, no determination of the navigability of Rennie Lake has been made by BLM.

Scott held that a surveyor's error in omitting an island from survey did not divest the United States of title or interpose any obstacle to surveying the island at a later time. 227 U.S. at 241-42. Scott is important because it clearly distinguished an island from land under water, such as the bed of a stream or lake. This distinction was blurred in Butler and Chandler-Dunbar, two cases relied upon by appellant.

Scott also distinguished the process by which an owner of riparian upland acquired an interest in the adjacent bed; this distinction focused upon the navigability vel non of the body of water. Quoting from Hardin v. Shedd, 190 U.S. 508, 519 (1903), Scott said:

"When land is conveyed by the United States bounded on a nonnavigable lake belonging to it, the grounds for the decision must be quite different from the considerations affecting a conveyance of land bounded on navigable water. In the latter case the land under the water does not belong to the United States, but has passed to the State by its admission to the Union. . . . When land under navigable water passes to the riparian proprietor, along with the grant of the shore by the United States, it does not pass by force of the grant alone, because the United States does not own it, but it passes by force of the declaration of the State which does own it that it is attached to the shore."

227 U.S. at 243. This distinction was made in Hardin v. Shedd because the Court feared "that there has been some misapprehension with regard to the point." 190 U.S. at 519.

In light of the distinctions set forth in Scott, we find no reason to limit the holding there to islands in navigable waters. Bode v. Rollwitz, supra at note 11, reached a similar conclusion.\footnote{Where, as here, it appears that the surveyor omitted Tract 37 from survey in 1852 because of the Surveyor General's instructions ("meander * * * all islands suitable for cultivation"), we hold that Scott applies a fortiori. It may reasonably be inferred that surveys were limited to islands upon which settlement had been, or was likely to be, made; in the absence of these conditions, Federal conveyance by patent was remote and an immediate survey was, therefore, unnecessary. See Bernard J. Gaffney, A-30327 (Oct. 28, 1965). From these conclusions, we find no basis for an inference that the United States intended to divest itself of an island omitted from survey.}

[2] NOMECO's other argument on appeal focuses upon the terms of the United States patent to the State of Michigan, dated July 27, 1891. Appellant contends that Tract 37 cannot be public land because this patent purported to convey "[a]ll of section one, containing five-hundred and thirty-four and twenty-six hundredths of an acre" (Statement of Reasons, July 29, 1987, at 4). Because the island is located entirely within sec. 1, the patent, which granted all of sec. 1 to the State, necessarily included the island, NOMECO states. The absence of any mention of the island in the survey does not alter the conclusion that it was conveyed with the balance of sec. 1. Id. at 5.

\footnote{See Morgenthaler, "Surveys of Riparian Real Property: Omitted Lands Make Rights Precarious," 30 Rocky Mt. Min. L. Inst. 19-30 (1985): "The doctrine of Scott v. Lattig was reinforced by a strikingly similar decision of the Supreme Court three years later, and was quickly recognized as settled law. A 1921 decision of the Montana Supreme Court [Bode v. Rollwitz] acknowledges the rule and correctly characterizes it as applying to navigable and non-navigable waters." (Footnotes omitted).}
In response, BLM has cited *Northern Pacific Railway Co.*, 62 I.D. 401 (1955), for the proposition that a United States patent to "all of" a particular section of land does not convey an unsurveyed island within such section. NOMECO replies by stating that *Northern Pacific Railway Co.* relied upon two cases, *Chapman & Dewey Lumber Co. v. St. Francis Levee District*, 232 U.S. 186 (1914), and *Lee Wilson & Co. v. United States*, 245 U.S. 24 (1917), that are distinguishable from the instant facts. The distinguishing factor, NOMECO observes, is the omission of a reference to "the official plats of survey" in the July 27, 1891, patent to the State of Michigan.

In *Chapman & Dewey Lumber Co.*, the Supreme Court held that a patent for "[t]he whole of the Township (except Section sixteen) * * * according to the official plats of survey of said lands returned to the General Land Office by the Surveyor General" did not convey lands erroneously meandered as a body of water and designated "Sunk Lands" on the official plats. Lands within these meander lines were excluded from survey, the plat and field notes showed. 232 U.S. at 196. The Court reasoned in this way:

Of course, the words in the patent "The whole of the Township (except Section sixteen)" are comprehensive, but they are only one element in the description and must be read in the light of the others. The explanatory words "according to the official plats of survey of said lands returned to the General Land Office by the Surveyor General" constitute another element, and a very important one, for it is a familiar rule that where lands are patented according to such a plat, the notes, lines, landmarks and other particulars appearing thereon become as much a part of the patent and are as much to be considered in determining what it is intended to include as if they were set forth in the patent. * * * The specification of acreage is still another element, and, while of less influence than either of the others, it is yet an aid in ascertaining what was intended, for a purpose to convey upwards of 22,000 acres is hardly consistent with a specification of 18,815.67 acres. * * * Giving to each of these elements its appropriate influence and bearing in mind that the terms of description are all such as are usually employed in designating surveyed lands, we are of opinion that the purpose was to patent the whole of the lands surveyed, except fractional section 16, and not the areas meandered and returned, as shown upon the plat, as bodies of water. That it is now found * * * that these areas ought not to have been so meandered and returned, but should have been surveyed and returned as land, does not detract from the effect which must be given to the plat in determining what was intended to pass under the patent. [Italics supplied.]

*Id.* at 196-97.

*Lee Wilson & Co.* involved essentially similar facts: An original plat of survey showed an area of 853.60 acres meandered as a lake, despite the fact that no lake existed. A patent was later issued to the State of Arkansas for "[t]he whole of the township except Section sixteen (16) containing fourteen thousand five hundred and sixty-five acres and three hundredths of an acre, according to the official plats of survey of the said lands returned to the General Land Office, by the Surveyor General." Upon discovering its error, the Department surveyed the 853.60 acres, and homestead entries commenced.

In response to an argument by the State's grantee "[t]hat as the selection made by the State was of Township 12, the exterior bounds of
that township became the measure of the State's title irrespective of what was surveyed or unsurveyed within those exterior lines," the Supreme Court found that this argument rested upon a contradictory assumption. 245 U.S. at 30. Such an argument "treats the designation of Township 12 as the measure of the rights conferred and immediately proceeds to exclude from view the criteria by which alone the existence and significance of the insisted upon designation (Township 12) are to be determined." 15 Id. (italics supplied).

The criteria referred to by the Court are set forth in statute,16 regulation,17 and the Department's Manual of Instructions for the Survey of the Public Lands of the United States, and embodied in the actual plat of survey and field notes. The notion that a legal description (such as Township 12 or, as here, "all of section one") owes its existence and significance to the survey on the ground 18 is further developed in United States v. Morrison, 240 U.S. 192, 199 (1916). This case held that "[p]rior to survey, the designated sections were undefined and the lands were unidentified." The impact of survey is succinctly stated by Cox v. Hart, 260 U.S. 427, 436 (1922): "A survey of public lands does not ascertain boundaries; it creates them." (Italics in original.) See also State of Oregon II, 80 IBLA 354, 91 I.D. 212 (1984).

We conclude from Lee Wilson & Co., Morrison, and Hart that a legal description, such as "all of section one," cannot be understood apart from the official plat of survey. For this reason, we hold that the omission from the United States patent to Michigan, dated July 27, 1891, of a reference "to the official plats of survey" does not remove the instant appeal from the principles stated in Chapman & Dewey Lumber Co. and Lee Wilson & Co.19

These two cases make clear that the effect of a meander line, such as that run along the margin of Rennie Lake in 1852, is to exclude absolutely from the township the area so meandered. 245 U.S. at 31. A patent for "all of section one," therefore, would not convey land meandered and returned as a body of water. 232 U.S. at 197. In the instant appeal, that land is the island at issue, Tract 37, and accordingly, we hold that this island was not conveyed to the State of

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15 Lee Wilson & Co. is frequently cited for two propositions that are relevant here and deemed "indisputable" because conclusively settled by previous decisions:

"First. Where in a survey of the public domain a body of water or lake is found to exist and is meandered, the result of such meander is to exclude the area from the survey and to cause it as thus separated to become subject to the riparian rights of the respective owners abutting on the meander line in accordance with the laws of the several States."

"Second. But where upon the assumption of the existence of a body of water or lake a meander line is through fraud or error mistakenly run because there is no such body of water, riparian rights do not attach because in the nature of things the condition upon which they depend does not exist and upon the discovery of the mistake it is within the power of the Land Department of the United States to deal with the area which was excluded from the survey, to cause it to be surveyed and to lawfully dispose of it." 245 U.S. at 29 (citation omitted).


17 43 CFR Part 9180.

18 A patentee of public land takes according to the actual survey on the ground, even though the official survey plat may not show the tract as it is located on the ground or the patent description may be in error as to the course or distance or quantity of land to be conveyed. Robert R. Perry, 87 IBLA 380 (1985); Elmer L. Lowe, 80 IBLA 101 (1984). Our research reveals two cases, in addition to Northern Pacific Railway Co., where the Department has concluded that a patent to all of a particular section did not convey unsurveyed lands therein. See State of Florida, 17 L.D. 585 (1883), and Utah Power & Light Co., 6 IBLA 79, 79 I.D. 397 (1972). See also Horne v. Smith, 159 U.S. 40, 45 (1895), a case involving an erroneous meander line, for the principle that a "patent conveys only the land which is surveyed."
Michigan at any time. BLM's action in surveying this island as public land was proper and infringed upon no rights of appellant. Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision of the State Director, Eastern States Office, is affirmed.

GAIL M. FRAZIER
Administrative Judge

I CONCUR:

FRANKLIN D. ARNESS
Administrative Judge

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Order of Dismissal

Appellant Papago Tribe of Arizona (now known as the Tohono O'odham Nation; here referred to as Papago, the name under which it filed the appeal) has appealed from final decisions by the contracting officer (hereinafter CO), dated September 11, 1984, and an Amendment thereto dated March 4, 1985. Each of these documents resulted in a bill of collection being issued to Papago, the first for $89,119, dated September 12, 1984, and the second for $229,586, dated March 15, 1985. These decisions concluded that the Bureau of Indian Affairs (BIA) had made payments to Papago under the contract for invoiced costs that were disallowed in a subsequent audit, and the bills of collection sought reimbursement for those costs.


(f) Any right of action or other remedy (other than those relating to a criminal offense) relating to any disallowance of costs shall be barred unless the Secretary has given notice of any such disallowance within three hundred and sixty-five days of receiving any required annual single agency audit report or, for any period covered by law or regulation in force prior to enactment of the Single Agency Audit Act of 1984 (chapter 75 of title 31, United States Code), any other required final audit report. [Italics supplied.]

The audit report disallowing the costs is dated June 6, 1980. The first CO decision sustaining the disallowance is dated September 11, 1984, far more than 365 days after the date of the report. Papago insists that subsection (f) applies to this case and requires dismissal on the ground of the running of the limitation period expressed therein.

BIA opposes dismissal on two bases: (1) There was no “required” audit report in this case and (2) construing the new subsection as Papago does requires a retrospective application thereof, something that generally, and specifically in the case of this statute, is not allowed.
BIA further contends that "required" as used in the portion of subsection (f) referring to the pre-Single Agency Audit Act of 1984 period (hereinafter the Audit Act) essentially means the same thing as "required" as used in the Audit Act, i.e., if a pre-Audit Act report by the contractor, is not "required" by law or regulation, then the limitations period for instituting an action based thereon, as expressed in the new subsection, does not apply. BIA further posits that this audit report was not "required" under any construction of the term because the audit activity was "conducted by the Office of the Inspector General in his [sic] discretion" (BIA Response at 4; italics in original).

We do not read "required" so narrowly. The audit was indeed conducted by the Office of Inspector General but at the request of the CO (Audit Report at 1, Appeal File (hereinafter AF), Exh. 16). The authority under the contract for the CO to "require" an audit is very plain and is found in paragraph 304 of the contract's General Provisions (AF, Exh. A). The CO is the Government's designated agent to negotiate the terms of a contact, to bind the Government by his signature, and thereafter to modify or enforce the terms of the contract.

Clearly, under paragraph 304 of the contract, the CO could "require" an audit, and if we read "required" in the subsection to modify the words closest to it, i.e., "final audit," rather than "report," then the subsection would apply because this was a report of a final audit that the CO could and did "require" under the contract. Even if "required" modifies "report," we believe the Amendments as a whole, considered in the context of this contract, in particular paragraph 304, allow no other conclusion than that this report was a "required" one as to which the new subsection was intended to apply. (See Sutherland Stat. Const. § 46.05 (4th ed.).)\(^1\)

Regardless of our conclusion on that issue, we would still have to deny Papago's motion to dismiss on the basis of the new subsection if BIA were correct in its other argument that the Amendments are properly read to apply only prospectively. The BIA argument begins with the basic tenet of statutory construction that a statute applies prospectively only, unless there is a clear, explicit expression that the legislature intended retrospective application, or unless that intent can be concluded as a matter of necessary implication by the terms actually used (BIA Response at 3). That is doubtless a correct statement of the rule on prospective/retrospective application of a statute; but, applying that rule to this case, we reach a result different from that urged by BIA.

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\(^1\) BIA has cited legislative history that in some respects, but not all, supports its version of the meaning of "required." We believe, though, that the better rule is not to resort to extrinsic aids to construction lightly when statutory language is plain. (See Sutherland Stat. Const., § 48.01 (4th ed.).) Here, "required" is a clear enough term and the legislative history cited is ambiguous enough that we choose not to consider this argument. We are further supported in this position by our view of the spirit of the Amendments as a whole, as mentioned in the text, and that view is actually bolstered by the legislative history BIA wishes us to consider.
BIA’s argument on this issue consists essentially of stating the rule and then claiming that it applies to this statute. It offers no explanation of the underscored language in the statute quoted above. We are not told why the reference to a period more than 4 years prior to the passage of the statute being construed does not amount to the “necessary implication” which BIA says establishes one of the exceptions to the general rule of a statute’s prospective application only.

Although BIA’s arguments do not resolve the issue, we are not entirely convinced by the plain meaning of the words alone that the “necessary implication” is present. When the language under scrutiny does not present sufficient clarity to decide definitively on its meaning, however, it is permissible to look at other parts of the same statute as an aid and, if thereafter sufficient clarity is still absent, to consider extrinsic aids like legislative history. Actually, as expressed in our earlier discussion on the “required” issue, the better rule in any event is to consider the entire statute and its intent first in determining whether the provision is sufficiently clear to apply its terms as stated, and not to make resort to the rest of the statute contingent solely on the absence of clarity in the provision itself. In fact, we have done that here but have separated consideration of the pertinent language from the rest of the statute for analysis. When we consider each of these aids, we discover that each separately and together leads us to the conclusion urged by Papago.

In the section following the section containing subsection (f), the Amendments also add a new section 110 to 93-638. Among the provisions of new section 110 are the following:

(c) The Equal Access to Justice Act [citation omitted] shall apply to administrative appeals by tribal organizations regarding self-determination contracts.

(d) The Contract Disputes Act [citation omitted] shall apply to self-determination contracts.

(e) Subsection (d) of this section shall apply to any case pending or commenced after March 17, 1986, before the Boards of Contract Appeals of the Department of the Interior.

The effect of these new provisions is to make certain cases subject to the Contract Disputes Act (CDA) and derivatively to the Equal Access to Justice Act (EAJA), and clearly to do that retrospectively. The retrospective period for applying the new provisions began March 17, 1986, the date on which the Board issued an order in this same case (Papago Indian Tribe of Arizona, IBCA-1962, Mar. 17, 1986, 86-2 CCH ¶ 18,777). The order was occasioned by a Papago motion for us to dismiss the case for lack of jurisdiction, and in it we announced, among other things, that the CDA does not apply to 93-638 contracts, relying on a Claims Court case to the same effect. The Congressional action in new section 110 effectively overruled that decision and, by doing so retrospectively to the date of the order announcing our rule, provided fairly persuasive evidence that the Congress had this very case in mind.
as it enacted the retrospective provision. This legislative history removes all reasonable doubt that the Congress had the Papago case in mind as it enacted the statute:

In Appeals of Papago Indian Tribe of Arizona,\(^{23}\) the Interior Board of Contract Appeals ruled that contract disputes before the Board involving self-determination contracts were not subject to the Contract Disputes Act. The Papago decision extended an earlier ruling in Busby School of the Northern Cheyenne Tribe v. United States\(^{24}\) that the Contract Disputes Act did not apply to self-determination contractors' claims before the Court of claims. If given general application, these rulings may have the effect of rendering self-determination contractors who are prevailing parties in such proceedings ineligible to seek an award of legal fees under the Equal Access to Justice Act under which “adversary adjudications” at the administrative level subject to the Act are defined in part by reference to proceedings under the Contract Disputes Act. \(\text{[Other footnotes omitted.]}\)

Section 110(c), then, reinstates the law as it existed prior to the Busby and Papago decisions, placing self-determination contractors on an equal footing with other federal contractors by allowing them to make application for an award of legal fees under the Equal Access to Justice Act when they are the prevailing party in an agency board of contract appeals proceeding involving a contract under the Indian Self-Determination Act.

The proposed new section 110(e) would make the amendments at the new section 110(c) and section 110(d)(1) retroactive for a limited class of cases, to protect those self-determination contractors who were deprived of the protection of the Contract Disputes Act (and derivatively the Equal Access to Justice Act) by the Papago decision as to proceedings pending before the Interior Board of Contract Appeals involving Indian Self-Determination Act contracts as of March 17, 1986 (or subsequently), the date the Interior Board of Contract Appeals first applied the Busby ruling to such board proceedings in the Papago decision.

The provision for such limited retroactivity is appropriate to ensure that those Indian Self-Determination Act contractors who were adversely affected by the Papago ruling will be accorded treatment equal with that originally intended by the Congress and as provided for in this amendment. The same rationale gave rise to the limited retroactivity provisions provided in the 1985 Equal Access to Justice Act amendments.

\(^{23}\) IBCA-1962 and 1966 (March 17, 1986).
\(^{24}\) 8 Cl. Ct. 596 (1985).


In light of the clear retrospective intent of new section 110, and the spirit and context of the entire statute, we believe that the new section 106 language also has sufficient clarity for us to conclude that the language referring to a 4-plus year-old period necessarily applies retrospectively.

As further support, we also note the following legislative history on new section 106 itself:\(^2\):

\(^2\) This is the same passage BIA wanted us to consider in the context of the “required” issue. For the reasons that we did not find this passage convincing on that issue, see footnote 1.
The new Section 106(e) would provide a time limit of 365 days on disallowing contract costs after receipt of the annual single agency audit report. This time limitation of 365 days applies also to any required audit reports submitted by tribal organizations prior to enactment of these amendments. While it is important to review audit reports, it is not in the interests of tribes or the Federal agencies to disallow costs and enforce actions against tribes years after the submission of a final audit report. [Italics supplied.]


By referring to the period “prior to the enactment of these amendments” and decrying the passage of “years after the submission of a final audit report” before the Government initiated an action, the Congress made clear that it had the type of case before us in mind in providing the new limitations period.

Based on the foregoing, we grant Papago’s motion to dismiss on the ground that the collection actions by the Government for the disallowed costs are barred by the time limitation provided in the statute.

RUSSELL C. LYNCH
Chief Administrative Judge

WE CONCUR:
WILLIAM F. McGRAW
Administrative Judge
BERNARD V. PARRETT
Administrative Judge

APPLICATION FOR ATTORNEY FEES, R & R ENTERPRISES

IBCA-2664-F Decided: June 14, 1990

Contract No. CC-9029-82-002, National Park Service.

Granted in part.


An appellant may be a prevailing party even if its award in the underlying litigation is based on contract principles unrelated to the theory of the case propounded by its attorney. Where only one claim is involved, the appellant can be a prevailing party for the purposes of the EAJA regardless of the basis of the Board’s award.

The test of substantial justification of the Government’s position for EAJA purposes is not its traditional view or the consistency of its position but how fair and reasonable it was in its evaluation of the appellant’s claim.


Reasonable and necessary expenses of an attorney incurred or paid in preparation for the adjudication of the specific case before the Board, which expenses are those customarily charged to the client where the case is tried, are allowable expenses under the EAJA. The quantum and method of proof of each allowable expense is discretionary with the Board.


Expenses incurred before a contracting officer’s decision denying a claim, and therefore prior to the appeal, may be awarded under the EAJA if they are primarily related to, intended for, and necessary in the subsequent adversary adjudication, rather than intended primarily in support of the claim initially presented to the contracting officer.

APPEARANCES: Joseph J. Connolly, Esq., Attorney at Law, Lynnwood, Washington, for Appellant; C. Richard Neely, Esq., Department Counsel, Portland, Oregon, for the Government.

OPINION BY ADMINISTRATIVE JUDGE PARRETTE

INTERIOR BOARD OF CONTRACT APPEALS

Background

This is an application for attorney fees and expenses under the Equal Access to Justice Act (EAJA or Act), 5 U.S.C. § 504 (Supp. IV 1986), by R & R Enterprises (R & R or applicant), the appellant in the underlying case by the same name, which was decided by the Board on March 24, 1989, 26 IBCA 89, 96 I.D. 148, 89-2 BCA ¶ 21,708, and affirmed on reconsideration July 6, 1989, 26 IBCA 249, 96 I.D. 313, 89-3 BCA ¶ 22,043.

In R & R, the Board awarded damages to appellant by jury verdict on the grounds that it had been damaged in its ability to operate a resort as a concessioner of the National Park Service (NPS) when NPS decided to replace the water and sewer system of the resort without the knowledge of, and without sufficient notice to, appellant, causing a loss of business and good will for more than a 2-year period just as R & R was initially attempting to reopen and revitalize the resort as a family business.

Amount of Fees and Expenses Claimed

In the present application, R & R originally sought attorney fees of $27,045 (out of the $31,110 billed to it), attorney expenses of $3,352.05, and additional expenses of R & R’s manager, Thomas Roberts, of $3,874.30, for a total of $34,271.35 (stated in the claim as $34,588.85).
The Government opposed all fees and expenses incurred before July 16, 1987, the date of the contracting officer's (CO's) decision, on the ground that they were not incurred in connection with the adversary adjudication before the Board, citing our decision in *Northwest Piping, Inc.*, IBCA-2642-F, 26 IBCA 351, 352, 90-1 IBCA ¶ 22,446, which denied prelitigation fees on the ground that the parties were not then before the Board and noted that adversary adjudication normally begins with the CO's decision denying the claim. The Government also opposed any fees or expenses personally incurred by Mr. Roberts as not being compensable under the Act.

The applicant agreed with the Government's contentions as to Mr. Roberts' expenses, and generally concurred as to its pre-July 1987 attorney fees and expenses, but it contends that the amounts spent for photographs while the construction was going on are proper. Applicant's revised claim is thus for 162.6 attorney hours at $75 per hour, equaling $12,195, and for revised expenses, including photographic expenses, of $3,049.75, for a new total claim of $15,244.75, the amount of the application now before us.

**Government's Opposition**

In addition to its challenge of applicant's monetary amounts, the Government opposes the application primarily on two grounds: First, the Government contends that appellant did not prevail upon its claims as submitted since they were for lost profits and for collateral damages, claims that were rejected by the Board, which made its award by jury verdict pursuant to language contained in the concession contract itself.

Second, the Government alleges that its position in the underlying matter was reasonable and therefore substantially justified under the EAJA because the appeal was a case of first impression before the Board; NPS had never considered the Contract Disputes Act (CDA) to be applicable to concession contracts; the amount of appellant's claims had varied during the course of the adjudication; and appellant had never asserted a claim pursuant to the clause of the contract under which the Board had made the award.

We will consider the "prevailing party" issue first, since if the applicant does not fall within the meaning of that term, it is not eligible for EAJA relief.

**Discussion**

[1] *Whether Appellant was a Prevailing Party*

The Government accurately quotes the rule set forth by the Supreme Court in *Hensley v. Eckerhart*, 461 U.S. 424, 433 (1983), that an applicant will be considered a prevailing party "for attorney's fees purposes if they succeed on any significant issue in litigation which
achieves some of the benefit the parties sought in bringing suit.”

However, the Government infers from that principle that a party
cannot be said to prevail unless it achieves its success on the theory of
the case actually presented to the Board. We do not agree. Nor do
other courts and boards. As stated in Harrell Patterson Contracting,
Inc., ASBCA No. 30801, et al., 88-1 BCA ¶ 20,510 at 103,685: “It is not
necessary that an applicant have 100% success to be considered a
prevailing party. Significant success which achieves some of the
benefits sought is considered sufficient. Hensley v. Eckerhart, 461 U.S.
424 (1983).”

In other words, how an appellant succeeds in winning a substantial
portion of the relief it sought is not as important as the fact that it did
succeed in winning. This view is consistent with the basic purpose of
the EAJA, which the Supreme Court has recognized is “to diminish the
deterrent effect of seeking review of, or defending against,

Here, appellant’s claim in the underlying appeal was for a total of
$64,894, and the Board awarded it $50,000 by jury verdict, clearly a
significant portion (77%) of its claim.

We therefore conclude that an appellant can be a prevailing party
even if its award in the underlying litigation is based on contract
principles that were unrelated to the theory of the case propounded by
its attorney. And where only one underlying claim is involved, we
think the appellant can be a prevailing party for the purposes of the
EAJA regardless of the technical basis of the Board’s award. Thus, the
Government’s contention that the applicant was not a prevailing party
under the Act is without merit.

[2] Whether the Government’s Position was Substantially Justified

Next, the Government contends that its position was substantially
justified, for the reasons set forth above. It particularly emphasizes
NPS’ long-held belief that concession contracts were not subject to the
CDA but, rather, were mere licenses to do business on Park property;
that this was a case of first impression; and that no claim was ever
made under the appropriate provisions of the concession contract, as
ultimately decided by the Board.

We do not find these arguments persuasive. The salient facts in the
case were all in favor of appellant, inasmuch as NPS had knowingly
and deliberately entered into a concession contract with appellant in a
situation where other concessioners had previously failed (partly for
reasons undisclosed to appellant); where a major water and sewer
project had already been planned and was expected to be funded
shortly; and where NPS was fully aware that appellant’s resources
were only marginally adequate even if everything went precisely as
appellant had projected. Then, when the inevitable occurred, and the
water and sewer construction project literally destroyed appellant’s
business, NPS failed even to consider reimbursing appellant under the
contract, but merely offered token damages ($3,218) based on the
admitted torts of its construction contractor.
We think the test of substantial justification of the Government's position for EAJA purposes ought not be an agency's traditional view of its contractual arrangements or the consistency of its internal position but, rather, how fair and reasonable its position was in relation to the nature and scope of the appellant's claim, and whether it made a realistic effort to evaluate the appellant's claim under the provisions of its contract, whether the agency thought the contract was subject to the CDA or not. That did not happen here. Thus, we think the actions taken by NPS in forcing the appellant to resort to adversary adjudication were clearly unjustified.

[3] What Fees and Expenses are Allowable

By far the most interesting issues presented by this application, however, have to do with what litigation expenses should, and should not, be allowed. The parties are correct that travel and related expenses incurred by a non-lawyer principal of the appellant are not allow able under the EAJA. See, e.g., M. Bianchi of California, ASBCA No. 26362 et al., 90-1 BCA ¶ 22,369 at 112,403-04; James W. Sprayberry, IBCA-2298-F, 89-2 BCA ¶ 21,797. They are also correct that fees and expenses incurred before the issuance of the CO's final decision are generally not allowable. Northwest Piping, supra.

However, the Government further alleges that expenses incurred by appellant's counsel in consulting an expert in Government contract law, parking expenses, photocopying expenses, expenses incurred in computerizing certain data, the costs of photography and binders relating to the NPS construction project (all incurred before the CO's decision), express mail costs, and all mail costs generally, are not recoverable. In response, appellant has deleted the costs of the computer conversion but has retained virtually all of the remaining costs.

What the Government has not challenged is (a) whether all of these costs were in fact incurred by appellant's counsel, rather than by appellant, and (b) if so, whether they were all separately billed to appellant rather than being included as part of the law firm's overhead. Since the application contains an affidavit by appellant's managing partner that he has read the attorney-prepared application and that the contents thereof are true, correct, and complete; and since he initially billed his own expenses in a separate exhibit; we will assume that all of the costs objected to by the Government were in fact incurred by appellant's attorney and billed to it separately. That hurdle out of the way, we will now consider the eligibility of the expenses set forth.

Like the Constitution, the EAJA is in places almost too succinct, and the courts and boards are still in the process of divining its intent. It may be said, however, that wide ranges of attorney expenses that are reasonable and necessary in connection with the adversary adjudication of the particular case before the particular tribunal are
increasingly being allowed. The best recent guidance on the subject by the Court of Appeals for the Federal Circuit (CAFC) is to be found in Oliveira v. United States, 827 F.2d 735, 743-44 (Fed. Cir. 1987), in which the CAFC overturned a decision by the Claims Court that had refused to award an applicant ordinary attorney expenses, such as photocopying, printing and binding of briefs, use of telephone, postal, and overnight delivery services. The court said the examples of legal expenses set forth in the EAJA are only examples and not an exclusive listing. Rather, expenses may be awarded that are (827 F.2d at 744):

* * * reasonable and necessary expenses of an attorney incurred or paid in preparation for trial of the specific case before the court, which expenses are those customarily charged to the client where the case is tried. The quantum and method of proof of each allowable expense is discretionary with the trial court. In contrast, expenses of an attorney that are not incurred or expended solely or exclusively in connection with the case before the court, or which expenses the court finds to be unreasonable or unnecessary in the pending litigation, cannot be awarded under the EAJA.

At least two other Federal circuit courts have subsequently stated, citing Oliveira, that the examples of allowable expenses mentioned in the EAJA are just that, examples, and that attorney expenses such as telephone, postage, travel, and photocopying costs (which are also allowed by one or more other circuit courts), air courier, and attorney travel expenses may be allowed. See Kelly v. Bowen, 862 F.2d 1333, 1335 (8th Cir. 1988), and Jean v. Nelson, 863 F.2d 759, 776-78 (11th Cir. 1988).

Under the circumstances of the case before us, where appellant was in one (rural) location, its attorney was in another (suburban) location, NPS personnel monitoring the concession contract were in at least three other (rural and urban) locations, and Government counsel was in still a fourth location, we see nothing unreasonable in awarding the amounts claimed for attorney parking fees, mailing costs, and similar expenses, incurred subsequent to the CO’s decision, with the understanding that they were separately billed to the client, as the applicant’s affidavit and the attorney’s expense exhibits clearly indicate. However, it should also be noted that these expenses were relatively de minimis. Had they been greater, we would have required a greater degree of proof that they are customarily billed separately by attorneys in the area in which the attorney was located.

[4] Whether Pre-CO Decision Expenses are Allowable
But what of the photographic expenses, all of which were incurred not only many months prior to the CO’s final decision, but also substantially before the claim was even submitted to him? We have decided to allow them.

In responding to the Government’s objections, the applicant merely states that the photographic expenses “are a necessary element in the presentation of Appellant’s case and a mandatory part of the hearings procedure in both case preparation and presentation.” We think the applicant substantially understates its case.
In Item 47 of our statement of General Facts in the underlying decision, 89-2 BCA at 109,142-43, we noted that “the 258 pictures introduced into evidence make abundantly clear the extent of the chaos that had resulted” to the resort from NPS’ water and sewer construction project. Those photographs, in fact, were virtually indispensable to the Board in weighing the divergent opinions of appellant’s and the Government’s witnesses concerning how extensive a disruption the construction project caused. The fact that they were taken during the construction period, which obviously occurred before any claim was asserted, seems essentially immaterial. Had appellant waited until after the CO’s denial to take its pictures, there would have been no construction pictures to take: By that time, the work had been finally completed, and little or no disruption of resort operations would have been seen.

Moreover, it is evident that even at that early date—i.e., the period of actual construction—appellant and its attorney were already seriously concerned by the Government’s position that the construction was not, and would not be, any serious obstacle to the resort’s current operations, but was, rather, vital to its future success. The photographs appellant’s lawyer took (or had taken) were obviously not really needed for the claim that was later presented to the CO: His reliance would essentially be on the reports and logs of the construction project engineer, inspector, and contractor, and of the local Park Superintendent’s office, which monitored both the concession contract and the construction contract. NPS apparently did not want, need, or even take seriously the photographs that appellant took to show that his concession was about to become insolvent because of the disruption to customer traffic that the construction contract caused.

In summary, we conclude that the 258 photographs at issue were taken precisely in contemplation of the subsequent adversary adjudication, because appellant and his lawyer were already convinced at the time they were taken that NPS had no great concern for the fate of the resort or its proprietors and, further, that litigation in some forum would be ultimately necessary if they were to recover anything for the losses caused by the construction project. Accordingly, we find that the costs of the photographs were reasonable and necessary expenses incurred for the purpose of an appellate proceeding, and we conclude they are allowable.

Succinctly stated, we hold that expenses incurred before a CO’s decision denying a claim, and therefore prior to the appeal, may nevertheless be awarded under the EAJA if they are primarily related to, intended for, and necessary in connection with the subsequent adversary adjudication of the appeal, rather than intended primarily in support of the claim initially presented to the CO.

We are aware that few, if any, courts or boards have had occasion to consider this issue. They therefore have tended, as this Board has, to
identify the *period* in which the expense was incurred, rather than its purpose, as controlling. *See, e.g.*, *Keyava Construction Co. v. United States*, 15 Cl.Ct. 135, 138 (1988), in which the court stated that the "EAJA does not entitle a prevailing party to recovery of fees and expenses incurred during prosecution of [a] claim before the contracting officer." But we read this language, as well as our own language in *Northwest Piping*, *supra*, to mean fees and expenses incurred for the purpose of prosecuting a claim before a CO, not fees and expenses (if any) incurred because of the ultimate probability of an appeal.

We note that the Armed Services Board, which has paved the way in establishing many of the principles applicable to EAJA cases, has briefly touched on this subject in some of its recent decisions, although it has apparently never had to deal with our precise situation. Its views are perhaps best summarized in *Building Services Unlimited, Inc.*, ASBCA No. 33283, 88-2 BCA ¶ 20,611 at 104,152-53, where Administrative Judge Riismandel notes in part: "[F]ees incurred prior to receipt of the contracting officer’s final decision may be reimbursed upon a specific showing that they were incurred in connection with the adversary adjudication."

If that is true, and we think it is, then we see no reason why the EAJA might not be equally applicable to fees and expenses incurred at an even earlier time, provided they were primarily appeal oriented and not intended for the prior proceeding. However, we think there continues to be a prima facie presumption that attorney fees and expenses incurred before the CO’s final decision were incurred in connection with the CO submission and not in connection with the proceeding before the Board. The burden of proving otherwise is on the applicant.

In summary, we will allow the photographic expenses incurred in this case. However, there are other pre-CO decision expenses in the amount of $282 which applicant does not sufficiently justify, and we also disallow all expenses that are identifiable as related to appellant’s contention that the Government was liable for the allegedly consequential damages incurred when its principal had to sell an unrelated income property in order to raise money for the resort’s operations. These costs amount to $300. Similarly, applicant’s attorney identifies 5 hours of legal time spent in connection with its income property, which we disallow, in the amount of $375.

Adding the $12,195 in legal fees, less $375 disallowed, or $11,820, to the $3,352 claimed in expenses, less the $582 disallowed, or $2,770, produces a total of reimbursable fees and costs in the amount of $14,590.
Accordingly, the applicant is awarded $14,590 in legal fees and expenses, as set forth above.

BERNARD V. PARRETTE
Administrative Judge

WE CONCUR:

WILLIAM F. MCGRAW
Administrative Judge

G. HERBERT PACKWOOD
Administrative Judge

APPEAL OF GARDNER ZEMKE CO.

IBCA-2626

Contract No. 6-CC-30-04240, Bureau of Reclamation.

Government Motions For Summary and Appellant's Cross-Motion for Summary Judgment Denied.


A Government motion for summary judgment filed in connection with a contractor's unilateral mistake in bid claim is denied where the Government fails to show that the release language included in a modification to the contract (relied upon by the Government for its affirmative defenses of abandonment, novation, release and accord and satisfaction) either expressly or by implication refers to any mistake in bid claim and where the Board finds that an affidavit filed by appellant raises a genuine issue of material facts as to the intention of the parties at the time the modification containing the release in question was negotiated and executed. The Government's motion for summary judgment is also denied on the alternative ground that subsequent to the execution of the release the parties showed by their conduct that they never considered the release as constituting an abandonment of the mistake in bid claim.


The Board denies a Government motion for summary judgment for the failure of the appellant to state a claim for relief with respect to its unilateral mistake in bid claim, where the Board finds (i) that the Government has failed to furnish any information as to what actions the contracting officer took with respect to his bid verification duties upon the opening of bids; (ii) that in the absence of such information it is not possible to determine the reasonableness of the contracting officer's actions; and (iii) that in ruling upon a motion for summary judgment all inferences are to be drawn in favor of the party against whom the motion for summary judgment is advanced.

An appellant's cross-motion for summary judgment is denied where the Board finds
(i) that the motion is predicated upon a particular application of the law of warranties;
(ii) that the principal grounds for the motion appears to be based upon the provisions of the Uniform Commercial Code; (iii) that all of the cases cited which apparently involve the Uniform Commercial Code are state cases; (iv) that in regard to such cases the appellant has failed to show that the principles apparently enunciated therein have been endorsed by the Federal courts so as to become a part of what has been described as the general Federal common law; (v) that the state cases so relied upon have not been shown to be dispositive of the question presented; and (vi) that appellant has failed to show that it is entitled to summary judgment as a matter of law.


OPINION BY ADMINISTRATIVE JUDGE McGRAW

INTERIOR BOARD OF CONTRACT APPEALS

Gardner Zemke Electrical and Mechanical Contractors (hereinafter GZ/contractor/appellant) has timely appealed from the decision of the contracting officer (CO) dated December 16, 1988, which denied GZ's request for reformation of the contract to correct a unilateral mistake in bid, after award of contract, and which made a downward adjustment of $225,195.63 for the calculated load losses in excess of the warranted load losses. In support of the decision reached, the CO states: "[T]he contractor's alleged mistake does not constitute a justifiable basis for contract reformation * * * nor was the mistake so apparent as to have charged the Contracting Officer with notice of probability of the mistake [1] at the time of contract award" (Appeal File (AF), tab 15, at 8).2

In the complaint GZ requests relief "based on (1) contract reformation to correct a mistake in bid; (2) unenforceability of the 'liquidated damages' provision as a penalty; and (3) waiver of right to seek damages because the Bureau effectively denied Gardner Zemke an opportunity to repair or replace the allegedly unsatisfactory transformers as was its right under the contract" (Appellant's Memorandum In Opposition to Motion to Dismiss at 1-2).

1 The Federal Acquisition Regulations (FAR) provides:
"After the opening of bids, contracting officers shall examine all bids for mistakes. In cases of apparent mistakes and in cases where the contracting officer has reason to believe that a mistake may have been made, the contracting officer shall request from the bidder a verification of the bid, calling attention to the suspected mistake. If the bidder alleges a mistake, the matter shall be processed in accordance with this section 14.406. Such actions shall be taken before award." (FAR 14.406-1).

2 The CO noted that mistakes in bid alleged after award are governed by FAR 14.406-4, which provides that determinations respecting rescission and reformation of the contracts awarded are to be made "only on the basis of clear and convincing evidence that a mistake in bid was made" and that "it must be clear that the mistake was (1) mutual or (2) if unilaterally made by the contractor, so apparent as to have charged the contracting officer with notice of the probability of the mistake" (FAR 14.406-4(c)).
Simultaneously with the submission of its answer, the Bureau of Reclamation (Bureau) filed a motion to dismiss the instant appeal on the grounds of abandonment, novation, release, accord and satisfaction, lack of timely notice of the mistake in bid claim and failure to state a claim for which any relief is available. After GZ filed an opposition to the motion to dismiss, the Bureau urged the Board to treat its motion as a motion for summary judgment. Appellant filed an opposition to the Bureau's motion for summary judgment, together with a cross-motion for summary judgment, accompanied by an affidavit from an officer of the company involved in negotiating and executing the modification relied upon by the Bureau for the affirmative defenses of abandonment, novation, release and accord and satisfaction. The Bureau filed a motion to strike the affidavit submitted by GZ as in violation of the parol evidence rule. Thereafter, in response to an Order of the Board, both parties filed additional memorandums in support of their respective positions. With a view to abbreviating the references to the memorandums so filed, the Board will refer to the memorandums by identifying the party filing the same, giving the date thereof and adding the appropriate page references.

Findings of Fact

1. Contract No. 6-CC-30-04240 and the related solicitation (No. 6-SI-30-04240) called for the completion of the Brady, Picacho, and Red Rock pumping plants and switchyards (Complaint ¶ 1). The solicitation called for bids to be submitted on a total of 538 bid items of which three items involved warranted characteristics. For the required work, GZ submitted a low bid of $12,892,194 and was awarded the instant contract in that amount on June 27, 1986 (AF, tabs 2, 3). Notice to proceed was received by the contractor on July 23, 1986, thereby establishing the original completion date of November 2, 1989 (AF, tab 15 at 2).

2. The contract required GZ to furnish and install two 115-kilovolt (KV), three-phase power transformers at each of three plant and switchyard locations. For Item 149 (the two transformers for the Brady pumping plant and switchyard) GZ submitted a lump sum bid of $470,819 (AF, tab 3 at F-1 and F-10 (revised)); for Item 331 (Picacho pumping plant and switchyard), GZ's lump sum bid was in the amount of $500,000 (AF, tab 3 at F-15) (revised) and F-24 (revised)); and for Item 510 (Red Rock pumping plant and switchyard), the lump sum bid of GZ was in the amount of $500,000 (AF, tab 3 at F-29 (revised) and F-38 (revised)).

3. The solicitation and resulting contract called for the characteristics of all of the 115-KV transformers to be warranted. The language employed in warranting the characteristics for Item 149,
together with the figures, inserted in the Schedule by GZ, reads as follows:

**SCHEDULE-PART A**

**WARRANTED CHARACTERISTICS**

Each bidder warrants that the performance of each transformer, in schedule item 149, will be at least as good as stated below, with rated voltage and frequency applied to each winding, see the clauses in subsection 1.4 entitled “Comparison of bids,” and “Failure to Meet Performance Warranties.”

| Item 149 |
|-----------------|--------|
| No-load losses, kilowatts | * 19.0 |
| Total losses, at the loading condition of: |
| 24,500-kilovolt ampere, including fan motor power requirements, and at a temperature of 85° C | * 75.0 |

* Rounded off to the nearest tenth of a kilowatt.

Losses measured at a different loading than that which is required, but extrapolated to the required loading will not be acceptable.

Failure to furnish the required appropriate values above will result in an incomplete bid which will not be considered.

(AF, tab 3 at F-1 and F-14).

4. The contract included the following clause:

**I.4.17 COMPARISON OF BIDS–RECLAMATION (DEC 1984)**

(a) The following factors in addition to that of the offered price will be used in computing amounts for comparison of bids:

1. **Losses.–** For each transformer, the losses will be evaluated on the basis of the warranted kilowatt losses and for voltage, frequency, and loading conditions as stated under “Warranted Characteristics.” The evaluated losses will be determined by multiplying the warranted kilowatt losses by the following rates:

<table>
<thead>
<tr>
<th>Losses</th>
<th>Rate</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>No-load losses</td>
<td>..........................</td>
<td>$1,760</td>
</tr>
<tr>
<td>* Load losses</td>
<td>..................................</td>
<td>$663</td>
</tr>
<tr>
<td>Total losses</td>
<td>..................................</td>
<td>$1,889</td>
</tr>
</tbody>
</table>

* The load losses will be considered as the difference between the warranted total losses and the warranted no-load losses both as stated under “Warranted Characteristics.”

The total evaluated losses for the transformers will be added to the prices offered for items 149, 331, and 510.

(AF, tab 18 at I-26).

5. The contract also includes the following clause:

**I.4.18 FAILURE TO MEET PERFORMANCE WARRANTIES–RECLAMATION (OCT 1981)**

If the Government elects to accept equipment which does not meet performance warranties, as determined by factory test, field test, or operation under service conditions, appropriate adjustment will be made of the contract price for such

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The language used by GZ to warrant the characteristics for Item 331 (Picacho) refers to that item and to Schedule-Part B for which it showed no-load losses, kilowatts of 21.0 and total losses (26,500 kilovolt ampere) of 82.0 (AF, tab 3 at F-15 (revised) and F-28). In warranting the characteristics for Item 510 (Red Rock) GZ refers to that item and to Schedule-Part C for which it also showed the same figures to be warranted for no-load losses, kilowatt (21.0) and for total losses (26,500 kilovolt amperes) of 82.0 (AF, tab 3 at F-29 (revised) and F-42). The characteristics warranted by all four bidders who responded to the solicitation are shown in Finding 9.
equipment: Provided, That no such adjustment will be made until after the Contractor has been given an opportunity to repair or replace defective equipment, wherever practicable. Because of the impossibility of determining the actual loss to the Government due to such failure to meet warranties, the following adjustment of price in the form of liquidated damages shall be final and conclusive with respect to both the Contractor and the Government, and neither shall have any claims against the other on any other basis whatsoever:

(a) A total monetary value shall be established for the actual losses of the transformers on the same basis as described in the provision in the clause of subsection I.4.16 [4] entitled “Comparison of Bids” for the warranted losses, assuming that the actual full-load copper loss is equal to the difference between the actual total losses and the actual no-load loss. In the event that this total monetary value exceeds the total monetary value calculated for the warranted losses and the full-load copper loss calculated as above, the price of the transformers will be reduced after applying price adjustment by the amount that the total monetary value of the actual losses exceeds the total monetary value of the warranted losses and the full-load copper loss calculated as above.

If the above adjustments result in a reduction in the contract price in an amount in excess of the amount due the Contractor, the Contractor shall promptly refund to the Government the amount of such excess, and the Contractor and the Contractor's sureties shall be liable for the amount thereof.

(AF, tab 18 at I-26).

6. After the opening of bids on May 21, 1986, the bids received were reviewed by a Bid Opening Board which noted (i) that four bids had been received at bid opening time; (ii) that one of the bidders (V.O. Contracting Co.) had not bid on numerous schedule items and, consequently, appeared to be disqualified by reason of a requirement of the solicitation that bids be submitted on all items; and (iii) that GZ was the apparent low bidder. The Bid Opening Board recommended that GZ be required to confirm its bid and upon confirmation and establishment of legal sufficiency of the bid that award be made to that company (AF, tab 1 at 1, 4).

7. The Bid Opening Board undertook to make a comparison of the bids received from the three low bidders, as is shown below:

<table>
<thead>
<tr>
<th>Bidder</th>
<th>Amount of bid</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total for Parts A, B, and C of the Schedule</td>
<td>$12,892,194.00</td>
</tr>
<tr>
<td>Adjustment for foreign materials</td>
<td>612.00</td>
</tr>
<tr>
<td>Adjustment for warranted characteristics</td>
<td>1,114,690.00</td>
</tr>
<tr>
<td>Amount for comparison</td>
<td>$14,007,496.00</td>
</tr>
<tr>
<td>Interect Constructors, Inc.</td>
<td>$14,405,130.11</td>
</tr>
<tr>
<td>Adjustment for foreign materials</td>
<td>0.00</td>
</tr>
</tbody>
</table>

* By amendment No. 3 to the solicitation, the erroneous reference to the clause number “I.4.16” was corrected to “I.4.17” (AF, tab 22 at 3).
Bidder | Amount of bid
--- | ---

Adjustment for warranted characteristics ............................................. 1,616,431.00

Amount for comparison ................................................................. $16,021,561.11

C.R. Fedrick, Inc .................... .................. $18,139,911.00

Adjustment for foreign materials .................................................. 0.00

Adjustment for warranted characteristics ........................................ 1,616,431.00

Amount for comparison ................................................................. $19,756,342.00

(AF, tab 1 at 2).

8. A comparison made by the Bid Opening Board of the three low bids received with the engineer’s estimate and with the program estimate shows the following:

<table>
<thead>
<tr>
<th>Bidder</th>
<th>Amount of Bid</th>
<th>% Engr. Est.</th>
<th>% Prog. Est.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. The Gardner-Zemke Company</td>
<td>$12,892,194.00</td>
<td>69.9%</td>
<td>53.7%</td>
</tr>
<tr>
<td>2. Interect Constructors, Inc</td>
<td>$14,405,130.11</td>
<td>78.1%</td>
<td>60.0%</td>
</tr>
<tr>
<td>3. C.R. Fedrick, Inc</td>
<td>$18,139,911.00</td>
<td>98.3%</td>
<td>75.6%</td>
</tr>
</tbody>
</table>

(AF, tab 1 at 2).

9. Bids received for the warranted transformer losses for the four bidders responding to the solicitation were as follows:

<table>
<thead>
<tr>
<th>Brady</th>
<th>Picacho and Red Rock</th>
</tr>
</thead>
<tbody>
<tr>
<td>No-Load</td>
<td>Total Losses</td>
</tr>
<tr>
<td>Interact</td>
<td>17.9</td>
</tr>
<tr>
<td>Federick</td>
<td>17.9</td>
</tr>
<tr>
<td>V.O.</td>
<td>17.9</td>
</tr>
<tr>
<td>Gardner Zemke</td>
<td>19</td>
</tr>
</tbody>
</table>

(Complaint, ¶ 15).

10. In August of 1987 (i.e., prior to shipment) General Electric Co. (subcontractor for the six transformers here in issue; hereinafter (GE))
tested the transformers in the presence of Bureau quality assurance representatives. The test results showed that the actual total losses were greater than the total losses bid by GZ (Complaint and Answer, ¶¶ 6, 21, 22). On October 26, 1987, GZ forwarded to the Denver office of the Bureau GE's test reports for the 115-KV power transformers (AF, tab 7).

11. In a memorandum under date of December 18, 1987, addressed to the Regional Director, Boulder City, Nevada, the Bureau's Engineering and Research Center in Denver, Colorado, stated: (i) that the transformer test reports submitted with GZ's letter of October 26, 1987, has been reviewed; (ii) that all of the submitted data except the transformer losses had been determined to be acceptable; (iii) that the actual transformer losses, measured at a base temperature of 85° C., had been found to exceed the evaluated losses warranted by the contractor; (iv) that since the actual transformer losses exceeded the warranted transformer losses, an adjustment must be made in accordance with paragraph I.4.18 of the Specifications; and (v) that after determining the total transformer losses by computing the transformer losses at the loading conditions listed under "Warranted Characteristics" in parts A, B, and C of the Specifications schedule, it was found that the total monetary adjustment to which the Bureau was entitled for transformer losses for Brady, Picacho, and Red Rock switchyards under I.4.18 of the Specifications was in the amount of $225,161.79 (AF, tab 8).

12. Modification No. 031 to the contract was executed by the contractor on January 22, 1988, and by the CO on February 3, 1988 (Bureau Memorandum (June 15, 1989), Exh. 4). Modification 31 was a supplemental agreement under which the Bureau agreed to pay GZ the sum of $197,302 for the changes to the contract reflected in Modification No. 11. In Modification No. 31, GZ agreed that the amount to be paid thereunder would constitute a complete equitable adjustment for the substitution of the transformer requirements contained in Modification No. 11 for those contained in the solicitation upon which GZ had bid. Included in Modification No. 31 was release language by which GZ released the Government from all proposals or claims arising out of, resulting from, or directly related to the revisions to the contract effected by the supplemental agreement (Bureau Memorandum (June 15, 1989), Exh. 4).

13. By letter of March 11, 1988, the Bureau formally notified the contractor of the findings made by the Engineering and Research Center in its memorandum of December 18, 1987. After referring to the provisions of paragraph I.4.18 of the Specifications (Finding 5), the
letter states: "Since the Government elects to accept this equipment, we are providing you with the opportunity to repair or replace the defective transformers due to the actual transformer losses." The letter went on to say that if GZ elected not to repair or replace the defective transformers, the Bureau would be entitled to a monetary adjustment in the amount of $225,195.63. The letter concluded by requesting GZ to inform the Bureau as to whether the contractor would be repairing or replacing the transformers in question or whether the Bureau should proceed with adjustment of the contract value in the amount indicated (AF, tab 9).

14. Meetings to discuss the transformers losses described in the Bureau's letter of March 11, 1988, were held between representatives of the Bureau, the contractor, and GE on April 28 and May 19, 1988 (AF, tabs 10, 11). On July 14, 1988, GZ wrote the Bureau to request an adjustment in the contract in the form of relief from a proposed penalty for failure by the contractor to meet warranted characteristics for the 115-KV transformers. The letter states that GZ did not realize a mistake in bid was involved until it received the Bureau's letter of March 11, 1988, and had subsequent discussions with GE representatives. After noting that FAR 14.406-4 provided relief for bid mistakes which involve clerical or mathematical errors or a misreading of the specifications, the letter adds parenthetically that its supplier (GE) appears to have "misread" the specifications in that it thought the load loss measurement for warranted characteristics would be at the self-cooled ratings rather than the forced-cooled ratings for the transformers (AF, tab 12).

15. Accompanying the letter from GZ of July 14, 1988 (Finding 14) was a copy of a communication between GE representatives in which the supplier states that the tested losses for the transformers, as listed in the Bureau's March 11, 1988, letter, exceeded the warranted characteristics submitted at the time of bid (Solicitation Bidding Schedule at F-14, F-28, F-42); that this was the result of an error in completing the bid schedule for the required loss values; and that this error was not discovered until well after award, design, and manufacture of these transformers. Elaborating upon the nature of the mistake made, the letter states, inter alia:

Our quoted losses were developed prior to bid and as is frequently the case, were transmitted verbally within hours of the bid opening time. What was provided in response to technical specifications was presumed to be what was required by the Bid Schedule.

In our opinion, a reasonable designer would assume that losses would be warranted for the loading at which they would be tested. Had he also read the Bid Schedule, the conflict would have been obvious and a clarification would have been sought prior to the bid date.

* The contractor's response is contained in its letter to the Bureau of Apr. 26, 1988, from which the following is quoted: "This letter confirms that the power transformers which were the subject of your letter dated March 11, 1988 will not be repaired or replaced" (Bureau Memorandum (Sept. 15, 1989), Exh. 2).
We therefore believe that the fundamental error resulted from a lack of communication and coordination between GE and Gardner-Zemke.

(AF, tab 12; GE's Letter of July 12, 1988).

16. In response to a request from the CO to comment on GZ's mistake in bid claim, the Chief, Construction Division (Denver Federal Center) stated in a memorandum under date of September 21, 1988, that various provisions of the specifications and bidding schedule sheets, F-14, F-28, and F-42, all clearly define the requirements for how the losses for each transformer will be evaluated including references to cooling equipment and loading conditions. After referring to the requirement for reformation of a contract as set forth in FAR 14.406-4 (note 2, supra) and after undertaking to say what information would be available to the CO at the time the four bids in question were received, the memorandum states that "based on the data available to the contracting officer, the mistakes the Contractor claims to have made were not apparent and did not, in effect, put the Government on notice of the probability of a mistake" (AF, tab 14).

17. In her decision of December 16, 1988 (issued as Modification 071 to the instant contract), the CO rejected the contractor's request for adjustment in the contract, in the nature of relief from a proposed penalty for failure to meet warranted characteristics with respect to transformers furnished for the Brady, Picacho, and Red Rock pumping plants. In support of the refusal to provide the relief requested, the CO found that the mistakes alleged by the contractor did not constitute a justifiable basis for contract reformation since the mistake was neither mutual nor so apparent as to have charged the CO with notice of probability of the mistake at the time of contract award. So finding, the CO further found that there should be a downward adjustment in the contract price in the amount of $225,195.63 for the calculated load losses in excess of the warranted load losses (AF, tab 15).

DISCUSSION

Before us for decision are the Bureau's motions for summary judgment and appellant's cross-motion for summary judgment. A motion for summary judgment will be granted if no material facts remain in issue and the moving party is entitled to a judgment as a matter of law. The moving party bears the burden of demonstrating both elements, and the party against whom the motion is advanced is entitled to have all inferences drawn in its favor. [Citation omitted.]

Santa Fe Engineers, Inc., ASBCA No. 31847 (Feb. 18, 1988), 88-2 BCA ¶ 20,619 at 104,211.
Government Motion for Summary Judgment Based on Release

In its motions for summary judgment against the appellant, the Bureau relies upon the affirmative defenses of abandonment, novation, release, and accord and satisfaction, as well as upon the defense that appellant has failed to state a claim for relief (Bureau Memorandums (June 15, 1989) at 1-4, 9-11, 18-19 and (Sept. 13, 1989) at 20-26). Establishing the affirmative defenses of abandonment, novation, release, and accord and satisfaction are all dependent upon the Government showing that the release language contained in Modification No. 31 is a bar to granting GZ's mistake in bid claim here in issue. Before addressing the effect to be given to the release provision included in Modification No. 31, we will first consider the principal contentions that the Bureau has advanced concerning the elements required to be shown to establish the affirmative defenses of accord and satisfaction or release.

Existence of a Dispute as a Prerequisite for Accord and Satisfaction Defense

One of the positions advanced by the Bureau is that it is unnecessary for the Government to show that there was a dispute concerning GZ's mistake in bid claim at the time Modification No. 31 was executed in order for that supplemental agreement to constitute an accord and satisfaction (Bureau Memorandum (Sept. 13, 1989) at 20). The cases cited at pages 21-22 of the same memorandum as setting forth the elements required to be shown to establish an accord and satisfaction do not support the Bureau's position. This is shown by the following quotation from King Fisher Marine Service, Inc. v. United States, 16 Cl.Ct. 231, 236 (1989):

Citing United States v. Johnson Controls, 713 F.2d 1541 (Fed. Cir. 1983), the Bureau has also moved to dismiss the appeal by GE, the subcontractor which supplied the transformers here in issue. Unlike the situation present in Johnson Controls, however, the appeal initiated on behalf of GE was taken by the prime contractor (GZ) in its own name and it was so docketed. It is the notice of appeal, not the complaint, that establishes the bounds of jurisdiction for the Board. Crawford Technical Services, Inc., ASBCA No. 38732 (Mar. 27, 1989), 89-2 BCA ¶ 21,783 at 109,608. It is not possible, of course, to dismiss an appeal that has neither been filed nor docketed. The Bureau has also moved to strike from the complaint the references to GE joining in the allegations to GE joining in the allegations of the complaint and in the request for relief. While it is considered to be somewhat unusual for the subcontractor (GE) to be joining in the allegations and in the request for relief contained in the complaint, it is clear that continued sponsorship of GE's claim by the prime contractor (GZ) is necessary for the Board to have jurisdiction over the claim asserted. Divide Constructors, Inc., IBCA-1154-12-76 (Mar. 29, 1977), 84 I.D. 119, 123-24, 77-1 BCA ¶ 12480 at 60,184. In his representations to the Board appellant's counsel unqualifiedly recognizes that GE has no standing before the Board except by reason of the sponsorship of the prime contractor (GZ's Memorandum (July 10, 1989) at 34). The Bureau's motion to strike is therefore denied.

Another affirmative defense advanced by the Bureau is that GZ waited too long to give the CO notice of the alleged mistake in bid (Bureau Memorandum June 15, 1989) at 10-11). Although the Bureau cites cases in support of its position, nowhere does it acknowledge the significance of the fact that, insofar as the present record discloses, GZ was unaware that any mistakes in bid had been made until it received the Bureau's letter of Mar. 11, 1988 (Finding 14); nor has the Bureau undertaken to show that any prejudice resulted from any delay by GZ in giving notice of the mistake in bid claim. The need to show some prejudice or injury resulting from a delay in giving notice of a claim necessarily raises a question of material fact that precludes granting summary judgment. Harbert International Services, ASBCA No. 36983 (Nov. 6, 1989), 90-1 BCA ¶ 22,449 at 112,717-18).

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9 Also cited by the Bureau is the decision of the Claims Court in Progressive Brothers Construction Co. v. United States, 16 Cl.Ct. 549, 553 (1989). The decision in Progressive Brothers is focused on the failure of the contractor to specifically enumerate any claim on the general release form it executed. It is noteworthy that in the Progressive Brothers case, the contractor knew of additional claims it wished to pursue but failed to enumerate them in the settlement agreement it signed (16 Cl.Ct. 550-51).
The operative elements of an accord and satisfaction are as follows: “Proper subject matter, competent parties, meeting of the minds of the parties [10] and consideration . . . [and acceptance] of payment or performance in satisfaction of a claim or demand which is a bona fide dispute” Nevada Half Moon Mining Co. v. Combined Metals Reduction Co., 176 F.2d 73, 76 (10th Cir. 1949), quoted in Brock & Blevins, 170 Ct.Cl. at 59, 343 F.2d at 955.

To the same effect is Robinson Contracting Co. v. United States, 16 Cl.Ct. 676, 680 (1989) (citing and quoting from, inter alia, Brock & Blevins Co. v. United States, 170 Ct.Cl. 52, 343 F.2d 951, 955 (1965).

In any event, the Bureau says the evidence shows a dispute did exist and in connection therewith states that “[p]rior to the execution of Modification No. 31, there was clearly a dispute as to the amount the Bureau owed Gardner Zemke to complete the amended contract or a claim by Gardner Zemke for additional compensation resulting from the amended contract as the contract was modified by change orders 9 and 11 and 31” (Bureau Memorandum (Sept. 13, 1989) at 21).

In point of fact, the record does not disclose what amount GZ sought initially as an equitable adjustment. It is thus clearly distinguishable from the situation present in King Fisher, supra, where it is apparent that the contractor sought more than the amount of the equitable adjustment the Government provided and that in that case “the parties sat down at a bargaining table in order to settle their disagreement” and “then reduced their agreement to writing, which included the release provision, supra, stating that such ‘modification constitutes compensation in full on behalf of the contractor . . . for all costs and markups directly or indirectly attributable to the changes ordered herein.’” 16 Cl.Ct. at 236-37.

Another argument advanced by the Bureau is that it “is not necessary that the Bureau show [a] ‘dispute’ as to every item or potential claim included in the overall ‘dispute’ leading to the accord and satisfaction where the contractor executes a release to ‘all claims * * relating to revisions to the contract’ as the case in this situation” (Bureau Memorandum (Sept. 13, 1989) at 21-22). GZ’s mistake in bid claim is not related in any way to “revisions to the contract” to which Modification No. 31 (executed by GZ on January 22, 1988) refers, however, but is predicated upon events which occurred prior to or at the time of its bid submission on or about May 21, 1986 (AF, tab 3).

Moreover, unless the language of the release involved is so broadly drawn as to encompass unknown claims, for an accord and satisfaction to be found, the dispute must relate to the specific claim involved in

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10 Returning to this subject a short time later in the opinion, the Claims Court states (16 Cl.Ct. at 236-37):

“The fourth element of an accord and satisfaction is a meeting of the minds.

"In order that a performance rendered by an obligor shall operate as a satisfaction of the claim against him, it must be offered as such to the creditor. . . . There must be accompanying expressions sufficient to make the creditor understand, or to make it unreasonable for him not to understand, that the performance is offered to him as full satisfaction of his claim and not otherwise. If not so rendered, there is no accord, either executory or executed, for the reason that there are no operative expressions of agreement—no sufficient offer and acceptance." Chesapeake & Potomac Telephone, 228 Cl.Ct. at 109, 564 F.2d at 716 (quoting Corbin, supra, § 1277); see also Eldon Industries, Inc. v. Paradies & Co., 397 F Supp. 536, 543 (N.D. Ga. 1976)." (Italics in original.)
the subsequent proceeding. This was clearly the case in *King Fisher Marine Service*, 16 Cl.Ct. at 234-37. See also *Lear Siegler, Inc.*, ASBCA No. 19258 (Feb. 19, 1975), 75-1 BCA ¶ 11,119 at 52,907 (citations omitted) ("We find no evidence that, as of the date of execution of the modification, the parties were in dispute about anything concerning the items ordered pursuant to Delivery Order No. 0001 including Item No. 0008. In circumstances such as are present here, the Board has found no accord and satisfaction") and *RCA Corp.*, NASA BCA No. 676-4 (Apr. 28, 1978), 78-1 BCA ¶ 13,220 at 64,666 ("We find in this case that one of the essential elements of an accord and satisfaction is missing—a genuine disagreement or dispute between the parties with reference to the claim asserted in this appeal, the overhead ceiling rates. Accordingly, we hold that the Appellant is not barred from asserting his present claim by virtue of his acceptance of the preceding change orders").

**Materiality of Intent of Parties at the Time the Release is Executed**

The Bureau devoted a considerable amount of effort to attempting to establish that the intent of a contractor at the time a release is executed is material only if the intent to assert future claims is manifested by specifying them on the release forms (Bureau Memorandums (Aug. 25, 1989) at 12 and (Sept. 13, 1989) at 10-15). According to the Bureau, it is relying upon the principles enunciated by the Claims Court in *Progressive Brothers Construction Co. v. United States*, 16 Cl.Ct. 549, 553 (1989), from which the following is quoted:

Ordinarily, "summary judgment may not be used to determine intent" ****. However, the subjective intent of the plaintiff is not a material issue. The law requires that a contractor manifest intent to assert future claims by specifying them on the release form. The subjective and unmanifested intention of the plaintiff will not avoid the otherwise absolute effect of a release. *H.L.C. & Associates Construction*, 176 Ct.Cl. at 295, 367 F.2d at 592. ** ** Regardless of plaintiff's intention, the release was complete on its face and did not specify any claims. Because the issue of whether plaintiff subjectively intended to waive future claims by signing a release is immaterial, allegations on these grounds will not preclude summary judgment.

The releases found to bar the claims considered in *Mingus Constructors, Inc. v. United States*, 812 F.2d 1387, 1394-96 (Fed. Cir. 1987), and in *Progressive Brothers, supra* at 550-53, and to bar one of the claims considered in *H.L.C. & Associates Construction Co. v. United States*, 176 Ct.Cl. 285, 291-95 (1966), all involved claims about which the plaintiffs were aware at the time the releases were executed.11 In the case here, however, it is uncontroverted that GZ was unaware of any mistake in bid claim until it received the CO's letter of March 11, 1988 (Finding 14) which was over 6 weeks after the execution by GZ of Modification No. 31 with the release language contained therein (Finding 12).

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11 See also *Mann Construction Co.*, IBCA-1280-7-79 (Dec. 10, 1981), 88 I.D. 1065, 82-1 BCA ¶ 15,481 in which a contractor's claim for interest was denied where the contractor proceeded to settlement of its substantive claims without excepting from the settlement reached a known claim for interest.
Not addressed by the Bureau is the fundamental question of how at
the time Modification No. 31 was signed, GZ could be said to have had
any intention, subjective or otherwise, about a mistake in bid claim of
which it was then completely unaware.

It has long been recognized that apparently conclusive language in a
release will not bar consideration of a claim on the merits which was
clearly not within the contemplation of the parties at the time the
document containing the release language was executed. See L. W.
Packard & Co. v. United States, 66 Ct.Cl. 184, 192 (1928) ("[A] receipt or
release, however conclusive in terms, is subject to explanation as to the
subject matter of the accord and satisfaction"). See also Bick-COM
Corp., VACAB No. 1320 (Feb. 15, 1980), 80-1 BCA ¶ 14,285 at 70,347
("The scope of an accord and satisfaction agreement is determined by
the specific language used and the intent of the parties as manifested
by the events and communications which preceded execution"); RCA
Corp., NASA BCA No. 676-4 (Apr. 28, 1978), 78-1 BCA ¶ 13,220 at
64,666 ("An accord and satisfaction does not operate as a bar in regard
to matters not contemplated by the agreement. John A. Volpe
Construction Co., Inc., GSBCA No. 2570, 70-1 BCA ¶ 8070; J.A. LaPorte,
Inc., IBCA No. 1014-12-73, 75-2 BCA ¶ 11,486, at p. 54,781"); and Hensel
Phelps Construction Co., IBCA-1010-11-73 (May 8, 1975), 82 I.D. 199,
210, 75-1 BCA ¶ 11,232 at 53,458 ("[I]t is well settled that an agreement
will not operate as an accord as to matters not contemplated by the
agreement"). (Footnote omitted.)

Consideration of Claim on the Merits as Vitiating Release

The Bureau acknowledges the validity of the general proposition
that the conduct of the parties in continuing to consider claims on
their merits after the execution of a release evidences that the parties
never regarded the release as an abandonment of the claim. The
position of GZ is that the actions of the CO in considering the mistake
in bid claim on the merits without reliance upon or even mention of
the release had the effect of vitiating the release as a defense to the
claim asserted. The Bureau attempts to distinguish the cases cited by
GZ in support of its position on the ground that the key to such cases
is the consideration of the conduct of both parties subsequent to the
date of the execution of the release (Bureau Memorandum (Sept. 13,
1989) at 15-19).

While factual differences between the instant case and the cases
cited by GZ do exist and have been pointed out by the Bureau, the
distinction sought to be made is not considered to be the rationale for
the decisions reached in such cases. In Addison Construction Co., IBCA-
1064-3-75 (Sept. 29, 1976), 83 I.D. 353, 358-59, 76-2 BCA ¶ 12,118 at
58,213, the basis for the decision reached is stated in the following
terms: "Since the contracting officer considered the request on its
merits, the Board cannot avoid similar consideration of the merits in
this appeal from the findings of the contracting officer.” (Footnote omitted.) This statement is included in the portion of the Addison decision quoted with approval in Middlesex Contractors & Riggers, Inc., IBCA-1964 (Feb. 8, 1989), 89-1 BCA ¶ 21,557 at 108,561.

In an apparent effort to bolster its argument, the Bureau cites and quotes from the decision of the Armed Services Board in Modular Devices, Inc., ASBCA No. 33708 (Apr. 14, 1987), 87-2 BCA ¶ 19,798 at 100,158. The decision in Modular is inapposite. It is not concerned in any way with questions related to release or accord and satisfaction but simply espouses the well-established principle that Board review of a CO’s decision is de novo. That de novo jurisdiction includes reviewing actions taken or not taken by CO’s in the administration of contracts and determining the legal effect to be given to actions so taken by them.

That the decision in Modular, supra, is not relevant to the question before us is shown by the numerous decisions of the Armed Services Board involving the question of the effect upon a release of consideration on the merits of a claim apparently covered by the release language. See Hibbitts Construction Co., ASBCA No. 37070 (Jan. 4, 1990), 90-1 BCA ¶ 22,598 at 113,392 (continued consideration of claim vitiates the effect of the release and puts the parties in the same position that they would have been in if no release had been executed). See also C&W Electric Co., ASBCA No. 34236 (Feb. 12, 1988), 88-2 BCA ¶ 20,624 at 104,245 (“Since the Government acted in a manner indicating that it did not consider the claim revisions barred by the release, the Motion for Partial Summary Judgement is denied”).

Near the end of its presentation the Bureau stated that “the single fact that * * * [its] contracting officer’s failure to reject the claim as barred by the release should not be held to nullify the effectiveness of the release because the contracting officer was correct in her decision to deny the claim for reformation albeit she did not cite the release as the grounds therefore” (Bureau Memorandum (Sept. 13, 1989) at 19). On this motion for summary judgment, the question is not whether the CO was correct in her decision but is rather whether her failure to rely upon the release as the ground for her decision has the effect of eliminating the release as a valid defense to GZ’s mistake in bid claim.

In concluding our discussion of this matter, the Board notes that this is not a case in which a CO routinely denies a claim immediately upon submission without relying upon a previously executed release as the basis for the denial. Here over 10 months elapsed between the execution of the release and the denial of the claim. During that interval representatives of the parties met in the office of the CO on at least one occasion where the items discussed included GZ’s mistake in bid claim. Upon formal submission of that claim by GZ’s letter of July 14, 1988, the CO transmitted the claim to the Bureau’s Engineering and Research Center for review and comment by her memorandum of August 1, 1988. Almost 3 months after receiving the comments and recommendation of the center, the CO issued
Modification No. 071 by which GZ's mistake in bid claim was denied (AF, tabs 11-15).

There is no evidence in the record that in conference or in correspondence any consideration was given by the parties to the release included in Modification No. 31 prior to the filing of the Government's motion to dismiss or that a mistake in bid claim was even mentioned by anyone prior to receipt by GZ of the Bureau's letter of March 11, 1988 (Finding 14). In the absence of any such evidence, it appears that "the conduct of the parties in continuing to consider [GZ's mistake in bid] claim after the execution of the release makes plain that they never construed the release as constituting an abandonment of the claim." J. G. Watts Construction Co. v. United States, 161 Ct.Cl. 801, 807 (1963).

Effect of Release

[1] As has been previously noted, the affirmative defenses of abandonment, novation, release, and accord and satisfaction can only be established by the Bureau showing that the release language included in Modification No. 31 is a bar to consideration of GZ's claim on the merits. If the Bureau were to make such a showing, the question of whether GZ has stated a claim for relief based upon a unilateral mistake in bid alleged after award would become moot. We now turn to consideration of the question of whether the language employed in Modification No. 31 encompasses the mistake in bid claim here in issue.

Modification No. 031 was signed by GZ on January 22, 1988, and by the CO on February 3, 1988. After citing as authority Section I, Contract Clauses, Paragraph I.4.11, Changes (AF, tab 18, at I-21), and Mutual Agreement and after setting forth the changes reflected in Modification No. 11, the modification increased the amount to be paid the contractor for the changes to the work by the lump sum of $197,302. The release included in Modification No. 31 reads as follows:

Release: The Contractor agrees that this supplemental agreement is a complete equitable adjustment for all contractor proposals or claims whatsoever arising out of, resulting from, and/or directly related to the above occurrences, revisions to the contract, and/or this supplemental agreement and hereby releases the Government from all liability under this contract for further equitable adjustment for said occurrences, revisions, and/or this supplemental agreement.

(Bureau Memorandum (June 15, 1989), Exh. 4).

In construing the language of a modification, we will look first to the text of the agreement. Wright Associates, Inc., ASBCA No. 33721 (July 22, 1987) 87-3 BCA ¶20,056 at 101,535. We will also undertake to determine the intention of the parties as gathered from the circumstances surrounding the negotiation and execution of Modification No. 31. See Beatty Electrical Co., EBCA No. 403-3-88 (Jan. 10, 1990), slip op. at 15-16. See also R. J. Crowley, Inc., ASBCA
No. 28730 (Jan. 31, 1986), 86-1 BCA ¶ 18,739 at 94,296, in which the Armed Services Board stated:

A claim is not considered released unless there are unequivocal acts showing expressly or by implication an intention to release. * * * Further, an agreement will not operate as an accord as to matters not contemplated by the agreement. Hensel Phelps Construction Company, IBCA No. 1010-11-73, 75-1 BCA ¶ 11,292 at 53,458.

* * * there can be no release without a showing of an intent to release, which must be sought from the entire instrument or the documents referenced therein, as well as the circumstances of its execution. [Citations omitted.]

Turning to the language of the release quoted above from Modification No. 31, the Board notes that in a provision taking up only seven lines on the contract page and containing less than 70 words, the term "equitable adjustment"12 is employed twice. From the use of the word "above" before the words "occurrences, revisions to the contract, and/or this supplemental agreement" in the first portion of the release and the later use of the word "said" before "occurrences, revisions, and/or this supplemental agreement" in the second portion of the release, it is considered to be clear that the "occurrences" and "revisions" to which the release refers is limited to those changes in the specification and drawings for which an equitable adjustment13 in the amount of $197,302 was provided elsewhere in the modification.

In addition to the question of the proper interpretation to be placed upon the language of the release, there is the question of the circumstances surrounding the negotiation and execution of Modification No. 31. In support of its position that execution by the contractor of Modification No. 31 does not foreclose consideration of its mistake in bid claim, GZ has submitted an affidavit of Richard Zemke, Vice President of Gardner Zemke Electrical and Mechanical Contractors, who had negotiated and executed the modification on behalf of the contractor. The Zemke affidavit states inter alia that at the time Modification No. 31 was negotiated and executed, there was no dispute between GZ and the Bureau concerning a mistake in bid claim based on original warranted characteristics of the transformers or the failure of the transformers to meet the warranted characteristics.

12 In United States v. Utah Construction & Mining Co., 384 U.S. 394, 403-04 (1966), the Supreme Court addressed the question of the nature and extent of the jurisdiction of agency boards of contract appeals and in connection therewith made the following statements pertinent to the question presented here:

"The Government reasserts here its position * * * that the disputes clause authorizes and compels administrative action in connection with all disputes arising between the parties in the course of completing the contract. In its view, the disputes clause is not limited to those disputes arising under other provisions of the contract * * * that contemplate equitable adjustment in price and time upon the occurrence of the specified contingencies. * * * We must reject the government position, as did all the judges in the Court of Claims."

13 No one has suggested that there is a clause in the instant contract under which relief in the form of an equitable adjustment could be provided for the mistake in bid claim here in issue. In Wixon Redbird & Associates, IBCA-1682-6-83 (Sept. 30, 1983), 90 I.D. 441, 84-1 BCA ¶ 16,924, an appeal was dismissed and remanded to the CO for decision on a mistake in bid claim first raised in the complaint. The decision noted that the claim as presented to the CO was for a change order because of the difficulties encountered in performing the contract work and that the manner in which claims for mistake in bids are to be treated and the relief available therefor are specifically provided for in a controlling regulation.
Citing the Zemke affidavit, GZ denies that the parties intended to extinguish any claim based on mistake in bid or that the parties even considered such a claim when Modification No. 31 was executed. Appellant states: "This genuine issue of material fact concerning the intention of the parties alone precludes summary judgment in the Bureau's favor" (GZ Memorandum (Aug. 10, 1989) at 7; Affidavit of Richard Zemke).

Invoking the parol evidence rule and citing a number of cases, the Bureau moved to strike the Zemke affidavit. Not addressed by the Bureau are those cases which have held that the parol evidence rule is not contradicted where the written contract is completely silent regarding the claim in issue. See, for example, Pan Artic Corp., ASBCA No. 20133 et al. (Apr. 22, 1977), 77-1 BCA ¶12,514 at 60,668-69 in which it was found that "the parties did not contemplate that the written agreement was intended to constitute the exclusive agreement of the parties." In reaching its decision, the Armed Services Board considered the decision of the Court of Claims in Sylvania Electric Products, Inc. v. United States, 198 Ct.Cl. 106, 128 (1972), to be controlling. In Sylvania the Court stated:

Parol or extrinsic evidence must be admissible on the issue of the extent to which a written agreement is integrated, for as has been said, the writing cannot prove its own integration. 3 Corbin, Contracts, supra, § 582; see also 9 Wigmore, Evidence, §§ 2400(5), 2470 (1940). Accordingly, "any relevant evidence" is admissible on whether the parties intended their written agreement to be a complete and exclusive statement of all the terms of their agreement.

The decision in Sylvania is also considered to be controlling on the question presented here. Modification No. 31 was completely silent with respect to any mistake in bid claim and included no comprehensive language from which it could be inferred that a mistake in bid claim was intended to be included. As is reflected in the foregoing discussion of the release language found in Modification No. 31, it is considered that only further claims for equitable adjustment are barred by the terms of the release. The Board need not finally determine this question, however, since in the absence of such a construction being placed upon the release language, the release is ambiguous with respect to claim coverage and thus warrants resorting to parol evidence to resolve the ambiguity. The Board therefore finds that the Zemke affidavit is properly includible in the record for the purpose of showing the intention of the parties at the time Modification No. 31 was negotiated and executed. Viz Manufacturing Co., ASBCA No. 17787 (Sept. 19, 1978), 78-2 BCA ¶13,469 at 65,862 ("Modification P010 is unclear as to what costs the price increase of $2,514.48 was intended to cover. Therefore parol evidence as to the parties' intentions may be considered").

Accordingly, the Government's motion to strike the Zemke affidavit is denied. Since the Government has failed to show either expressly or
by implication any intention by GZ to release its mistake in bid claim and since the Zemke affidavit squarely raises a genuine issue of material fact concerning the intention of the parties at the time Modification No. 31 was negotiated and executed, the Government’s motion for summary judgment on the grounds of abandonment, novation, release, and accord and satisfaction is also denied.\textsuperscript{14}

**Unilateral Mistake in Bid Claim as a Claim for Relief**

[2] The Bureau denies that the complaint states a claim for which the relief requested by appellant may be granted. Noting that the appeal involves a mistake in bid not alleged until after the contract is awarded and citing a number of cases in support of its position, the Bureau states, \textit{inter alia}, (i) that appellant can recover for a unilateral mistake only if the CO knew, or should have known, of the mistake at the time the bid was accepted; (ii) that where reformation of a contract is sought, the contractor must establish by clear and convincing evidence what the bid price would have been but for the error; (iii) that where a mistake is attributable to the failure of the CO to verify a bid, the mistake may be corrected if it involved clerical errors or a misreading of the specifications but not if the mistake reflects errors in business judgment; and (iv) that to be correctable, the mistake must not have arisen from negligence where the means of knowledge were easily accessible (Bureau Memorandum (June 15, 1989) at 18-19).

In contesting the validity of the Bureau’s position, GZ states that the complaint allegations pertaining to reformation based on a unilateral mistake alone are sufficient for the appeal to survive the Government’s motion. GZ also asserts that the elements for the relief sought (as set forth in FAR 14.406-4) are that there must be evidence of a mistake in bid and that the mistake was so apparent as to have charged the CO with notice of the probability of a mistake. In addition, appellant notes that under section 1.4.17 of the specifications (Finding 4), the Bureau was not only required to consider the warranted characteristics but also to use them to calculate an important (and potentially critical) evaluation factor. GZ also calls attention to what it describes as the magnitude of the discrepancy between the total losses bid as warranted characteristics by GZ and the total losses bid by the other three offerors, as set forth in paragraph 15 of the complaint (Finding 9) (GZ Memorandum (July 10, 1989) at 6-8).

In \textit{Chemtronics, Inc.}, ASBCA No. 30883 (Dec. 3, 1987), 88-2 BCA ¶ 20,534, a contract to supply personal chemical decontamination kits was reformed because of a unilateral mistake. There the Armed Services Board found that the Government’s request for verification of

\textsuperscript{14}The Government’s motion for summary judgment is also denied on the alternative ground that subsequent to the execution of the release, the parties showed by their conduct that they never considered the release as constituting an abandonment of appellant’s mistake in bid claim. See \textit{Hibbitts Construction Co.}, ASBCA No. 37070 (Jan. 4, 1990), 90-1 BCA ¶ 22,598 at 113,392, and other cases cited in opinion under caption “Consideration of Claim on the Merits As Vitiating Release.”
the contractor's initial proposal was inadequate and that, in its "Request for Best and Final Offers," the Government had failed to apprise the appellant that there were substantial disparities between the appellant's refill kit price, its total price, and the corresponding prices contained in the remaining proposals, the historical record and the Government's estimate. In submitting its proposals, Chemtronics had relied upon an erroneous quotation from a sole source for specialized aluminum foil used to make the personal chemical decontamination kits. The price intended to be quoted by the contractor for the kits should have been based upon a foil price of $1.61 per 1,000 square inches, rather than the foil price of $1.61 per 100,000 square inches reflected in the proposals submitted.

In providing the reformation relief requested in Chemtronics, the ASBCA noted, inter alia (i) that in relying upon an erroneous oral quotation from a sole source aluminum foil supplier, the contractor had violated its own established policy of requiring firm written quotations from its suppliers; (ii) that it did not matter that the clerical error was that of the aluminum foil supplier rather than that of the appellant; (iii) that while the conduct of Chemtronics in failing to adhere to its own policy of requiring written quotations was at the very least misguided, it was not the type of judgmental error that precludes the application of the reformation remedy; (iv) that the appellant's failure to give the Government written notice of the mistake for 15 months after the mistake was discovered was inconsequential where the Government should have known prior to award that Chemtronics' proposal was in error; and (v) that the facts and circumstances known or reasonably available to the CO prior to the award of contract should have raised a presumption of error in his mind (88-2 BCA at 103,835-37).

Concerning the question of when a CO may properly be charged with constructive notice of a mistake in bid, the opinion in Chemtronics, supra, at 103,836-37, states:

The oft-cited decision of the Court of Claims in Wender Presses v. United States, supra, [15] sets forth the standards for determining whether the contracting officer had constructive notice of possible error:

[T]he task of ascertaining what an official in charge of accepting bids "should" have known or suspect[ed] is, of course, not always an easy one. Mistakemaking contractors will naturally seek to impose upon such officials a rather high level of brilliance for the purpose of detecting the error. If, for instance, the knowledge of the government's "staff of experts" available to the contracting officer is imparted to such officer... then what the contracting officer "should" have known would cover a very wide range indeed. However, the test... must be that of reasonableness, i.e., whether under the facts and circumstances of the particular case there were any factors which reasonably should have raised the presumption of error in the mind of the contracting officer... without making it necessary for the agency's experts in every case to assume the burden of examining every... bid for possible error... (citations omitted)

The record in this case is entirely devoid of any evidence indicating what the CO did prior to award of the contract in discharge of his responsibility to examine the bids received for possible mistakes. Questions raised by this record include the following:

1. Prior to the award of the instant contract, did the CO read the report of the Bid Opening Board (AF, tab 1)?
2. Did the CO request GZ to confirm its bid, as had been recommended by the Bid Opening Board (AF, tab 1 at 4)?
3. What consideration, if any, did the CO give to the fact that bidders were required to warrant characteristics on only three bid items (all of which involved transformers) out of the 538 bid items covered by the solicitation (AF, tab 3) and that in reference to the warranted characteristics the dollar figures assigned to the bids for bid evaluation purposes were $1,114,690 for the GZ bid and $1,616,481 for the other bids received, a difference of $501,741 (AF, tab 1 at 2)?
4. Did the CO's examination of the bids submitted disclose that not only did the second and third lowest bidders warrant the characteristics of the transformers called for by Bid Items 149, 331, and 510 by the submission of identical figures for each of such items but so did the bidder disqualified for failure to bid on all 538 items (AF, tab 1 at 2; AF, tab 14 at 2)?
5. Was any consideration given by the CO to the pattern of bidding which resulted in the characteristics warranted by GZ on three bid items (out of 538) being assigned a value for bid evaluation purposes of approximately half a million dollars less than the values assigned for warranted characteristics to the other bids received (item 3, supra) and which shows that on all 538 items the difference between the low bid submitted by GZ and that of the next low bidder was only $1,512,936.11 (AF, tab 1 at 2; AF, tab 3)?

As to the nature of the CO's responsibilities in this area, the Bureau states that whether a CO has fulfilled his duty to verify a bid is a question of law and that whether the CO knew, or should have known, of the alleged mistake in bid, asserted after award, is based on a reasonableness test (Bureau Memorandum (June 15, 1989) at 18-19). The Board notes, however, that a legal issue may not be decided in a factual vacuum and that any determination must rely upon a factual predicate. Murson Constructors, Inc., ASBCA No. 34538 (Jan. 27, 1988), 88-2 BCA ¶ 20,549 at 103,885. The Board also notes the recent decision in the case of Artic Corner, Inc., ASBCA No. 38075 (Jan. 11, 1990), 90-1 BCA ¶ 22,617 at 113,460, in which it is stated: "Issues that require...

16 In United States v. Hamilton Enterprises, Inc., 711 F.2d 1038, 1048 (Fed. Cir. 1983), the Court of Appeals for the Federal Circuit denied the reformation relief requested by the appellant because it found that the erroneous bid had resulted from a mistake in judgment but nevertheless provided the contractor some relief based upon the Court's finding of mutual fault. In Don Simpson, ICA 2058 (Feb. 24, 1986), 93 I.D. 76, 86-2 BCA ¶ 18,768, the contract in issue was rescinded where, citing the Hamilton Enterprises, Inc., decision as authority, this Board found that the case involved mutual fault. Accord Reaco Services, Inc., IBCA-2260 (Mar. 18, 1987), 94 I.D. 86, 87-1 BCA ¶ 18,659. Cf. Kitchens Construction, Inc., IBCA-2140, 2141-42 (July 16, 1986), 86-3 BCA ¶ 19,137.
June 19, 1990


Here the Bureau has failed to furnish any information as to what action the CO took or failed to take upon the opening of bids to "examine all bids for mistakes" (footnote 1). In the circumstances, the Board has no factual basis upon which to judge the reasonableness of the CO's actions in the performance of his bid verification duties. In the absence of any such factual basis and drawing all inferences in favor of appellant as the party against whom the motion for summary judgment is advanced, the Board finds that there are genuine issues of material fact in dispute and that the Bureau is not entitled to summary judgment as a matter of law. Accordingly, the Bureau's motion for summary judgment based upon the failure of appellant to state a claim for relief is denied.

Cross-Motion for Summary Judgment

[3] Appellant's cross-motion for summary judgment is predicated upon two grounds. The first ground is filed as a response to the Bureau's theory of novation and the Bureau's position that Modification No. 31 extinguished any claim GZ may have had that the warranted characteristics were mistakenly bid. Appellant states: "Thus, if the Board accepts the Bureau's misguided novation theory, it is Gardner Zemke, and not the Bureau, that is entitled to summary judgment" (GZ's memorandum (Aug. 10, 1989) at 13, 15). Since the Bureau's novation theory has not been accepted, there is no need for the Board to concern itself further with the first ground assigned by GZ for granting its cross-motion for summary judgment.

As a second ground for its cross-motion, appellant states that it "is entitled to summary judgment whether the Bureau's novation theory is adopted or not because the warranty offered in its bid and included in the contract was premised on and applied to the original transformer specifications and did not extend to the transformers as modified by the Bureau" (GZ Memorandum (Aug. 10, 1989) at 15-16). Decisions of the Armed Services Board are cited in support of the general propositions (i) that the buyer's remedies under an express warranty are controlled by the terms of that warranty; (ii) that the buyer has the burden of proving that the warranty extended to the defects complained of; and (iii) that the agency must show that the particular supplies on which the claim is based did not satisfy the terms of the warranty. None of the ASBCA cases so cited involved warranty clauses at all similar to those contained in the instant contract (Findings 3-5) and none of them entailed applying the provisions of the Uniform Commercial Code upon which GZ's position
appears to be primarily based; nor has GZ made any effort to show that the circumstances under which the warranty clauses were invoked in the cases cited were at all comparable to the circumstances with which we are here concerned.

In support of its cross-motion, appellant also cites several state cases in which the decisions reached apparently involved applying the provisions of the Uniform Commercial Code. Thus, citing authorities, GZ states that "the Bureau lost any warranty protection concerning the transformers' performance characteristics by changing the specifications upon which the original warranty was based and failing expressly to require a warranty based on the revised specifications when it entered into Modification No. 31." A short time later appellant states that "the Bureau may not recover under the original warranty because it agreed to the specification changes and the price for those changes with knowledge that the performance characteristics of the revised transformers did not meet the previously warranted characteristics" (GZ Memorandum (Aug. 10, 1989) at 16-17). As to the reliance placed upon the state cases involving the Uniform Commercial Code, the Board notes that appellant has failed to show that the principles apparently enunciated therein have been endorsed by the Federal courts so as to have become a part of what has been described as the general Federal common law. See Federal Pacific Electric Co., IBCA-334 (Oct. 23, 1964), 71 I.D. 384, 389, 1964 BCA ¶ 4494 at 21,585.

Since the cases relied upon by appellant have not been shown to be dispositive of the question presented, appellant has failed to show that it is entitled to judgment as a matter of law. Appellant's cross-motion for summary judgment is therefore denied.

Summary

The Government's motions for summary judgment and appellant's cross-motion for summary judgment are denied. Within 20 days from the date of receipt of this decision, each of the parties shall file with the Board a schedule for the completion of discovery or, within such time period, shall advise the Board that no discovery is contemplated.

WILLIAM F. MCGRAW
Administrative Judge

I CONCUR:

RUSSELL C. LYNCH
Administrative Judge
MOBIL OIL CORP. v. ALBUQUERQUE AREA DIRECTOR, BUREAU OF INDIAN AFFAIRS

18 IBIA 315

Decided: July 2, 1990

Appeal from a determination that two tribal oil and gas leases had expired by their own terms because of failure to produce oil and/or gas in paying quantities.

Affirmed.

1. Indians: Leases and Permits: Cancellation or Revocation--Indians: Leases and Permits: Generally--Indians: Mineral Resources: Oil and Gas: Generally

A Bureau of Indian Affairs determination that an Indian oil and gas lease has expired by its own terms is not a cancellation of the lease within the meaning of 25 CFR 211.27.


3. Indians: Leases and Permits: Generally--Indians: Mineral Resources: Oil and Gas: Generally

An oil and gas lease issued under the Indian Mineral Leasing Act of 1938, 25 U.S.C. §§ 396a-396f (1982), for a primary term and "as long thereafter as oil and/or gas is produced in paying quantities" expires by operation of law when, after the primary term, production ceases.


No prior notice to the lessee is required where an oil and gas lease issued under the Indian Mineral Leasing Act of 1938, 25 U.S.C. §§ 396a-396f (1982), expires by operation of law. The lessee's right to due process is protected by the administrative appeals process at 25 CFR Part 2 and 43 CFR Part 4, Subpart D.

APPEARANCES: R. Dennis Ickes, Esq., Salt Lake City, Utah, for appellant; Barry K. Berkson, Esq., Office of the Field Solicitor, U.S. Department of the Interior, Santa Fe, New Mexico, for appellee; Thomas H. Shipps, Esq., Durango, Colorado, for the Southern Ute Indian Tribe.

OPINION BY ADMINISTRATIVE JUDGE VOGT

INTERIOR BOARD OF INDIAN APPEALS

Appellant Mobil Oil Corp. seeks review of an August 11, 1989, decision of the Albuquerque Area Director, Bureau of Indian Affairs (Area Director; BIA), finding that Southern Ute Tribal Oil and Gas Leases Nos. MOO-C-1420-1660 (Lease No. 1660) and MOO-C-1420-1661 (Lease No. 1661) had expired by their own terms because of failure to

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produce in paying quantities. For the reasons discussed below, the Board affirms the Area Director’s decision.

**Background**

On August 22, 1974, the Southern Ute Indian Tribe (Tribe) and TransOcean Oil, Inc., entered into Lease No. 1660, covering 1,282 acres of tribal land, and Lease No. 1661, covering 1,245.56 acres of tribal land. The lease term for both was “10 years from and after the approval hereof by the Secretary of the Interior and as much longer thereafter as oil and/or gas is produced in paying quantities from said land.” The leases were approved by the Acting Superintendent, Southern Ute Agency, BIA, on September 10, 1974.

Both leases were placed into production during their primary terms. In September 1979, TransOcean entered into a gas purchase contract with Northwest Pipeline Corp., under which Northwest was to purchase all the gas produced from the two leases. In 1981, the leases were assigned to appellant; appellant also succeeded to TransOcean’s gas purchase contract with Northwest.

In August 1987, appellant entered into a farmout agreement covering both leases with Vince Allen and Associates. On August 11, 1988, Allen assigned its interest in the agreement to Meridian Oil Inc. (70%) and San Juan Basin Drilling Associates (30%). Meridian and San Juan completed two wells, the Ute 200 and Ute 201 wells, on the leases in November and December 1988. Another well, the Ute 1-2 well, had been recompleted by their predecessors-in-interest. The parties agree that all three wells received the necessary authorizations and approvals from the Tribe and the Department.

Beginning in 1984, the Federal Energy Regulatory Commission (FERC) issued a number of orders affecting the transportation of natural gas through pipelines. These orders, *inter alia*, encouraged pipeline companies to convert from purchaser/sellers of natural gas to open access transporters of gas. On June 10, 1988, Northwest accepted a permanent open access transportation certificate under FERC Order No. 500.

Northwest shut in Leases Nos. 1660 and 1661 on July 18, 1988. By letter dated September 30, 1988, Northwest notified the producers with which it had gas purchase contracts that it would terminate the contracts on November 1, 1988, pursuant to their “noneconomical purchases” provisions, unless the contracts were either revised to provide for “best effort” takes or assigned to Northwest’s sister company, the Williams Gas Supply Co., an unregulated entity.

On May 3, 1989, the Tribe informed the Superintendent, Southern Ute Agency, that no commercial production from the leases had been reported from August 1, 1988, through March 31, 1989. After
reviewing production reports, royalty payment reports, and tribal
severance tax returns, and ascertaining that appellant had not
requested approval for the shut-in; the Superintendent notified
appellant by letter dated May 5, 1989, that the leases had expired. The
Superintendent stated:

It has come to the attention of this office that there has been no commercial
production from the * * * leases during the period of August 1988 through March 31,
1989, the last reported period.

The absence of production on the * * * leases requires this office to conclude that the
leases have terminated and expired by their own terms. Accordingly, you are hereby
notified that said leases have expired, and that operations conducted by you, your agents
or employees on said premises should cease.

Past the primary term, the production in paying quantities is judged on a monthly
cycle, therefore, production is considered to have ceased prior to the August 1988
monthly cycle. These leases expired of their own terms, due to lack of production.

(Superintendent’s May 5, 1989, Letter at 1-2).

Appellant appealed this notification to the Area Director. On
June 28, 1989, pursuant to a request from the Tribe, the Area Director
ordered appellant to post an appeal bond in the amount of $1.5 million
and imposed certain conditions under which appellant was to be
permitted to manage the leases during the pendency of the appeal.
Appellant appealed this order to the Board. Before the appeal to the
Board was briefed, the Area Director decided the underlying appeal.
Accordingly, the Board dismissed the appeal pending before it as moot.

Mobil Oil Corp. v. Albuquerque Area Director, 17 IBIA 269 (1989).

On August 11, 1989, the Area Director affirmed the Superintendent’s
May 5 decision, stating in part:
The statute pursuant to which the * * * leases were issued, 25 USC 396a, further states
that the duration of such leases shall be “for terms not to exceed ten years and as long
thereafter as minerals are produced in paying quantities.” The * * * leases are in their
extended terms. Past the primary term, the production in paying quantities is judged on
a monthly cycle. The facts of this case clearly indicate that there was absolutely no
commercial production from the * * * leases during the period of August 1, 1988,
through March 31, 1989. The appellants do not dispute this fact of nonproduction. In this
case the statutory requirements of 25 USC 396a control and only Congress can change
the clear provisions of the statute. Therefore, production is considered to have ceased
prior to the August 1988 monthly cycle.

(Area Director’s Aug. 11, 1989, Letter at 1-2).

Appellant’s appeal from this decision was received by the Board on
September 8, 1989. Another appeal from the same decision was filed by
Meridian and San Juan; it was docketed as No. IBIA 90-3-A. The
appeals were consolidated on October 12, 1989.

On November 27, 1989, the Board approved an interim agreement
and stipulation between all appellants and the Tribe. The agreement,
which had been approved by the Superintendent,
provided: (1) Meridian and San Juan would conduct oil and gas
operations on lands embraced by the leases prior to final resolution of this dispute; (2) the Tribe would be paid royalties pursuant to the terms of the leases in dispute; (3) an additional payment, constituting a 4-percent overriding royalty interest before payout and a 12-1/2-percent overriding royalty interest thereafter, would be paid into an escrow account; (4) the escrowed funds would be disbursed to the Tribe if the decision at issue in this appeal is ultimately affirmed and to appellant if it is ultimately reversed; (5) in the event appellant prevails, operations may continue under the leases; and (6) in the event the Area Director’s decision is affirmed, the Tribe, Meridian, and San Juan will execute a Minerals Agreement that has been negotiated and agreed to by the Tribe, Meridian and San Juan. The Superintendent indicated by letter dated November 13, 1989, that he intends to approve the Minerals Agreement if the Area Director’s decision is affirmed.

On December 18, 1989, the Board received from Meridian and San Juan a motion for leave to withdraw from this appeal. The Board granted the motion and dismissed Docket No. IBIA 90-3-A on December 20, 1989. *Meridian Oil Inc. & San Juan Basin Drilling Associates v. Albuquerque Area Director, 18 IBIA 86 (1989).*

Appellant, the Area Director, and the Tribe filed briefs in Docket No. IBIA 89-102-A.

**Discussion and Conclusions**


> On and after May 11, 1938, unallotted lands within any Indian reservation or lands owned by any tribe, group, or band of Indians under Federal jurisdiction * * * may, with the approval of the Secretary of the Interior, be leased for mining purposes, by authority of the tribal council or other authorized spokesmen for such Indians, for terms not to exceed ten years and as long thereafter as minerals are produced in paying quantities.

Regulations implementing the IMLA are found at 25 CFR Part 211.

Appellant concedes that no oil and/or gas was produced from Leases Nos. 1660 and 1661 for a period of at least 6 months, *i.e.*, from c. July 18, 1988, through c. January 31, 1989,\(^4\) while the leases were in their extended terms. Even so, appellant contends, its leases did not expire. It advances a number of arguments in support of this contention: (1) the leases did not expire without a factual determination because 25 U.S.C. § 396a is not a self-executing statute; (2) appellant was denied due process; (3) the requirement that production during the extended term of the leases must occur during a 30-day cycle is an invalid unpublished rule; (4) the Area Director’s decision was arbitrary and capricious, an abuse of discretion, and

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\(^3\) All further references to the *United States Code* are to the 1982 edition.

\(^4\) In his answer brief, the Area Director concedes that the original statement that the period of nonproduction extended through Mar. 31, 1989, was incorrect (Area Director’s Brief at 18). The parties agree, however, that there was no production for at least 6 months.
inconsistent with underlying statutes; (5) BIA is estopped to hold appellant’s leases terminated because of its delay in informing appellant of the termination; (6) appellant has performed under the leases; and (7) appellant is excused from performance by force majeure.

Appellant characterizes its first argument as a threshold argument. The Board agrees. If, contrary to appellant’s view, 25 U.S.C. § 396a is a “self-executing” statute, in the sense that a lease in its extended term expires automatically when it ceases to produce in paying quantities, then many of appellant’s further arguments need not be reached.

Appellant argues that expiration of its leases was not automatic but required some action on the part of the Superintendent. Further, appellant contends, the Superintendent was required to follow the procedures for lease cancellation in 25 CFR 211.27, and his failure to do so was a denial of appellant’s right to due process.

[1] Appellant’s argument concerning the applicability of 25 CFR 211.27 is easily disposed of. The Board has previously held that a BIA determination that a lease has expired by its own terms does not constitute a cancellation of the lease. See Bekco Oil & Gas Corp. v. Acting Muskogee Area Director, 18 IBIA 202, 204 (1990). Accord Solicitor’s Opinion, “Oil and Gas Leases on Allotted Indian Lands,” 58 I.D. 12 (July 2, 1942). Accordingly, the Board holds that the Superintendent did not cancel appellant’s leases and was not required to follow the cancellation procedures in 25 CFR 211.27.

The Area Director and the Tribe argue that appellant’s leases expired automatically by the terms of the statute and the leases. The Tribe contends that, interpreted strictly, 25 U.S.C. § 396a requires automatic termination of a lease for any cessation of production during the extended term, no matter how temporary. The view that expiration is automatic and immediate is in accord with established Departmental interpretation. In the Solicitor’s Opinion cited above, the Acting Solicitor stated:

By what is known in the nomenclature of the oil industry as the “thereafter clause,” contained in section 2 of these leases, each lease specifies with particularity the conditions upon which extension of the lease beyond the 10-year period depends. Unless the conditions specified are met, it is firmly established that the lease terminates, not by forfeiture, but by expiration of the period fixed by the contract of the parties. * * * Neither payment of rent nor excuses for nonperformance can avoid that result. * * * No act or declaration of the lessee can revive the lease. * * * And no notice to the lessee of the expiration of the lease is required. * * * Under the “thereafter clause” as found in the usual oil and gas lease the lease terminates, after the primary term has expired, when production stops. In order to keep the lease alive it is not only necessary to take the oil from the ground but the oil must also be marketed in order to carry out the purposes for which the lease is made.

*25 CFR 211.27(a) provides:

"When, in the opinion of the Secretary of the Interior, the lessee has violated any of the terms and conditions of a lease or of the applicable regulations, the Secretary of the Interior shall have the right at any time after 30 days' notice to the lessee specifying the terms and conditions violated, and after a hearing, if the lessee shall so request within 30 days after issuance of the notice, to declare such lease null and void, and the lessor shall then be entitled and authorized to take immediate possession of the land."
Solicitor’s Opinion, 58 I.D. at 13, 14, 15.

A similar interpretation formerly governed oil and gas leases on public lands and was apparently the impetus for a 1954 amendment to section 17 of the Mineral Leasing Act of 1920, 30 U.S.C. § 226i, providing for, inter alia, notice and a period of at least 60 days in which a lessee may place a shut-in lease into a producing status in order to avoid termination of his lease. The House report on the amendment states:

Under existing law, if a discovery is made on a lease by a well capable of producing oil or gas in paying quantities but is shut off for various reasons, such as lack of transportation facilities, lack of market, etc., upon the shutting-off of such well, departmental decisions have held that if the lease is in its secondary term by virtue of the discovery well, it terminates when production ceases. The proposed amendment would continue the lease for 60 days or more after notice that he must place his well on a producing status.


No provision corresponding to this amendment appears in the IMLA. Appellant argues, however, that BIA should follow the same policy for Indian leases as Congress has legislated for public land leases, because “Congress saw that it was grossly unfair for producing leases to be terminated for justifiable temporary cessation of production. Congress did not indicate that what was considered unfair for public lands would be considered fair for Indian lands” (Appellant’s Opening Brief at 50).

The Board considered and rejected a similar argument, made with respect to cancellation of rights-of-way, in Star Lake Railroad Co. v. Navajo Area Director, 15 IBIA 220, 94 I.D. 353 (1987), aff’d, Star Lake Railroad Co. v. Lujan, 17 Indian L. Rep. 3052 (No. 88-2135 (D.D.C. Feb. 27, 1990)). In that case, the Board held that a statutory provision excusing nonuse of a right-of-way over public lands should not be read into the statutes governing rights-of-way over Indian lands because “[the] failure of Congress to include such a provision in the Indian right-of-way statutes, when it has included one in the public land statutes, is reasonably construed * * * as an indication of intent on the part of Congress to deal differently with these different types of land” and because “the general body of statutory law governing tribal lands reflects a policy quite different from the policy which guides the management of the public lands.” 15 IBIA at 238, 94 I.D. at 362.

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6 As amended, 30 U.S.C. § 226i provides in part:

“No lease issued under this section covering lands on which there is a well capable of producing oil or gas in paying quantities shall expire because the lessee fails to produce the same unless the lessee is allowed a reasonable time, which shall be not less than sixty days after notice by registered or certified mail, within which to place such well in producing status or unless, after such status is established, production is discontinued on the leased premises without permission granted by the Secretary under the provisions of this chapter.”

7 In affirming the Board’s decision, the district court noted: 

“The IBIA thoroughly considered related statutes that do provide for discretion and that excuse conditions of easements and other grants of public lands. * * * Given the difference between those statutes and the statute and regulations at issue here—the former specifically provide for such exceptions, while the Indian Right of Way Act does not—the IBIA properly declined to read similar exceptions into plaintiff’s grant of easement.”

(Footnotes omitted; emphasis in original). Star Lake Railroad Co. v. Lujan, 17 Indian L. Rep. at 3055.
For the same reasons, the Board rejects appellant’s argument here. As discussed below, the Federal policy governing Indian mineral resources includes a Federal trust responsibility to manage those resources for the benefit of the Indian owners and a rule requiring interpretation of ambiguities in the relevant statutes and regulations in favor of those Indian owners. These characteristics clearly distinguish the Federal policy for Indian mineral resources from the policy concerning mineral resources on the public lands.

Appellant’s leases are governed by the IMLA, the regulations promulgated thereunder, and the leases’ own terms. There is no provision in the IMLA which excuses nonproduction after the primary term of a lease. We turn therefore to the regulations and to the language of appellant’s leases.

Appellant argues that 25 CFR 211.19 and section 3(f) of its leases are force majeure provisions which excuse nonproduction in the circumstances of this case. 25 CFR 211.19 provides:

The lessee shall exercise diligence in drilling and operating wells for oil and gas on the leased lands while such products can be secured in paying quantities; carry on all operations in a good and workmanlike manner in accordance with approved methods and practice, having due regard for the prevention of waste of oil or gas developed on the land, or the entrance of water through wells drilled by the lessee to the productive sands or oil or gas-bearing strata to the destruction or injury of the oil or gas deposits, the preservation and conservation of the property for future productive operations, and to the health and safety of workmen and employees; plug securely all wells before abandoning the same and to shut off effectually all water from the oil or gas-bearing strata; not drill any well within 200 feet of any house or barn on the premises without the lessor’s written consent approved by the superintendent; carry out at his expense all reasonable orders and requirements of the supervisor relative to prevention of waste, and preservation of the property and the health and safety of workmen; bury all pipelines crossing tillable lands below plow depth unless other arrangements therefore are made with the superintendent; pay the lessor all damages to crops, buildings, and other improvements of the lessor occasioned by the lessee’s operations. *Provided*, That the lessee shall not be held responsible for delays or casualties occasioned by causes beyond the lessee’s control.

By paragraph 3(f) of its leases, appellant agreed to assume these obligations.

It is apparent that the proviso to 25 CFR 211.19 pertains to the obligations imposed upon the lessee in that section and would excuse, under certain circumstances, a lessee’s failure to meet those obligations. There is no indication, however, that the proviso is intended to modify 25 CFR 211.10, “Term of leases,” or the durational provisions of appellant’s leases.9

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* 25 CFR 211.10 provides: “Mining leases may be made for a specified term not to exceed ten years from the date of approval by the Secretary of the Interior, or his authorized representative, and as much longer as the substances specified in the lease are produced in paying quantities.”

* In some instances, the durational provisions of Indian leases have been explicitly modified to allow for nonproduction in circumstances such as those present here. The leases discussed in the Solicitor’s Opinion noted above contained such a modification. Section 2 of those leases provided that they were

Continued
To the contrary, another provision in Part 211 indicates that the regulations do not intend to alter the durational provisions of leases by excusing nonproduction in the circumstances present here. Section 211.14a permits the Secretary to authorize suspension of production in cases where “it is considered that marketing facilities are inadequate or economic conditions unsatisfactory,” in certain specified circumstances, i.e., where the tribe consents, where the lease is in its primary term, and where the lease is for minerals other than oil and gas. The clear import of this section is that suspensions are not permitted in circumstances other than those described. None of the conditions required by this section are present here—the Tribe did not consent; the period of nonproduction did not occur during the primary term; the lease was not for minerals other than oil and gas; and the Secretary did not authorize a suspension of production.

By their terms, neither the regulations in Part 211 nor appellant’s leases excused appellant’s nonproduction.

In addition to the language of the statute, the regulations, and the leases, the Board takes into consideration the Federal policy concerning oil and gas leasing on Indian lands, as expressed in congressional enactments and interpreted by the Federal courts.

[2] Congress has explicitly acknowledged that the administration of Indian oil and gas is a trust obligation of the United States. See section 2 of the Federal Oil and Gas Royalty Management Act of 1982, 30 U.S.C. § 1701. The Federal courts have held that the IMLA,
specifically, imposes fiduciary responsibilities upon the Federal Government. E.g., Assiniboine & Sioux Tribes v. Montana Board of Oil & Gas Conservation, 792 F.2d 782, 794 (9th Cir. 1986). Further, "[a]s a fiduciary for the Indians, the Secretary is responsible for overseeing the economic interests of Indian lessors, and has a duty to maximize lease revenues"; and BIA "must take the Indians' best interests into account when making any decision involving leases on tribal lands." Kenai Oil & Gas, Inc. v. Department of the Interior, 671 F.2d 383, 386, 387 (10th Cir. 1982).

Both the statutes and the regulations concerning Indian mineral resources are subject to the rule that enactments intended to benefit Indians must be liberally construed in their favor. Jicarilla Apache Tribe v. Andrus, 687 F.2d 1324, 1331-32 (10th Cir. 1982). Further, where the mineral leasing regulations may reasonably be interpreted in two ways, the trust responsibility requires that the Secretary choose the alternative which is in the best interests of the Indians. Jicarilla Apache Tribe v. Supron Energy Corp., 728 F.2d 1555, 1566-69 (10th Cir. 1984) dissenting opinion adopted as majority opinion, 782 F.2d 855 (10th Cir.) (en banc), cert. denied, 479 U.S. 970 (1986).

Under the principles enunciated in these cases, if there were any ambiguity in the statute or regulations as to whether appellant's nonproduction could be excused, it would have to be resolved in favor of the best interests of the Tribe. In this case, it seems apparent that the best interests of the Tribe coincide with the manifest intent of the regulations not to excuse nonproduction in circumstances such as are present in this case. The Tribe clearly considers the termination of appellant's leases to be in its best interests. The Tribe's assessment is supported by the fact that it has now negotiated a minerals agreement which it expects to yield it greater revenue than it received from appellant's leases.

[3] The case law concerning the administration of Indian mineral resources supports the conclusion that no provision of the IMLA, 25 CFR Part 211, or appellant's leases excused appellant's nonproduction. The Board holds, therefore, that appellant's nonproduction was not excused and that its leases have expired by operation of law.

[4] The Board briefly touches on some of appellant's remaining arguments. Appellant contends that its right to due process was violated because, inter alia, it was deprived of a substantial property right by the Superintendent's decision but was not given notice and an

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13 The Tribe states that it is presently a party to 17 minerals agreements under the Indian Mineral Development Act of 1982, 25 U.S.C. §§ 3101-2108, and that many of its agreements permit the Tribe to participate as a working interest owner in addition to being a royalty recipient. It notes that "[i]n investigative proceedings before the United States Senate Select Committee on Indian Affairs, held only several months ago, the Southern Ute Indian Tribe was broadly acclaimed for its sophistication in oil and gas resource management." (Tribe's Response to Appellant's Motion for Reconsideration of Appeal Bond and Interim Orders, July 26, 1989, at 10.)
opportunity to be heard before the decision was issued. As discussed above, however, appellant’s leases expired by operation of law, not by act of the Superintendent. The expiration had already occurred at the time the Superintendent wrote his May 5, 1989, letter to appellant. 14

Unlike 30 U.S.C. § 226(i), the IMLA does not require that notice be given before leases may expire by their own terms. In this regard, the IMLA resembles an Indiana statute concerning the lapse of unused mineral interests which was addressed by the Supreme Court in *Texaco, Inc. v. Short*, 454 U.S. 516 (1982). Rejecting an argument that the absence of specific prior notice rendered ineffective the self-executing feature of the statute, the Court stated:

> The State of Indiana has enacted a rule of law uniformly affecting all citizens that establishes the circumstances in which a property interest will lapse through the inaction of its owner. None of the case cited by appellants suggests that an individual must be given advance notice before such a rule of law may operate.

454 U.S. at 537.

The Superintendent’s letter informed appellant of its right to appeal to the Area Director under 25 CFR Part 2. Appellant has participated fully in all proceedings before the Area Director and this Board. The Board finds that, in the circumstances of this case, appellant’s due process rights have been adequately protected by the administrative review procedures in 25 CFR Part 2 and 43 CFR Part 4 Subpart D. *See Martineau v. Billings Area Director*, 16 IBIA 104 (1988).

Appellant also argues that the Superintendent relied on a rule of his own devising when he stated that “production in paying quantities is judged on a monthly cycle.” Such a rule, appellant contends, is invalid because not published in accordance with the Administrative Procedure Act (APA), 5 U.S.C. § 553. The Superintendent’s letter, however, is clearly not a rule within the meaning of the APA. 15 In any event, inasmuch as neither the IMLA nor 25 CFR Part 211 allow any grace period following cessation of production, appellant’s leases technically expired immediately upon cessation of production. The Superintendent’s allowance of a “monthly cycle” in which to judge production was therefore to the advantage of appellant, rather than to its detriment. For this reason, and for the even more obvious reason that appellant’s leases were in a state of nonproduction for 6 months, it is clear that the Superintendent’s reference to a “monthly cycle” did no harm to appellant. Even if error, therefore, it was harmless error.

Appellant’s remaining arguments have been considered and rejected, in light of the conclusions reached above.

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14 Accordingly, the Superintendent’s letter is perhaps more properly characterized as a notice of expiration than as a decision. Such notifications are fully appealable under 25 CFR Part 2. *Bekco Oil & Gas Corp.*, supra.

15 5 U.S.C. § 551(4) defines “rule” as “the whole or a part of an agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy or describe the organization, procedure, or practice requirements of an agency and includes the approval or prescription for the future of rates, wages, corporate or financial structures or reorganizations thereof, prices, facilities, appliances, services or allowances therefor or of valuations, costs, or accounting, or practices bearing on any of the foregoing.”
Therefore, pursuant to the authority delegated to the Board of Indian Appeals by the Secretary of the Interior, 43 CFR 4.1, the Albuquerque Area Director's August 11, 1989, decision is affirmed.

ANITA VOGT
Administrative Judge

I CONCUR:

KATHRYN A. LYNN
Chief Administrative Judge

APPEALS OF MONTEREY CONSTRUCTION CO.

IBCA-2627-2634 Decided: July 17, 1990

Contract No. 5-CC-57-00690, Bureau of Reclamation.

Decision Approving ADR Settlement.


Boards of Contract Appeals have jurisdiction to make awards pursuant to the Contract Disputes Act upon determining that private settlements entered into by the parties appear reasonable and that their ratification by the Board having jurisdiction over the appeal is in the best interests of the Government.

APPEARANCES: Val S. McWhorter, Esq., Smith, Pachter, McWhorter, D’Ambrosio, Vienna, Virginia, for Appellant; William A. Perry, Esq., Department Counsel, Denver, Colorado, for the Government.

OPINION BY ADMINISTRATIVE JUDGE PARRETTE

INTERIOR BOARD OF CONTRACT APPEALS

These appeals were docketed by the Board on April 3, 1989. The contract in question, entered into by the Bureau of Reclamation (BOR/Government) on December 14, 1984, involved the construction of the Brantley Dam, located on the Pecos River approximately 15 miles north of Carlsbad, New Mexico (the project), by the Monterey Construction Co. (Monterey/appellant), a division of Guy F. Atkinson Co. The price stated in the contract for the project was $44,800,770.

However, appellant allegedly encountered differing site conditions and defective specifications, as well as Government changes and other requirements for additional work, in discharging its responsibilities under the contract, and thereby incurred more than a year’s delay and very substantial monetary losses for which the Government was allegedly responsible, in the total amount of $56,787,900—not including
interest, attorney fees, costs, and amounts relating to two separate subcontractor appeals in the contractor's name.

After granting the Government's request for an extension of time for preparation and shipment, the Board by the end of October 1989 had received approximately 150, 3-inch, loose-leaf notebooks as part of the appeal (Rule 4) file in the case; and at that point it began its efforts to have the parties stipulate as many matters as possible prior to the hearing, which was scheduled for the entire months of November and December 1990 and was expected to occupy much of both the parties' and the Board's time for nearly 6 months, even without likely time extensions and possible witness complications.

The pendency of this matter was thus instrumental in the Board's February 15, 1990, decision to adopt and encourage Alternative Disputes Resolution (ADR) procedures in connection with all of its pending and future appeals. On the same date, the Board wrote to the parties involved here, calling their attention to its adoption of ADR, providing them with materials pertaining to ADR resolutions in similar Army Corps of Engineers cases, and offering to assist them in every practicable way if they were willing to attempt an ADR resolution of the appeals.

Counsel for the parties maintained frequent communication between themselves and with the Board, and by letter dated June 8, 1990, they confirmed understandings reached during a June 7 meeting that appellant had sufficiently established its actual costs (on the basis of a modified total cost approach) that the claims had the value alleged by appellant, and that this figure would be the basis of any further negotiations between the parties. Appropriately, the Board was not notified of this agreement at the time.

On June 15, 1990, following a conference call with the Board on other matters, which confirmed that ADR efforts were still being undertaken, the Board wrote to the parties asking for a list, within 30 days, of principal issues to be tried, stating whether they were factual, legal, or both, and for advice on how the matters raised could best be resolved.

At that point, the parties again called the Board to say that they had agreed to seek mediation of their dispute, and that the mediation session would be held in Salt Lake City July 11 and 12, or until completed, under the auspices of the American Arbitration Ass'n, with the costs of the mediation to be shared by the parties. The Board agreed to defer its request for a statement of issues until the mediation sessions had been completed, but asked for their results to be reported to it no later than July 16.

The subsequent mediation session consisted of a joint statement of facts and issues presented to the mediator, followed by a 10-page brief by each of the parties summarizing their individual contentions in the case. The mediator then met with each party separately on different days, followed by a joint meeting at which only counsel and a principal of each party possessing settlement authority were present.
The parties' principals, consisting of the Deputy Assistant Commissioner of BOR responsible for the project and of the Senior Vice President and Secretary of the Atkinson Company, agreed to a final settlement figure of $45,500,000 for all contractor claims, of which $2,218,193 represented a gross receipts tax under the laws of the State of New Mexico and $7,492,436 had already been paid. The Government agreed to pay interest (at a rate calculated in accordance with the provisions of the Contract Disputes Act (CDA)) in the amount of $10,017,219 through June 30, 1990, with a daily rate of $11,219 thereafter through December 31, 1990. Thereafter, a Treasury-determined CDA rate would apply until payment, if payment had not been made by then. Both sides agreed to release each other from all other liability arising under the contract on the basis of facts then known to them, except for the subcontractor claims previously referred to, which were docketed under other IBCA numbers. They also agreed to submit their Stipulation of Settlement to the Board for an entry of judgment in the amount stated. A representative of the Department's Inspector General's office participated in the preparation of the settlement stipulations.

The Board was informed by the parties by conference call of the terms of the proposed stipulation before it was signed, was subsequently briefed by both counsel on the matter, and has also discussed it with them as to both substance and procedures. It has further examined the record before the Board in the matter, as well as the joint and individual statements presented to the mediator, and has determined that the proposed settlement is reasonable. It therefore concurs both in the proposed resolution of the matter and in the amount of the settlement involved.

Based upon numerous precedents by other boards, we find that boards of contract appeals have jurisdiction to make awards pursuant to the CDA upon determining that private settlements entered into by the parties are reasonable and that their ratification by the board having jurisdiction over the appeal is in the best interests of the Government. We so find in this matter.

Accordingly, the settlement stipulation is hereby approved, and appellant is awarded judgment in the amounts set forth above, subject only to the terms and conditions of the stipulation being carried out. A copy of the approved Stipulation of Settlement and Mutual Release, dated July 13, 1990, is appended to this decision for reference.

Bernard V. Parrette
Administrative Judge

I concur:

G. Herbert Packwood
Administrative Judge
CERTIFICATION

I certify that the foregoing is a true copy of the decision of the Interior Board of Contract Appeals in the Appeals of Monterey Construction Co., IBCA Nos. 2627 through 2634, rendered in conformance with its charter. Dated:

[JULY 17, 1990]

EDWARD P. DRONENBURG
Recorder

APPENDIX

United States Department of the Interior
Office of Hearings and Appeals
Board of Contract Appeals

Appeal of MONTEREY CONSTRUCTION CO., A DIVISION OF GUY F. ATKINSON CO.

IBCA-2627, 2628, 2629, 2630, 2631, 2632, 2633, 2364

Contract No. 5-CC-57-00690.

STIPULATION OF SETTLEMENT & MUTUAL RELEASE

1. The appeals referenced above are pending before the Interior Board of Contract Appeals (Board). The amount in dispute totals $56,787,900.00.

2. It is the mutual desire of the parties, Monterey Construction Co. (Contractor) and the United States Bureau of Reclamation (Government), to avoid further controversy and to settle all existing differences between them regarding the facts and law involved in these appeals, and the subject contract.

3. As a result of mediation between the parties, under the auspices of the Board, the Government, and the Contractor have agreed to a settlement of the issues involved in these appeals and do hereby stipulate that the terms of this settlement are set forth below.

4. It is agreed that the Contractor encountered differing site conditions at the site of the work.

5. It is agreed that the Contractor attempted to perform the contract work under defective specifications.

6. It is agreed that the differing site conditions and defective specifications caused changes and additional work and increased the Contractor's costs of performing the work and its planned contract performance.

7. It is agreed that the Contractor performed changes and additional work at the Government's direction, also increasing the Contractor's
costs of performing the work and its planned contract performance time by 433 days.

8. It is agreed that the foregoing differing site conditions, defective specifications, changes, and additional work entitle the Contractor to additional compensation in the amount of $45,500,000.00 (Settlement Amount), and that the Government will adjust the contract price to reflect this Settlement Amount, as it shall be adjusted in accordance with the terms of this Stipulation.

9. It is agreed that the Settlement Amount includes compensation for the Contractor’s increased time of performance.

10. It is agreed that the Government has previously paid the Contractor $7,492,436.00 as partial compensation for its increased costs of performance and that the Contractor will credit this amount against the Settlement Amount. It is further agreed that the $7,492,436.00 represents payments for the Contractor’s claims only, and not for the claims of any subcontractor.

11. It is agreed that the Settlement Amount includes a payment of $2,218,193.00 representing the gross receipts tax due on the principal amount of $43,281,807.00 under the laws of the State of New Mexico.

12. It is agreed that the Government shall pay interest on the Settlement Amount as follows:

A. The Government will pay $10,017,219.00 as the amount of interest due on the Settlement Amount, through June 30, 1990.

B. The amount of interest due on the Settlement Amount for the period July 1 through December 31, 1990 is at a daily rate of $11,219.00.

C. The amount of interest paid on the Settlement Amount for the period after December 31, 1990 shall be in accordance with the Department of the Treasury rates fixed by law, on the full amount remaining due until payment thereof.

13. It is agreed that, unless specifically excepted in this Stipulation of Settlement and Mutual Release, the Contractor does hereby release the Government from any and all liability for claims, demands, disputes, or any other issues arising out of the performance by the Contractor of Contract No. 5-CC-57-00690, which liability is predicated on facts known to the Contractor at the time of this Stipulation of Settlement and Mutual Release.

14. It is agreed that, unless specifically excepted in this Stipulation of Settlement and Mutual Release, the Government does hereby release the Contractor from any and all liability for claims, demands, disputes, or any other issues arising out of the performance by the Contractor of Contract No. 5-CC-57-00690, which liability is predicated on facts known to the Government at the time of this Stipulation of Settlement and Mutual Release.
15. It is agreed that the matters docketed before the Board as IBCA Nos. 2493 and 2641, the appeals of the Contractor's subcontractors, are specifically excepted from this Stipulation of Settlement and Mutual Release. No other exceptions exist.

16. It is agreed and understood that payment under this Stipulation is contingent upon the availability of funds and that the Government will use its best efforts to seek funding for and pay the Settlement Amount along with appropriate interest within a reasonable period of time and that the Mutual Release shall not operate against the Contractor until such time as the Government has paid the full Settlement Amount and all interest due thereon.

17. It is agreed that for the purposes of any and all Warranty liability on the part of the Contractor under the contract, final acceptance of all work under the contract occurred on July 28, 1989.

18. It is agreed that in the event, for any reason whatsoever, this Stipulation should fail to become operative and binding upon the parties, then it shall be of no force and effect whatsoever, either as an admission by either party or otherwise, and the rights of the parties shall be the same as though this document had never been executed.

19. It is agreed that this Stipulation will be submitted jointly by the parties to the Interior Board of Contract Appeals for entry of Judgment in the amount of $45,500,000.00, plus interest in the amounts set forth in this document.

Dated this 13th day of July 1990.

FOR THE UNITED STATES:
J. Austin Burke
Deputy Assistant Commissioner
Bureau of Reclamation

William A. Perry
Department Counsel

FOR THE CONTRACTOR:
Robert D. Langford
Senior Vice President &
Secretary
Guy F. Atkinson Co.

Val S. McWhorter
Attorney for Appellant

APPEAL OF NOSLOT CLEANING SERVICES, INC.
IBCA-2554
Decided August 14, 1990

Contract No. GS-11P-87-MJC-0069, Office of Personnel Management.

Appellant's Request for Issuance of Subpoenas Denied.
August 14, 1990


A request for the issuance of subpoenas is denied where the Board finds (i) that instead of proceeding with voluntary discovery in an orderly and timely manner, appellant precipitately filed an application for the issuance of subpoenas to three Government employees calling for them to appear as appellant’s witnesses at a requested oral hearing and to bring with them to the hearing voluminous Government records; (ii) that in the absence of appellant’s counsel having had an opportunity to review the documents requested prior to the hearing and to winnow therefrom material irrelevant to the issues involved in the appeal, the granting of the subpoenas requested would confront the Board at the hearing with the choice of either delaying the commencement of the hearing while the winnowing process took place or encumbering the record with a great deal of extraneous material by accepting into evidence all of the documents covered by the subpoenas; and (iii) that resort to either of these alternatives would not be compatible with the requirement that the Board’s rules be interpreted so as to secure a just and inexpensive result without unnecessary delay.

APPEARANCES: David L. Schneier, Attorney-at-Law, Bethesda, Maryland, for Appellant; James S. Wright, Jr., Senior Litigation Counsel, Office of Personnel Management, Washington, D.C., for the Government.

OPINION BY ADMINISTRATIVE JUDGE McGRAW

INTERIOR BOARD OF CONTRACT APPEALS

Appellant’s counsel having requested that the instant appeal be reinstated, the request is granted and the above-captioned appeal is hereby restored to the Board’s active docket.

In its April 26, 1990, letter, appellant (Noslot/appellant/contractor) also requests that the Board issue subpoenas for three Government employees to appear as witnesses for appellant at the requested oral hearing and to bring with them to the hearing voluminous Government documents. Before undertaking to determine whether Noslot has made out a case for the issuance of the requested subpoenas, it would perhaps be well to provide some background against which the disparate contentions of the parties may be viewed.

Background

The contract here in issue was awarded pursuant to a solicitation calling for the furnishing of custodial services for Federal Office Building No. 9, 1900 E Street, NW., Washington, D.C. (Appeal File, Exhibit 1; hereinafter AF, Exh. 1). The solicitation required services to be provided for an initial period of 1 year, effective October 1, 1987, through September 30, 1988, with an option in the Government to extend the terms of the contract for four additional 12-month periods. Following verification of appellant’s bid, award of the contract was made to Noslot on July 22, 1987, at the price bid for the initial year of $435,264 (AF, Exhs. 3 and 4, tabs A-D).
In its claim letter of April 8, 1988, the contractor requested that the contract price be increased by the sum of $64,866.80 for the initial year. Noslot also claimed an additional sum of $4,368 on the stated ground that the wage determination attached to the solicitation had failed to show a pension contribution requirement. According to the claim letter, the Government had failed to provide Noslot with information which would have made the prospective contractor aware that the daily population of the Office of Personnel Management (OPM) building could be increased by approximately 300,000 visitors annually (AF, Exh. 6).

In the decision from which the instant appeal was taken, the contracting officer (CO) found, inter alia, (i) that while the contractor may not have been provided with specific information about the number of daily visitors to the OPM building in the solicitation or during the site visit, bidders were encouraged to satisfy themselves regarding all general and local conditions that might affect the cost of contract performance; (ii) that the evidence submitted by Noslot did not show that the underestimation of the work required had resulted from faulty specifications or inadequate information provided during the building survey; and (iii) that the doctrine of superior knowledge on the part of the Government did not apply in the circumstances involved in the instant appeal (AF, Exh. 9).

Appellant's April 26, 1990, letter to the Board requests that subpoenas be issued for attendance at the oral hearing of (1) Mary E. Holloway, GSA National Capital Region, 7th and D Streets, SW., Washington, D.C. (the contract specialist involved with the solicitation), who is expected to testify as to the manner in which the solicitation was conducted, what the prospective bidders were told about the use of the OPM building by the public, the anticipated use of the Federal Job and Retirement Centers, and vendor use in the building; (2) Martin J. Carter, OPM, 1900 E Street, NW., Washington, D.C. (in charge of site visit), who will be able to testify as to what prospective bidders were told and shown at the site visit; and (3) Teressa Gibson, Director, OPR Real Property Contracts Division.

In addition, the application requests that the following documents be brought to the hearing by Ms. Mary E. Holloway:

[A]ll documents she has as to Contract No. GS-11P-87-MJC-0069 including the solicitation [sic], bid proposals, correspondence or memos to or from OPM as to specific needs or circumstances involving the OPM building or any other correspondence concerning the solicitation and award of the above-mentioned contract, contracts, amendments, written recommendations of award, award letters, procurement case summaries, contractor claims, price adjustments and findings, performance standards used to develop terms and conditions of janitorial specifications for janitorial contracts, and documentation as to the number of visitors to the OPM building generally to the Federal Job and Retirement

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1 In its complaint appellant states: "Noslot hereby withdraws its claim of $4,368.00 for the pension contribution inadvertently omitted from its bid costs."

The complaint increased the amount of the claim to $76,170.80 per year. Assuming the Government were to exercise its option to renew the contract for the 4 additional years permitted by the contract, the total claim would be in the amount of $380,854.
centers specifically, and use of the buildings by vendors from 1984 through the date of the award of the contract to Noslot. [2]

According to appellant's counsel, he is requesting the subpoenas for the General Services Administration (GSA) because he has not received the above-listed documents pursuant to the requests made earlier in his letters of February 3, 1989, and January 29 and March 27, 1990.

In a letter to the Board dated May 2, 1990, Government counsel contests the accuracy of a number of the representations made by appellant's counsel in the application to the Board for the issuance of subpoenas. Apropos the statement that a subpoena for documentation in the custody of GSA was being requested only because such documents were not received in response to an earlier request made in a letter dated February 3, 1989, Government counsel states (i) that the February 3, 1989, letter was addressed to OPM; (ii) that all documents in OPM's possession covered by that letter were promptly made available to Noslot; (iii) that at the time such documents were made available to Noslot, appellant's counsel was told that OPM had no control over the production of documents in the possession of GSA but upon request the identity of the GSA official who did control those documents would be supplied; (iv) that it was only shortly before the target date for completion of voluntary discovery that the identity of the GSA official in charge of the GSA records in question was requested by appellant's counsel, and (v) that in response to that request the name and telephone number of the GSA official in charge of the GSA records covered by the February 3, 1989, letter was furnished. The nature of the impasse reached in regard to continuing with voluntary discovery is reflected in the letter of May 2, 1990, from Government counsel from which the following is quoted:

At the deposition of Mary Holloway, a GSA procurement official, held on February 7, 1990, one week after the discovery deadline of January 31, 1990, Mr. Schneier again requested access to the documents in GSA's control. Mr. James Vranekovic, GSA Assistant Regional Counsel, and I informed him that since no proper request for these voluminous documents had been made in a timely manner, the documents would not be made available on an informal basis.

Discussion

At least some of the problems encountered by Noslot in obtaining access to records in the custody of GSA appears to have stemmed from the haphazard manner in which appellant had proceeded with voluntary discovery. The Complaint was filed on October 11, 1988, and counsel for appellant entered his appearance on November 21, 1988. No discovery was initiated by Noslot until February 3, 1989, however,

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2 The application for subpoena states that "Mr. Carter should bring with him any documents he may have that are listed for Ms. Holloway, as well as the visitor documents specified above from 1984 through the present." The application characterizes the subpoena for Ms. Gibson as "a subpoena for a document request only for the documents listed for Ms. Holloway for all janitorial contracts and solicitations for the O.P.M. building (Federal Bldg. #9) for the contracts solicited in 1981, 1984 and 1987" (Letter to Board from appellant's counsel dated Apr. 26, 1990, at 1-2).
when by a letter of that date the Government was requested to furnish numerous documents. Although the record shows that only documents in the possession of OPM were supplied to appellant, no action pertaining to discovery appears to have been taken until October 27, 1989, when, in response to our order dated October 6, 1989 (directing the parties to furnish a schedule for the completion or discovery), Noslot advised the Board that both counsel estimated that discovery would be completed by January 31, 1990. The record shows that appellant did not proceed with discovery until shortly before January 31, 1990 (i.e., the target date agreed upon by the parties for the completion of voluntary discovery). Only after the dismissal of the appeal without prejudice on April 20, 1990, did Noslot request the Board to issue the subpoenas here in issue by its letter of April 26, 1990.

The impasse reached may have resulted in part from a misconception by the Government that some form of sanctions are available for a party's failure to meet a target date for the completion of voluntary discovery. To the Board's knowledge, however, sanctions have never been imposed in connection with matters related to voluntary discovery. See, for example, *Alisa Corp.*, AGBCA No. 84-193-1 (July 23, 1986), 86-3 BCA par. 19,139; *Able Contracting Co.*, ASBCA No. 27411 (Mar. 25, 1985), 85-2 BCA par. 18,017 at 90,385 (“The Government seeks sanctions for Biele's lack of cooperation with voluntary discovery. Sanctions, however, are appropriate only for refusal to comply with a Board order”).

The record also indicates that the Government may have had some doubts as to whether documents in the possession of third parties were subject to discovery in a board proceeding. Prior to the passage of the Contract Disputes Act of 1978 (CDA), 41 U.S.C. §§ 601-613, boards of contract appeals (absent special statutory authority) consistently refused to issue discovery orders requiring testimony from third parties or requiring them to provide documents in their possession, as it was considered that third parties were not within the purview of their jurisdiction. See *Unicon Management Corp.*, VACAB Nos. 470 and 515 (Aug. 12, 1968), 68-2 BCA par. 7180 at 33,319 (“We find no basis in the Discovery Rule for requiring the Government to seek out and procure, for Appellant's benefit, documentary evidence that belongs to, and is in the possession of, an independent party”); *Carl W. Olson & Sons*, IBCA No. 930-9-71 (Apr. 15, 1974), 81 I.D. 182, 74-2 BCA par. 10,724; *Iverson Construction Co.*, IBCA No. 981-1-73 (May 1, 1973), 80 I.D. 299, 73-1 BCA par. 10,019; and *Felton Construction Co.*, AGBCA No. 406

Sanctions have been imposed by boards of contract appeals in a variety of circumstances, as is exemplified by *W. H. Kruger*, ASBCA No. 33081 (July 20, 1988), 88-3 BCA par. 21,943 (sanctions imposed for contracting officer's failure to respond to contractor's settlement proposal even after being directed to do so by the Board); *Ralph Construction, Inc.*, ASBCA No. 39639 (Mar. 22, 1988), 88-3 BCA par. 20,721; (two Government witnesses not permitted to testify at hearing where Government had refused to permit the witnesses to be interviewed even after the board had instructed the Government to make the two prospective Government witnesses available for questioning); and *Evergreen Engineering Inc.*, IBCA No. 994-5-73 (Oct. 29, 1974), 81 I.D. 615, 74-2 BCA par. 10,906; 85 I.D. 197, 78-2 BCA par. 13,295 (claim submitted on behalf of asphalt subcontractor denied where the appellant failed to answer interrogatories pertaining to subcontractor's claim).
Concerning the significance of these decisions to present board practice, a commentator states: "These cases have become academic because Section 11 of the Contract Disputes Act of 1978 gives the appeal boards the power to issue subpoenas" (McBride & Touhey, Vol. 1A, Section 6.20[9][F]).

Very recently in the case of Heritage Reporting Corp., GSBCA No. 10596 (May 15, 1990), 90- BCA par.6 (involving a Federal Supply Schedule contract), the GSA Board of Contract Appeals denied a motion to quash a subpoena filed by the Department of Justice (a third party and user agency), even though the subpoenas called for the furnishing of thousands of documents. After finding the documents requested to be relevant to the issues involved in the appeal, the GSA board stated: "since respondent does not possess this information, subpoenaing them from mandatory user agencies like DOJ is the only way appellant can secure them. Thus, we will not quash the subpoena" (Slip op. at 3).

Turning to the case at hand, the Board notes that in the application appellant does not cite our Rule 4.120 governing the issuance of subpoenas; nor does the application state "the reasonable scope and general relevance to the case of the testimony and of any books and papers sought," as required by that rule (43 CFR 4.120(c)(2). The application for subpoenas appears to be deficient in other respects as well. From the listing of the documents sought, it is not apparent that all of the documents requested are in existence (see Blount Bros., Corp., GSBCA No. 1385 (June 8, 1965), 65-2 BCA par. 4898). There is also a question as to whether compliance with some of the discovery requests would require the Government to engage in research or to make compilations from records in its possession. See Allison & Haney, Inc., IBCA-587-9-66 (June 19, 1967), 74 I.D. 178, 67-2 BCA par. 6401. While the decisions in Blount Bros., supra, and in Allison & Haney, supra, did not involve requests for the issuance of subpoenas, it is well established

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1 Cf. Essex Electro Engineers, Inc., DOT CAB No. 1025 (Apr. 16, 1980), 80-1 BCA par. 14,387, in which the Transportation Board granted the appellant's motion to quash a subpoena ducem tecum where it found that the Government had failed to show a "general relevance and reasonable scope" of the documents requested, as required by the Board's rules. The rules of this Board require that "a request for a subpoena shall state the reasonable scope and general relevance to the case of the testimony and of any books and papers sought." 43 CFR 4.120(c)(2).

2 In Blount Bros. (text, supra), the General Services Board stated:

"The purpose of the discovery rule, as we understand its legal significance, is not to discover what exists, but to force the production of records that do exist. An order to produce should not be entered until the existence of the desired documents is established. Whether a particular document exists, what its nature may be, and in whose custody it may lie, may be ascertained through deposition or by interrogatory." 65-2 BCA at 23,188.

3 In Allison & Haney, (text, supra), this Board offered the following comments:

"The Government contends that it is not obliged to prepare appellant's case. Its point is well-taken. A party ordinarily will not be required to 'make research and compilation of [data] not readily known to him.' This is precisely what the Government is being called upon to do. Moreover, the information here sought by interrogatory is more appropriate to the device of a motion for the production of documents, as the Government impliedly recognized when it voluntarily expressed its willingness to make available to the contractor at the contracting officer's office the various papers which might reveal the data sought by these questions." 74 I.D. at 185-86; 67-2 BCA at 29,877 (footnotes omitted).
that the subpoena process is subject to the rules governing discovery. 


Perhaps answers to some of the questions raised were provided by Ms. Holloway in her deposition to which the application for subpoenas refers. For present purposes the Board need not be concerned with answers to these questions, however, since whatever the answers may be the issuance of the subpoenas in the form requested and under the circumstances present here would not be conducive to an inexpensive and expeditious resolution of the issues involved in this appeal. Here, instead of proceeding with voluntary discovery in an orderly and timely fashion as contemplated by our rules, appellant precipitately filed an application for the issuance of subpoenas to three Government employees and in connection therewith requested that voluminous Government records be brought to the hearing. In the absence of appellant’s counsel having had an opportunity to review the documents requested in the subpoenas in advance of hearing and to winnow therefrom what is irrelevant to the issues involved in the appeal, the issuance of the requested subpoenas would confront the Board with the choice of either delaying the hearing while the winnowing process took place or encumbering the record with a great deal of extraneous material by accepting all of the subpoenaed documents into evidence. Neither alternative is considered to be compatible with our Rule 4.100(e)(3) which states: “These rules will be interpreted so as to secure a just and inexpensive determination of appeals without unnecessary delay.” 43 CFR 4.100(e)(3).

Accordingly, for the reasons stated and based upon the authorities cited, appellant's request for the issuance of subpoenas is denied as premature.

Outline of Principles Governing Discovery & Directions to Parties Concerning Future Discovery

In ruling upon motions or requests for discovery, the Board will be guided by the following principles:

1. The general principle favoring discovery will be given a broad application and the exceptions thereto will be narrowly construed. 


2. Ordinarily, a discovery request will be granted if the documents sought are relevant to the matters in dispute or are reasonably calculated to lead to the discovery of admissible evidence, unless allowing the discovery would be prejudicial or oppressive to the parties

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7 In Shakespeare (text, supra), the Court of Claims stated:

"There is, and can be, no contention that the use of a subpoena duces tecum does not apply to the government in a case such as this. Kanen Soap Products Co., Inc. v. United States, 124 Ct.Cl. 519, 541, 110 F.Supp. 430, 442 (1963).

"If a proper showing is made of good cause we do not hesitate to order production either on motion for discovery or by subpoena process. However, as we stated earlier, the subpoena process is in the nature of a discovery and thus must meet discovery standards. In other words, something more than a fishing expedition must be shown." 182 Ct.Cl. at 126.

3. Claims of privilege will be closely scrutinized. Anyone asserting a claim of privilege has a heavy burden to overcome the normal process of requiring full disclosure in order to ascertain the facts. Automar IV Corp., DOT CAB No. 1867 (May 26, 1988), 88-2 BCA par. 20,821; 88-3 BCA par. 20,846; 88-3 BCA par. 20,854.

4. In ruling upon objections to discovery, the Board “will require that the objections be particularized and in detail. It will require that documents or portions of documents be clearly identified, that the objection be stated specifically and the grounds thereof be set forth in detail.” Airco, Inc., IBCA-1074-8-75 (Oct. 17, 1977), 84 I.D. 838, 844, 77-2 BCA par. 12,809 at 62,320.

5. When discovery is resisted, the burden is on the objecting party to establish legitimate reasons for withholding discovery. Dawson Construction Co., VABCA No. 1967 (June 21, 1985), 85-3 BCA par. 18,209 at 91,391.

In the absence of the parties arriving at a mutually acceptable arrangement for future discovery (e.g., the documents to be furnished, the depositions to be taken) and so advising the Board within 20 days from the date of receipt of this decision, the parties shall proceed with discovery in the manner and within the timeframe set forth below:

1. Within 20 days from the date of receipt of this decision, a party who wishes to initiate discovery shall file with the Board a motion for order directing (the other party) to provide documents (and to answer interrogatories if that is desired). The documents to be furnished (specifically identified) and the interrogatories to be propounded (if any) shall be included with the motion for order as separate documents and shall have appropriate captions such as “Request for Production (Exhibit A)” or “(Appellant’s or Government’s) First Set of Interrogatories (Exhibit B).”

2. Within 20 days from the date of receipt of an order granting permission to proceed with discovery, to the extent indicated therein, the party to whom the discovery requests are addressed shall respond thereto and, in connection with any refusal to comply with a particular discovery request, the response shall set forth in detail the reason or reasons for such refusal accompanied by citation to any authorities the party wishes the Board to consider in reaching a decision on the refusal or refusals.

3. After the first round of discovery has been completed, the Board will entertain motions for permission to take oral depositions or depositions upon written interrogatories.

4. If a party is dissatisfied with the results obtained in the preceding rounds of discovery, that party (or the parties) may file with the Board an application (or applications) for the issuance of subpoenas to persons to testify at the requested oral hearing. It is assumed that the
documents relevant to the appeal will already have been furnished in response to a party's request or as a result of the Board having ruled upon questions raised concerning particular documents.

It is anticipated that the above time constraints will be adhered to and that discovery will be completed in sufficient time to permit the scheduling of the requested oral hearing in November or December of this year.

William F. McGraw
Administrative Judge

I concur:

G. Herbert Packwood
Administrative Judge
FOREST OIL CORP. (ON RECONSIDERATION)


Petition granted; decision reaffirmed.

1. Federal Oil and Gas Royalty Management Act: Royalties--Oil and Gas Leases: Royalties: Generally--Outer Continental Shelf Lands Act: Oil and Gas Leases

Although royalty underpayments are improper by definition and may, under some circumstances, subject the payor to civil and/or criminal penalties, the issue in the context of a royalty audit is what, if any, additional royalty is due and owing to the lessor. Where an audit is made of royalty payments for an oil and gas lease, underpayments disclosed by the audit are properly offset by royalty overpayments on the same lease revealed within the period of the audit regardless of the fact that the underpayments were intended to recoup the prior overpayments.


OPINION BY ADMINISTRATIVE JUDGE GRANT

INTERIOR BOARD OF LAND APPEALS

Counsel for Minerals Management Service (MMS) has filed with the Board a Motion for Partial Reconsideration of the Board's decision in this case, cited as Forest Oil Corp., 113 IBLA 30, 97 I.D. 11 (1990). MMS seeks reconsideration on the issue of whether overpayments of royalty disclosed during the audit of an offshore oil and gas lease may be offset against royalty underpayments which resulted when the payor recouped the overpayments on subsequent monthly reports. Although the overpayments were not the subject of a formal refund request filed within 2 years of the payment, Forest has asserted the recoupments were filed within 2 years of the overpayment. MMS points out that the Board has upheld prior MMS decisions disallowing the taking of credit adjustments on Form MMS-2014 to offset past overpayments. It is asserted that such credit adjustments contravene the provisions of section 10 of the Outer Continental Shelf Lands Act (OCSLA), 43 U.S.C. § 1339 (1982), requiring formal application for a refund within 2 years of the overpayment. Concern is expressed by MMS that the result of our decision will be to encourage payors to unilaterally recoup overpayments without applying for refunds.

MMS seeks to distinguish this case from others where the Board has upheld the offsetting of overpayments against underpayments on a lease account during the period of the audit. It is contended those cases
involved overpayments initially discovered during the audit. Petitioner argues the offset should be disallowed in this case on the ground that the overpayments were discovered by the payor within 2 years and were the subject of subsequent unauthorized unilateral recoupment. Further, MMS contends that the prior practice of the Geological Survey (Survey) Conservation Division (the predecessor of MMS for royalty management functions) of allowing such adjustments on royalty reports during the time period covered by the Forest audit is irrelevant in light of our current understanding of the law. Accordingly, MMS asserts the Board erred in allowing the offset of the overpayments against the underpayments.

Forest has responded to the petition. Forest asserts that our decision in this case is not inconsistent with other audit cases involving the offset of overpayments against underpayments. The limitation of offsets to "unrelated" overpayments and underpayments argued by MMS is asserted by Forest to be unsupported by, and contrary to, past Board precedents.

An occasional byproduct of the decision of appeals on a case-by-case basis is that issues which are distinct but related will be approached from a somewhat different legal basis depending upon the characterization of the issue. This is the case with the issue of offsets within the framework of an audit as distinguished from the question of the allowance of unauthorized recoupment. This case provides the Board an opportunity to seek to reconcile these lines of precedent. We find it appropriate to grant the petition for reconsideration in order to clarify our holding herein.

In our prior decision in this case the Board analyzed the applicability of an offset to the audit in this case as follows:

With respect to the overpayments of royalty which were the subject of the subsequent alleged unauthorized recoupments taken by appellant on Form MMS-2014, we believe the precedents established in Mobil Oil Corp., 65 IBLA 295 (1982), and Shell Oil Co., [52 IBLA 74 (1981)], are relevant. In the lead case, Shell Oil Co., we dealt with the question of whether, in the circumstances of an audit of royalty payments on a lease account, overpayments disclosed in the audit may be allowed as an offset to underpayments disclosed in the audit notwithstanding the fact that the audit was conducted more than 2 years after the overpayment so that a refund would be barred by the terms of section 10 of OCSLA. The Board answered the question in the affirmative: Had Shell initiated a request in 1979 for a refund of its November 1974 overpayment, we believe Survey would have been correct in denying such request as untimely. In Phillips Petroleum Co., 39 IBLA 393 (1979), we so held. Where, however, Survey undertakes to audit a producer some 4 years after the payments at issue have been made, we hold that a sense of fundamental fairness requires Survey to recognize both a producer's underpayments and overpayments of royalty. We believe Survey should have properly offset Shell's underpayment by the amount of its overpayment. We do not believe that the 2-year period of limitations was established to give Survey a procedural advantage in computing royalty payments.

52 IBLA at 78. This precedent was further developed in Mobil Oil Corp., supra.

In the Mobil case the asserted overpayments which appellant sought to offset were discovered by the lessee rather than by Survey in the audit. The Board found this distinction immaterial: "The question then, is not whether the statute bars refunds or credits, but whether—assuming overpayments occurred—Survey should have recognized
and offset these in the same audit period in which it discovered and assessed underpayment.” 65 IBLA at 304. The Board answered this question in the affirmative and remanded the case to allow Survey to determine the extent of any allowable offsets. The scope of our holding was defined further by the concurring opinion wherein we recognized the past practice of permitting offsets and declined to invalidate this past practice:

It is true that, in the past, Survey has permitted the offsetting of overpayments in one month by deductions from subsequent payments in future months. Our decision herein does not invalidate this practice. It does, however, properly limit it to the 2-year period mandated by 43 U.S.C. § 1339(a) (1976). In other words, where a lessee made royalty payments for any month in excess of that required by law, the excess may be deducted from future royalty payments provided that the excess payment occurred within 2 years of the future payment. Where, however, an excess payment has not been discovered within this 2-year period, such payment may not be recouped by diminution of future payments owing from production in the lease. Indeed, allowance of such deduction would be directly contrary to the 2-year limitation on refunds which Congress has expressly imposed. [Emphasis in original; footnote omitted.]

65 IBLA at 305-06 (Burski, A.J., concurring).

Subsequently, MMS issued the Oil and Gas Payor Handbook. Effective August 1, 1983, the Handbook was amended to specifically provide that a “payor cannot recoup an overpayment on an OCS lease through entries to Form MMS-2014 without receiving prior approval from MMS.” Payor Handbook Addendum No. 4, page 3 of 5 (July 1983); see 2 MMS, Royalty Management Program, Oil and Gas Payor Handbook § 4.4.2 (1986). In the absence of an MMS audit, the Board has upheld MMS decisions applying this provision to disallow recoupments of overpayments on Form MMS-2014 without prior authorization. [Footnotes omitted.]

113 IBLA at 43-45, 97 I.D. at 19-20.

The lead Board decision on the disallowance of unauthorized recoupment is Kerr-McGee Corp., 103 IBLA 338 (1988). In that case, a refund of royalty overpayments for gas produced from 1961 through 1970 resulting from a Federal Power Commission ordered refund to gas purchasers was requested in January 1978. The amount of the requested refund was deducted in the following month from royalty payments on the monthly report of sales and royalty. We expressly recognized the Solicitor’s opinion concluding that the 2-year limitation on repayments applies to credits against future royalty obligations as well as to repayments. Refunds & Credits Under the Outer Continental Shelf Lands Act, Solicitor’s Opinion, 88 I.D. 1090 (1981). Citing Mobil Oil Co., supra, the Board distinguished offsets involving the credit of overpayments against past payments due within the period of an audit from the taking of a credit against future payments due which is governed by the 2-year limitation just as refunds are. 103 IBLA at 339. The Board found in the Kerr-McGee case that an offset was not involved. Rather, appellant followed an untimely refund request with an improper credit against current royalty due which was properly disallowed by MMS.

[1] We find the Kerr-McGee case is distinguishable from the present appeal in certain material aspects. The overpayments at issue in Kerr-McGee were the subject of a refund request filed more than 2 years
after the overpayments and a subsequent unauthorized recoupment in the form of an underpayment on current royalty obligations. The underpayments by Forest came within 2 years of the overpayment which they were designed to recoup. Most significantly, both the under and overpayments fell within the timeframe of an MMS audit designed to ascertain the amount of royalty due and owing for that time period. The Board has upheld the view of the Solicitor and MMS that the recoupment of past royalty overpayments through applying a credit against current royalty obligations is a form of "refund" which may not be taken unilaterally, but which requires compliance with the procedures of section 10 of the OCSLA. Notwithstanding this principle, the purpose of a royalty audit is to ascertain the net amount of royalty due and owing to the United States. In resolving this issue it is necessary in the context of an individual lease to offset overpayments against underpayments within the timeframe of the audit. Although all underpayments are by definition improper, that fact provides no basis for ignoring the overpayments in determining the amount of the royalty due. The propriety of underpayments may be a proper issue in a civil penalty proceeding under section 109 of the Federal Oil and Gas Royalty Management Act of 1982, 30 U.S.C. § 1719 (1982), but this case does not involve a civil penalty.

We find this analysis to be consistent with the Solicitor's Opinion, supra, which specifically considered the question of offsets within the scope of an audit and the 2-year limitation. Citing with approval the Board's decision in Shell Oil Co., supra, the Solicitor found that section 10 of OCSLA permits offsetting (i.e., crediting of overpayments against past payments due) within the audit period. 88 I.D. at 1103. The Solicitor analyzed the applicability of the 2-year limitation to offsets within the timeframe of an audit in terms of the purpose of the statutory limitation. The opinion noted that the excess payments to be offset would not be withdrawn from the Treasury. Additionally, because offsets affect only past payments, they pose no threat to projected revenue estimates. Id. Further, the Solicitor held that the purpose of the limitation to protect against stale claims could hardly be invoked when the Department has already decided to shoulder the burden of reviewing monthly payments during the audit period. Id.

In a subsequent case, Santa Fe Energy Co., 107 IBLA 32 (1989), the Board expanded somewhat the Kerr-McGee precedent. We affirmed MMS orders requiring restitution of unauthorized credit adjustments on Form MMS-2014 notwithstanding the fact the underpayments sought to recoup prior royalty overpayments at least some of which were made within 2 years of the overpayment. In Mesa Petroleum Co., 107 IBLA 184 (1989), MMS required restitution of net-downward adjustments of royalty payments taken on Form MMS-2014 because

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1 Thus, the former Survey practice of allowing credit adjustments within 2 years, recognized in the concurring opinion in Mobil, has now been found improper.

2 Although the dates of all the overpayments and the corresponding underpayments in Santa Fe are not set forth in the opinion, those for which dates are given occurred within 2 years. 107 IBLA at 33.
the payor had not filed a refund request under section 10 of the OCSLA. The adjustments were taken in part for overpayments made within 2 years and in part for overpayments made more than 2 years before. Upon the subsequent filing of a refund request, the MMS Director denied the request as to all overpayments made more than 2 years prior to the filing of the request and held offsets could be recognized only in the context of an MMS audit and not where the overpayments had been deducted from subsequently filed royalty reports. The Board upheld the rejection of the refund request as to royalty overpayments made more than 2 years previously without comment regarding the availability of offsets of overpayments against subsequent underpayments within the scope of an audit. 107 IBLA at 190.

We find that *Santa Fe* and *Mesa* are distinguished from the present case by the absence of an MMS audit during the term of which the overpayments and underpayments were made. Consistent with the Solicitor’s Opinion, supra, and with the Board precedents in *Shell Oil Co.*, supra, and *Mobil Oil Corp.*, supra, we find that this distinction is dispositive.9 Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the prior decision of the Board is reaffirmed on reconsideration.

C. Randall Grant, Jr.
Administrative Judge

I CONCUR:

Gail M. Frazier
Administrative Judge

CITIES SERVICE OIL & GAS CORP.

117 IBLA 17

Appeals from separate decisions of the Director, Minerals Management Service, determining the proper fractionation allowance and affirming in part and reversing in part an order to recalculate and pay additional royalties. MMS-86-0345-OCS, MMS-86-0375-OCS, MMS-87-0006-OCS, MMS-87-0027-OCS.

Affirmed in part; reversed in part; set aside and remanded in part.

1. Administrative Practice—Administrative Procedure: Adjudication

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9 It appears appellants in those cases did not argue, and hence the Board did not consider, whether a recoupment taken on Form MMS-2014 might be sufficiently stated and itemized as to constitute a request for refund which might be allowable to the extent it was filed within 2 years of the overpayment.
As a general rule, adjudications should be so structured that determinations of subsidiary or interrelated questions are made within the confines of a single unified decision so as to avoid needless multiplicity of appeals and the resulting confusion which piecemeal adjudication engenders.

2. Oil and Gas Leases: Royalties: Natural Gas Liquid Products--Outer Continental Shelf Lands Act: Oil and Gas Leases
Since, pursuant to the provisions of 30 CFR 206.152(a)(2) (1987), the reasonable allowance for the costs of processing natural gas liquid products was, as a general matter, to be based on "actual plant costs," the fact that other lessees were permitted a greater allowance is a legal irrelevancy so long as each lessee's allowance is based on its actual plant costs.

3. Oil and Gas Leases: Royalties: Natural Gas Liquid Products--Outer Continental Shelf Lands Act: Oil and Gas Leases
Where the calculation of a processing allowance involves consideration of a profit factor based on the sales values of natural gas liquid products, and where it is necessary to provide a separate extraction and fractionation allowance, the profit factor is properly computed only once in the combined extraction/fractionation allowance computation.

4. Oil and Gas Leases: Royalties: Natural Gas Liquid Products--Outer Continental Shelf Lands Act: Oil and Gas Leases
Where the determination of the processing allowance to be permitted for natural gas liquid products requires the separate determination of an extraction and fractionation allowance, these two allowances are properly added together to arrive at the combined processing allowance.

5. Administrative Procedure: Rulemaking--Oil and Gas Leases: Royalties: Natural Gas Liquid Products--Outer Continental Shelf Lands Act: Oil and Gas Leases
The "Procedure Paper on Natural Gas Liquid Products Valuation," developed by MMS, is not a substantive regulation subject to the rulemaking requirements of the Administrative Procedure Act, 5 U.S.C. § 553(b) (1988).

6. Oil and Gas Leases: Royalties: Natural Gas Liquid Products--Outer Continental Shelf Lands Act: Oil and Gas Leases
Since, unless otherwise expressly provided, all royalty payments are accepted subject to audit, a subsequent determination that additional royalties are due does not give rise to a question of retroactive application of a new rule if the determination that a deficiency exists was made under the regulation applicable at the time that the payment was originally made.

7. Oil and Gas Leases: Royalties: Natural Gas Liquid Products--Outer Continental Shelf Lands Act: Oil and Gas Leases
In the absence of acceptance of a lessee's royalty valuation as conclusive by an official authorized to bind the Department on such matters, the fact that the Office of Inspector General may have conducted an audit of payments made on a lessee's behalf does not prevent the duly authorized officials from thereafter timely reviewing the lessee's original valuation and determining that royalty is still owing.

8. Oil and Gas Leases: Royalties: Natural Gas Liquid Products--Outer Continental Shelf Lands Act: Oil and Gas Leases
Where it is MMS policy to accept DOE ceiling prices for natural gas liquid products as representing fair market value for royalty purposes in certain instances, and MMS has followed that policy in a number of cases, its refusal in another case to accept those
ceiling prices in favor of the monthly average spot market price must be deemed arbitrary and capricious.

9. Oil and Gas Leases: Royalties: Natural Gas Liquid Products--Outer Continental Shelf Lands Act: Oil and Gas Leases

Where a floor price was established generally for natural gas liquid product valuation for royalty calculation, royalty could not be assessed using a higher rate than the floor price.


OPINION BY ADMINISTRATIVE JUDGE BURSKI

INTERIOR BOARD OF LAND APPEALS

These two consolidated appeals involve separate, but interrelated, decisions of the Director, Minerals Management Service (MMS), generally requiring the submission by Cities Service Oil & Gas Corp. (Cities Service)¹ of increased royalties for natural gas liquid products (NGLP’s) produced from Outer Continental Shelf lands (OCS) leases and processed at the Grand Chenier Processing Plant (Grand Chenier) and the Lake Charles Fractionator. In light of the identity of some of the issues presented, they have been consolidated for purposes of decision.

Grand Chenier, while denominated a “processing plant,” is actually a plant for the extraction of the liquid constituents (or raw make) from the natural gas stream. Grand Chenier is owned by a number of parties, including appellant, and is operated by Conoco Inc. on their behalf, processing natural gas from approximately 40 OCS leases. After the liquid components have been separated from the wet gas, they are sent to the Lake Charles Fractionator where they are further processed to obtain ethane, propane, butanes, and pentanes (NGLP’s). While Grand Chenier, as indicated above, is owned by a number of companies, the Lake Charles Fractionator is totally owned by appellant. Appellant receives 12.4 percent of the NGLP’s processed at Lake Charles as its fee for fractionating the liquid components extracted from the natural gas stream for other lessees.²

Sometime in 1983, the Office of Inspector General (OIG) conducted an audit of royalty payments made on NGLP’s processed at Grand Chenier and the Lake Charles Fractionator for the years 1977 through 1982. In its final audit report, issued in February 1984, OIG noted

¹ Since initiating the instant appeal, Cities Service has changed its name to OXY USA Inc. For purposes of clarity, however, we shall continue to refer to appellant as Cities Service in this decision.

² We note that in its supplemental statement of reasons (SOR) before the Director, MMS, Cities Service argued that, in fact, its fractionation fee was 13.1 percent. See Supplemental SOR at 8. This contention, however, has not been pursued before the Board and the actual fee is, in any event, irrelevant to the determination of the legal principles involved in this appeal.
various areas in which it felt adjustments were necessary and would result in higher royalty assessments. Included, *inter alia*, were determinations that numerous companies had undervalued NGLP's for royalty purposes and had understated revenues and overstated plant expenditures for the 1979/1981 biennial period. Of particular relevance to the instant appeal, OIG also challenged appellant's entire fractionation fee, noting that Cities Service had declined to provide it with revenue and expense information relating to the operation of the Lake Charles Fractionator. The fractionation fee which appellant had claimed was the same 12.4 percent which it charged other companies for fractionating at the Lake Charles facility.

Thereafter, MMS conducted its own review of the royalty payments relating to NGLP's processed at Grand Chenier and the Lake Charles Fractionator. This review led to a series of orders which are the subject of the instant appeals.

The appeal docketed as IBLA 88-140 arose from a decision of the Director, MMS, dated November 3, 1987, granting, in part, separate appeals from three orders issued by the Regional Manager, Tulsa Regional Compliance Office (TRCO), Royalty Management Program (RMP). Prior to the issuance of these three orders, the Regional Manager had, by letter dated April 14, 1986, informed appellant that a preliminary review of its operations had led to an initial determination to disallow the fractionation deduction which appellant had taken. Appellant was afforded an opportunity both to provide the actual cost and expenditures figures related to the Lake Charles Fractionator and to make any other comments it deemed warranted. Pursuant to this invitation, Cities Service responded on May 16, 1987, arguing that, in its view, the fractionation allowance which it took, even if it were deemed not to have been the result of an arm's-length transaction, possessed the same characteristics manifested by other arm's-length transactions which MMS had accepted as indicative of fair market value for other producers. Accordingly, Cities Service requested that it be permitted to take the same deduction allowed the other lessees who used the Lake Charles Fractionator.

Following receipt of this response, MMS began the adjudicative process which resulted in the eventual issuance of the four orders under review herein. The first of these orders, dated June 4, 1986, directed appellant to recompute the amount of royalty due based on a disallowance of the entire fractionation fee. This order noted, however, that the recalculation for leases OCS 0767 and OCS 0768 could exclude the period from April 1982 through October 1982, as that period was being covered by a separate compliance action. This order was timely appealed and docketed before the Director, MMS, as MMS-86-0345-OCS.

The second order was dated June 10, 1986, and covered leases OCS 0767 and OCS 0768 for the period April 1982 through October 1982. Like the June 4 order, it rejected any deduction for processing costs attributable to fractionation. Unlike the June 4 order, however, rather
than directing Cities Service to recompute the amount of royalties due, MMS determined that the amount due was $7,842.68. This order was duly appealed and docketed before the Director, MMS, as MMS-86-0975-OCS.

The third order issued on November 17, 1986. Subsequent to its appeal of the June 4 and June 10 decisions, Cities Service had submitted actual cost information relating to the Lake Charles Fractionator for the period from January 1977 through December 1982 (the period of the audit). In his November 17 decision, the Regional Manager, TRCO, approved a fractionation allowance of 1.42 cents per gallon for the period from October 1977 through September 1979, and a fractionation allowance of 1.91 cents per gallon for the period from October 1979 through September 1981. In this decision, the Regional Manager rejected any fractionation allowance for the period from January 1977 through September 1977 and from October 1981 through December 1982 because actual costs for the full biennial period had not been submitted. The Regional Manager also disallowed any consideration of insurance costs and rejected attempts by appellant to obtain either a return on investment (ROI) or imputed interest. Appellant timely appealed this decision to the Director, MMS, where it was docketed as MMS-87-0006-OCS.

It should also be noted that one day after this third order, the Regional Manager, TRCO, sent a letter to appellant’s attorney informing her that, in view of the November 17 order, the original order of June 4 was being amended to conform thereto. This letter also noted that, since no fractionation allowance had been approved for any period after September 1981, no change in the June 10 order was effected by the November 17 order.

The end result of these three orders was that Cities Service was directed to recompute royalties for the period from January 1977 through September 1977 with no fractionation allowance deduction, to recompute royalties for the period from October 1977 through September 1981 using the deductions specified in the November 17 order, to recompute the royalties for the period from October 1981 through December 1982 (except for royalties due for leases OCS 0767 and OCS 0768 for the period from April 1982 through October 1982) without any deduction for fractionation, and to remit $7,842.68 in past due royalties accruing from leases OCS 0767 and OCS 0768 for the April 1982 through October 1982 period, which represented no deduction for the fractionation allowance.

In its appeal to the Director, MMS, appellant assailed the orders of the Regional Manager on a number of bases. Thus, appellant noted that it had utilized the same fractionation deduction that all other lessees who used the Lake Charles Fractionator had employed. Yet, while MMS had permitted these lessees to make this deduction it had refused to allow the same deduction for appellant. In his November 3,
DECISIONS OF THE DEPARTMENT OF THE INTERIOR

1987, decision, the Director reviewed the three orders described above, affirming the June 4 order, as revised by the November 17 order, and the June 10 order. Appellant thereupon appealed to the Board.

The second appeal, IBLA 88-169, arose from a decision of the Director, MMS, dated October 16, 1987. While this decision actually issued prior to the decision in IBLA 88-140, the underlying order of the Regional Manager, TRCO, had issued on December 12, 1986, subsequent to the three orders involved in IBLA 88-140. In this order, the Regional Manager detailed the results of the MMS review of the OIG audit and specified various revisions which should be made in computing royalties. In addition to again disallowing the 12.4-percent fractionation allowance which had already been the subject of the three earlier orders, the Regional Manager directed additional changes in the manufacturing allowance claimed and adjustments to gross liquid production figures submitted, and further held that royalty for NGLP's should be recomputed in accordance with the "Procedure Paper on Natural Gas Liquid Products Valuation" (Procedure Paper), utilizing the monthly average Mont Belvieu spot market price for those non-arm's-length transactions where the value reported by Cities Service for determining royalty was below the low Mont Belvieu price for that month. With two exceptions not relevant to the instant appeal, the October 21 decision of the Director affirmed the order of the Regional Manager. Cities Service duly appealed this decision.

[1] Before examining the arguments pressed on appeal before the Board, we are constrained to comment upon the adjudicative procedures followed by MMS with respect to the instant appeals. In essence, the Regional Manager issued four separate orders directing recalculation of royalties paid on NGLP's produced from Grand Chenier, three of which covered only the fractionation allowance, while the last order covered the fractionation allowance in addition to other matters. Thus, appellant was required to file four separate appeals to the Director, MMS and, eventually, two appeals to this Board, even though the last order, issued while the prior orders were on appeal to the MMS Director, subsumed all of the issues covered by the prior orders. The MMS Director, for his part, decided the last appeal first which essentially rendered his decision relating to the earlier issued three orders a foregone conclusion.

The multiplicity of orders relating to the calculation of royalty for the NGLP's by the Regional Manager, as well as the failure of the Director, MMS, to either decide the earlier appeals first or consolidate

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[97 I.D.

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While the MMS decision in IBLA 88-169 was issued prior to the MMS decision in IBLA 88-140, the relevant case files in IBLA 88-169 were not transmitted to the Board until Jan. 7, 1988. The case files in IBLA 88-140, however, were received by the Board on Dec. 23, 1987. Since appeals are docketed upon receipt of the case files, the unexplained tardiness in transmission of the case files for IBLA 88-169 has further confused these appeals since the earlier MMS decision now bears a later IBLA docket number.

With respect to a dispute over transportation allowances, the Director granted appellant 90 days in which to submit documentation to the RMP (Decision at 11). Also, the Director's decision noted that an earlier misapplication of the yardstick values to Conoco Inc.'s sales figures rather than appellant's had been corrected (Decision at 19).
all four appeals in one decision, have added significantly to the confusion engendered in attempting to review these appeals.

It seems an elementary matter of adjudicative practice to attempt to determine all subsidiary questions relating to a specific determination within the confines of a single decision, if at all possible. Herein, in his order of June 4, 1986, which was the first of the orders involved herein, the Regional Manager expressly noted that: "This letter addresses the fractionation allowance percentage which was used to compute and pay royalties on Cities' interests in the OCS leases processed at the Lake Charles Fractionator. *All other areas of interest to MMS associated with these leases remains subject to further review*" (emphasis supplied). Thus, MMS knew, almost for a certainty, that further adjustments would be required in order to arrive at the royalty payment MMS thought was justified, yet, nevertheless, chose to proceed with a fragmented adjudicatory approach.

We see little purpose to be served in the issuance of piecemeal decisions covering the same essential question, namely the proper royalty to be paid for the NGLP’s during the period in issue. All of the issues ultimately covered in the Regional Manager’s fourth order were included in the OIG audit report. All of them necessarily bore on the determination of the proper royalty assessment. The first three orders of the Regional Manager involve but one element in the determination of the proper royalty rate, i.e., the fractionation allowance. Each of these three orders instructed appellant to recompute the royalty due based only on changes of the fractionation allowance, despite the fact that the Regional Manager was already considering other modifications suggested by the OIG report. Even if appellant had agreed to the original order issued by the Regional Manager and proceeded to recompute the royalty due, its actions would have been useless. It would have been forced, under the fourth order, to redo all of the computations since other changes not directed in the initial three orders were involved.

There seems little utility in issuing an independent determination on the question of the fractionation allowance when it is merely one aspect of the entire controversy. Our opinion is strengthened by the fact that the MMS Director was apparently of the same mind as he chose to adjudicate the appeal of the fourth order before entertaining the appeals of the earlier three orders. We believe the approach followed below not only puts an appellant to the unfair burden of simultaneously defending numerous separate, but intrinsically related, matters but also adds a considerable burden to this Board’s adjudications in sorting out the resulting confusion.

With respect to the substance of the instant appeals, inasmuch as questions relating to the fractionation allowance are common to both

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* Why these appeals were not consolidated, however, is unexplained.
decisions under review, we will examine that issue first. Thereafter, we will adjudicate those matters which were solely the subject of the Director's October 16, 1987, decision.

As noted above, while MMS originally disallowed any deduction for fractionation because of appellant's failure to submit its revenue and expense information relating to the Lake Charles Fractionator, it ultimately relented when Cities Service submitted these figures, at least with respect to the two biennial periods for which appellant submitted complete information. For those two periods, MMS allowed a deduction of 1.42 cents per gallon and 1.91 cents per gallon, respectively. Appellant challenges this allowance primarily on the ground that, as computed by MMS, the fractionation allowance is limited solely to actual costs and does not include the allowance of any profit factor with respect to appellant's investment in the Lake Charles Fractionator. Additionally, appellant asserts that the sales values of its NGLP's were improperly calculated. Finally, appellant alleges that the Director failed to make any allowance for insurance costs associated with the Lake Charles Fractionator. For reasons which we shall set forth, we find ourselves in substantial agreement with the decision of the Director, MMS, and expressly hold that where the processing allowance is based on a profit factor derived from the value of the NGLP's sold, rather than on a return on investment, the profit factor may only be counted once in the computation of the processing allowance.

In his decision, the Director noted that the processing allowance for OCS leases (as opposed to onshore leases) was determined by RMP according to the following formula:

\[
\text{Processing Allowance} = \frac{\text{Costs} + \text{Profit Factor} + \text{Depreciation}}{\text{Sales Value of Liquids}}
\]

(Decision at 2). Thus, the ultimate processing allowance permitted is expressed as a percentage of the value of the NGLP's. The question, of course, is the determination of the proper processing allowance in the instant case.

The starting point for the Director's analysis of this issue was 30 CFR 206.152(a)(2) (1987). That regulation provided, in relevant part, for the payment of royalty on all natural gasoline, butane, propane and other substances extracted from the natural gas, but further provided that: "A reasonable allowance, determined by the Director and based upon regional plant practices and actual plant costs and other pertinent factors, may be made for the cost of processing and may be deducted from the royalty payment due on said constituent

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*The oil and gas valuation regulations were substantially revised in 1988. See 53 FR 1272 (Jan. 15, 1988); 53 FR 45084 (Nov. 8, 1988). We express no opinion as to the proper interpretation of these new provisions with respect to the issues determined by this decision.*
substances." Based on this language, the Director concluded that this regulation required that the fractionation allowance be based on actual costs (Decision at 2). The Director noted that, inasmuch as the other lessees who used the Lake Charles Fractionator were charged 12.4 percent of the NGLP’s processed as a service charge, this figure represented their actual costs and was properly deductible under the regulation. But, since Cities Service owned the Lake Charles Fractionator, its use of the 12.4-percent figure could not be justified because this did not represent an actual cost to Cities Service.

The Director noted that, in the alternative, Cities Service had argued that the actual costs used in calculating the fractionation allowance should include factors other than simply out-of-pocket expenditures, viz., either an ROI or a profit factor, and insurance costs. The Director disagreed. With respect to insurance costs, the Director noted that Cities Service was largely self-insured and that, in any event, it had failed to prove any insurance costs. More importantly for this appeal, while the Director agreed that a profit factor should be applied to the extraction allowance, he held that no such profit factor was applicable to the fractionation allowance because, in the Director’s view, use of a profit factor based on total sales value in both the extraction allowance and the fractionation allowance would constitute double-counting (Decision at 6-7).

Appellant makes a number of arguments to counter the Director’s analysis. First, it notes that the regulation does not, in any way, provide that a profit factor may be taken for the extraction process but may not be taken for the fractionation process. Indeed, the regulation does not refer to either of these two processes but merely references “the cost of processing.” Thus, appellant argues that allowance of a profitability factor for one of these elements without also allowing it for another can scarcely be based on the regulatory language.

Second, it argues that the Director’s decision is internally inconsistent since at one point it suggests that the fractionation allowance applicable to offshore leases includes a profit factor in lieu of return of investment (Decision at 3), while at another point it states that no profit factor could be allowed in the fractionation allowance because it would duplicate the profit factor already granted in the extraction allowance (Decision at 7).

Finally, with respect to the actual computation of its allowances, appellant argues that MMS made both theoretical and computational errors. We turn now to a consideration of these questions.

[2] Before the Director, MMS, appellant had argued that it should be allowed the same deduction as allowed to those lessees for whom it fractionated NGLP’s at Lake Charles, since these agreements were the result of arm’s-length transactions and established a fair market value for the fractionation of the NGLP’s. In this regard, we note that where a lessee disposes of NGLP’s in a non-arm’s-length transaction, the
Procedure Paper does provide the lessee with an opportunity to show that its non-arm’s-length contracts had characteristics similar to arm’s-length contracts so that the valuation of NGLP’s under its non-arm’s-length contract might be used for the purpose of establishing fair market value. See, e.g., Shell Offshore Inc., 116 IBLA 246 (1990); Cities Service Oil & Gas Corp., 113 IBLA 255, 262-63 (1990). However, nothing in either the Procedure Paper or the applicable regulations authorizes a similar comparison where the issue involved concerns the allowance to be granted for the cost of processing. Nor would we deem such an approach appropriate. Questions pertaining to the establishment of fair market value necessarily partake of an element of inexactitude. Fair market value can fluctuate greatly over a short period of time and the determination of the market value of a commodity at any specific point in time has inherent uncertainties. Thus, in attempting to determine fair market value in those situations involving interaffiliate and subsidiary transactions, the Procedure Paper has provided a mechanism by which a lessee can attempt to show that its non-arm’s-length contract had characteristics similar to arm’s-length contracts negotiated at the same time in the same general area for the same product so as to support reliance upon the price provided for in the non-arm’s-length contract as establishing fair market value. See generally Shell Offshore Inc., supra at 250, 251.

With respect to the determination of actual costs, however, no such uncertainties should exist. In determining such costs, the Department is not concerned with an idealized concept such as “fair market value.” Rather, it is concerned with actual expenditures made by each lessee. In this regard, it is essentially irrelevant what costs another lessee absorbs since the purpose of 30 CFR 206.152(a)(2) (1987) is to compensate each lessee for its expenses in processing NGLP’s. Thus, the fact that every other lessee was permitted a fractionation deduction equal to 12.4 percent of the total NGLP’s which it produced must be seen in light of the fact that this represented each of those lessee’s actual expenditures. This deduction has no necessary relationship, however, to appellant’s actual expenditures. The Director properly rejected appellant’s attempt to justify a 12.4-percent fractionation deduction for its NGLP production on the ground that this was the amount which all other lessees were allowed. This 12.4 percent represented the “actual costs” of those lessees; it does not represent the “actual costs” borne by appellant.

The foregoing, however, is subject to one important caveat. The regulation expressly authorizes the Director to look at “other pertinent factors,” in addition to actual costs in determining the processing allowance. The real question which this appeal presents is whether or not the Director has considered these “other pertinent factors.” The essential thrust of appellant’s objection is that he did not and the failure to either provide appellant with an ROI for its expenditures at Lake Charles or to separately provide for a profit factor in computing its fractionation allowance was arbitrary and capricious.
Initially, we note that had this case involved onshore rather than OCS leases there seems little question that an ROI for the Lake Charles Fractionator would have been permitted. The reason for this is that a dichotomy had developed between the computation of processing allowances. As noted above, NGLP's processed from OCS leases were granted a profit factor in computing processing allowances. Onshore, lessees were not allowed a profit factor. Rather, the value of imputed interest on the undepreciated investment was allowed. While the genesis of this disparity is unclear, all parties agree that the profit factor normally results in a higher processing allowance than the imputed interest factor because it is adjusted to an after-tax rate. See Statement of Reasons (SOR) (IBLA 88-140) at 9; Answer (IBLA 88-140) at 5. The important point to keep in mind, however, is that allowance of the profit factor is a substitution for an ROI based on imputed interest.

Appellant's main objection, however, is not to the failure of MMS to allow imputed interest rather than a profit factor. Instead, appellant focuses on the perceived failure of MMS to allow a separate profit factor in the computation of the fractionation allowance. It is this failure which appellant contends is arbitrary and capricious. Our analysis of the computations utilized to derive a processing allowance, however, convinces us that, in point of fact, MMS correctly refused to compute the extraction allowance using a profit factor and then separately compute the fractionation allowance again using a profit factor.

We noted above that RMP used the following formula to derive the processing allowance:

\[
\text{Processing Allowance} = \frac{\text{Costs + Profit Factor + Depreciation}}{\text{Sales Value of Liquids}}
\]

Since the profit factor allowed is based on a 15-percent rate of return on sales after income taxes, the formula can also be stated as:

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*There are, however, indications that the profit factor was intentionally chosen for OCS leases because of the increased costs associated with production on the OCS.*
where:

PA = Processing Allowance
A = Liquids Value
B = Operating Expenses
D = Depreciation
.15 = Profitability Range Limit
.54 = Nontaxable Portion of the Income Tax Base.

Counsel for MMS suggests that where, as here, it was necessary to compute both an extraction allowance and a fractionation allowance, MMS first computes the extraction allowance with a profit factor, next computes the fractionation allowance without a profit factor, and then adds the two allowances to arrive at the processing allowance. Thus, under this approach the formula may be stated as follows:

\[
PA = B + \left( \frac{.15A}{.54} \right) + D + \frac{B + D}{A}
\]

where:

PA = Processing Allowance
A = Liquids Value
B = Operating Expenses (Extraction)
B₁ = Operating Expenses (Fractionation)
D = Depreciation (Extraction)
D₁ = Depreciation (Fractionation)

Appellant argues that, under this approach, it is only receiving a profit factor on the costs and expenses associated with extraction and not on fractionation. This argument, however, is based on a misinterpretation of the algebraic formulation. Thus, the above formula may also be expressed in a single equation as follows:
This formulation clearly shows that the profit factor applies equally (to the extent that it applies at all) to the cost and depreciation aspects of both the extraction and fractionation processes.

The mistake which appellant makes is in assuming that the profit factor being granted by MMS has any correlation to the level of its investment and an acceptable ROI. It does not. The profit factor being allowed is strictly a function of the sales values of the NGLP’s and does not vary regardless of the size of the expenditures being deducted for either costs or depreciation. While MMS states that it performed two separate computations to arrive at the total processing allowance, it could have done it in one computation. Indeed, in the instant case, MMS could also have placed the profit factor in the fractionation computation rather than the extraction computation without making any change, whatsoever, in the ultimate processing allowance granted.

The simple fact of the matter is that while MMS may authorize a profit factor based on total sales in lieu of a return on investment they are not equivalent concepts. Appellant is, in essence, attempting to meld the onshore approach which grants an ROI, instead of a profit factor, with the OCS approach which grants a profit factor in place of an ROI. They are, however, simply not compatible. By attempting to have the profit factor counted both in the computation of the extraction allowance and in the computation of the fractionation allowance, appellant is, as the Director argued, attempting to recoup a double profit. The Director correctly rejected this attempt.

We note that the foregoing presupposes that the Liquids Value (factor A) remains constant. In his October 16, 1987, decision, the Director pointed out that

[the RMP included 100 percent of the plant’s operating expenses (factor B) and depreciation (factor D) in its calculation of the processing allowance. Therefore, the “liquid sales value” (factor A) had to include the value of 100 percent of the plant’s liquid production, regardless of the ownership or disposition of the liquids.]

(Decision at 14). The problem, however, is that only if Lake Charles processed all of the Grand Chenier NGLP’s, and only the Grand Chenier NGLP’s, would factor A remain constant for both the extraction and fractionation calculation when factor A is based on total plant throughput. If, on the other hand, Lake Charles processed NGLP’s in addition to those processed at Grand Chenier, it would make a difference where the profit factor was allocated since the profit factor is a direct function of the Liquid Values figure and the Liquid Values figure would be different in the two computations.
In such an eventuality, the proper method for computing the processing allowance for appellant would be to determine Cities Service’s aliquot portion (i.e., the portion of each plant’s total throughput which represents Cities Service’s share of production) of the operating expenses and depreciation at both Grand Chenier and Lake Charles and utilize Cities Service’s gross NGLP sales rather than either of the plant runs. By doing this, one would arrive at a constant value for A for purposes of computing both the extraction allowance and the fractionation allowance. Our affirmation of this aspect of the Director’s determination is thus premised on the assumption that the Liquid Values figure used was the same for both the extraction allowance and the fractionation allowance. If it was not, on remand MMS is directed to recompute appellant’s processing allowance as indicated above.8

[4] Appellant also challenges the manner in which MMS calculated the combined processing allowance. It notes that these two allowances should be added together and then subtracted from the gross value. Appellant argues that the following formula reflects the approach that should be taken:

\[
\text{Value} - (\text{Extraction} + \text{Fractionation}) = \text{Net Value} \times \text{Royalty Rate}
\]

Thus, appellant suggests that, assuming a value of 100, an extraction allowance of 30 and a fractionation allowance of 10, the computation should be:

\[
100 - (30 + 10) = 100 - 40 = 60 \times \text{Royalty Rate}
\]

Appellant complains that, rather than make this relatively simple mathematical calculation, MMS reduced the fractionation rate by the percentage of the extraction allowance and that this improperly reduced the amount of its total processing allowance.9 Accordingly, it requests that corrections be made to the computations.

This aspect of the case is particularly troubling. We note that in a memorandum dated May 18, 1987, to the Chief, Division of Appeals, MMS, the Regional Manager stated that the correct MMS formula is:

\[
\text{Value} \times [(1.0 - \text{Processing allowance}) \times (1.0 - \text{Fractionation Fee})] = \text{Net Value Subject to Royalty}
\]

(Memorandum of May 18, 1987, at 4).

We must admit that we find it difficult to understand the theoretical basis for this formula. In effect, this formula calls for the multiplication of the reciprocal of the processing allowance and the fractionation fee, the product of which is then multiplied by the gross value to arrive at net value subject to royalty. Not only is there no

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8 No alteration would be needed in any event with respect to any other user of the Lake Charles Fractionator since MMS permitted these users to subtract their actual costs (12.4 percent of the NGLP’s processed) as their fractionation fee.

9 In its SOR, appellant argued that the formula to represent this calculation would be: “Value – [(Extraction + (Extraction x Fractionation)] = Net Value.” The problem, however, is that since the extraction and fractionation elements of the equation represent real numbers and not percentages, the equation cannot work. An accurate algebraic expression of this calculation would be considerably more involved: “Value – [(Value x Extraction %) + [(Value – (Value x Extraction %)) x Fractionation %]] = Net Value.”
explanation of the theory by which this calculation can be said to
arrive at the net value subject to royalty, it is also obvious that this
formula results in a varying net value subject to royalty even in
situations in which the combined extraction/fractionation allowance is
the same.

Thus, if we assume a gross value of $100, an extraction allowance of
20 percent, and a fractionation fee of 20 percent (for a total of 40-
percent allowable costs), the computation works as follows:

\[
$100 \times [(1.00 - .20) \times (1.00 - .20)] = $100 \times [.80 \times .80] = $100 \times .64 = $64 \text{ Net value subject to royalty}
\]

If, however, we assume a gross value of $100, an extraction allowance
of 30 percent, and a fractionation fee of 10 percent (still a total of 40
percent of allowable costs), the computation works as follows:

\[
$100 \times [(1.00 - .30) \times (1.00 - .10)] = $100 \times [.70 \times .90] = $100 \times .63 = $63 \text{ Net value subject to royalty}
\]

Quite apart from the failure of MMS to submit any theoretical
justification for its approach, the fact that different net-value figures
can be obtained even while the total allowance remains constant must
compel a conclusion that use of this formula is inherently arbitrary
and capricious. Had MMS utilized this formula to compute the
combined extraction/fractionation allowance we would find it
necessary to reverse its actions.

The problem, however, is that it does not appear that MMS actually
used this formula in computing the allowance. Thus, the Regional
Manager's memorandum of May 18, 1987, noted that “[t]he formula
actually required by MMS is 100 × (100% − 30%) − cents per gallon
frac deduction = Value subject to royalty” (Memorandum at 4). Thus,
MMS asserts that, in fact, it did not multiply the reciprocals of the
allowances but rather effectively subtracted both of the allowances
from the gross value. We note further that counsel for MMS asserts in
its answer that after calculating the separate extraction and
fractionation allowance, MMS “then added the two allowances together
to arrive at Cities’ processing allowance” (Answer (IBLA 88-140) at 6).
Assuming that these statements correctly reflect the reality of the
calculations, it is obvious that the formula set forth above was not
utilized as the basis for determining appellant’s deductions. Cities
Service’s objections on this point are therefore overruled.

In summary, on the issue of the proper processing allowance, we
conclude that MMS was not required to permit appellant to deduct
12.4 percent of the NGLP’s, but rather properly required Cities Service
to submit proof of its actual costs and expenses; that, since the profit
factor allowed is based on the sales values of NGLP’s, it is properly
computed only once in the combined extraction/fractionation
allowance computation; and that the extraction and fractionation
allowances are properly added together to arrive at the combined processing allowance. ¹⁰

We turn now to the issues presented which are specific to the appeal in IBLA 88-169. With respect to this appeal, appellant makes a number of arguments. First, it contends that the adoption of the Procedure Paper constitutes improper rulemaking in violation of the relevant provisions of the Administrative Procedure Act (APA), 5 U.S.C. § 553 (1988). Next, it argues that even if the adoption of the Procedure Paper did not violate the provisions of the APA, it should not be applied retroactively to payments made before its adoption. Moreover, with respect to the period 1978 through 1980, appellant specifically argues that since these payments, made on its behalf by Conoco, had already been subject to an OIG audit, MMS was precluded from re-auditing payments made by Conoco on appellant’s behalf. Finally, appellant challenges the valuation of NGLP’s utilized by MMS, arguing, inter alia, that the “yardstick” valuation therein outlined results in valuations in excess of Department of Energy (DOE) maximum prices during the period of DOE mandatory price control.

We note that all of these arguments have been examined in a number of prior Board decisions. In Cities Service Oil & Gas Corp., supra, we briefly described those portions of the Procedure Paper relevant to the consideration of the instant appeal:

[T]he Procedure Paper is designed to assure that proper royalties are tendered on NGLP production. To effectuate this intent, the Procedure Paper set out to develop what it referred to as a “yardstick valuation technique” (Procedure Paper at 3). The Procedure Paper noted that a review of various factors such as the NGLP sales contracts, prices received by lessees, Table 7 (DOE) prices, and commercially available NGLP bulletins, had led to the conclusion that the price bulletins represented the best available price source and would, in most instances, be indicative of NGLP fair market value (Procedure Paper at 5). Accordingly, use of three bulletins were recommended. The “yardstick” price was to be derived by using the highest and lowest prices for each month from the appropriate bulletin. Any reported value falling within this range would be within the “yardstick” valuation. If the reported value was below the range of values for a specific month, the average value of the “yardstick” for that month would be the minimum value accepted by MMS (Procedure Paper at 6-7). [Footnote omitted.]

Id. at 257-58.

It must also be noted, however, that while the Procedure Paper provided for development of a “yardstick” valuation, this “yardstick” valuation would only be applied in limited circumstances. Thus, if an arm’s-length contract existed, the Procedure Paper provided that the contract price would normally be considered to establish fair market value unless the actual proceeds received were higher. Of particular note for the instant appeal, the Procedure Paper also provided that if, ¹⁰ Our affirmation is without prejudice to any subsequent submission by appellant with respect to the two biennial periods for which no fractionation allowance was permitted. In this regard, we note that the order of the Regional Manager merely requested that appellant submit cost and expenditure data for the 6-year period of the audit. If MMS desired the data for all 8 years encompassed by the four biennial periods it should have expressly requested it. We note that there might be some question as to the authority of MMS to request data for the biennial period from October 1975 through September 1977. See Phillips Petroleum Co. v. Lujan, No. 96-C-1457-5 (N.D. Okla., Oct. 18, 1989), appeal docketed No. 99-6122 (10th Cir.). Inasmuch as this issue has not been raised by either party, we consider it inappropriate to address it at the present time.
during the period in which NGLP prices were controlled by DOE regulations, a lessee received a maximum permissible price under the DOE regulations, this price would be accepted as fair market value, even if it were less than the price called for in an existing sales contract or under the “yardstick” valuation. The applicability of this latter provision is examined subsequently in the text of this opinion.

[5] Appellant’s generalized objections to MMS’s use of the Procedure Paper may be quickly disposed of. With respect to appellant’s assertion that the adoption of the Procedure Paper constituted improper rulemaking in derogation of the provisions of 30 CFR 206.150 (1987), we noted in Amoco Production Co., 112 IBLA 77 (1989), that:

In fact, the Procedure Paper itself relies on the factors set forth in the regulation—the lessee’s price, regulated prices, posted prices, and gross proceeds. It provides guidance by specifying which of the factors listed in 30 CFR 250.64 (1982) is to be given the most weight in various circumstances.

Id. at 81. Similarly, in Conoco Inc., 110 IBLA 232, 242-43 (1989), we held that:

The Procedure Paper merely clarified the existing regulations by setting forth a yardstick by which MMS would measure the reasonableness of royalty values reported by lessees. It did not require lessees to value their production by any specific method, nor did it modify any existing regulation. Rather, it found that, after consideration of the factors listed in the regulations, the best measurement of the reasonable value of NGLP in situations where no arm’s-length contract existed was the commercially available spot price bulletins. We find the Procedure Paper to be essentially a policy guideline adopted by MMS to assist in valuing NGLP production for royalty purposes under the provisions of the relevant regulation. As such, it does not have the force and effect of law as a duly promulgated regulation does, and the Board will decline to follow it where it is inconsistent with the terms of the relevant regulations.

Consistent with our past holdings, we reject appellant’s assertion that the Procedure Paper constitutes a substantive rule of law adopted in violation of the applicable provisions of the APA. Rather, the Procedure Paper merely establishes internal guidelines to be used in implementing the relevant regulatory and statutory mandates. Accord Cities Service Oil & Gas Corp., supra; Amoco Production Co., supra; Conoco Inc., supra.

[6] In addition, to the extent that appellant’s argument concerning retroactive application of a new rule is premised on the contention that the Procedure Paper constitutes a substantive rule of law, this contention also must fail. Nor does the initial acceptance of its payments by MMS officials compel a different result. In the absence of an express statement to the contrary, “all royalty payments are accepted subject to audit and the ‘silent acceptance of royalty when initially tendered does not constitute an express determination of the proper royalty level.’” Cities Service Oil & Gas Corp., supra at 260, citing Supron Energy Corp., 55 IBLA 318, 321 (1981).

Thus, the mere fact that appellant valued its production under one method and submitted royalty based on this valuation does not give
rise to any right in appellant to insist on the acceptance of its valuation method. As we noted in Cities Service Oil & Gas Corp., supra, where Government acceptance of the tender of royalties is made subject to post audit, the mere recomputation of the royalty payments due to the Government to correctly reflect fair market value of NGLP's does not constitute imposition of a penalty or give rise to an issue of retroactive application of a new rule. [Footnote omitted.]

Id. at 261.

[7] We recognize that appellant argues that a prior OIG audit of Conoco, which included royalty payments made on behalf of Cities Service, should estop the Government from challenging these royalty payments essentially on the theory that the failure of that audit to challenge the NGLP valuation should be interpreted as constituting "an express determination of the proper royalty level," within the meaning of Supron Energy Corp., supra. We do not agree.

In Conoco Inc., supra, we rejected this precise contention when it was argued by Conoco. In that case, the Board examined at some length the OIG audit in question:

In 1981, the Office of the Inspector General (OIG), U.S. Department of the Interior, conducted a general audit of Conoco's Federal oil and gas leases for the years 1978 through 1980. The purpose of the audit was to determine if Conoco's settlement procedures adequately provided for the proper computation and payment of royalties for the gas removed from its Federal leases. The OIG concluded that, with certain exceptions, Conoco's settlement system for the payment of royalties did not contain any material weaknesses and adequately provided for the reasonable payment of royalties. The OIG also noted that Conoco used actual net-back values as the basis for its determination of the value of NGLP produced from the leases. Although the OIG found certain problems with the calculation of royalties on NGLP, these problems did not directly relate to the net-back method of valuing NGLP. The OIG recommended that the Geological Survey (GS), the predecessor of MMS, direct Conoco to pay additional royalties based on the audit. As a result of this audit, Conoco has indicated that it paid $572,498 in additional royalties for the years 1978 through 1980.

Subsequently, the OIG conducted a specific audit of the royalties paid on NGLP removed from Federal leases and processed at the Grand Chenier Gas Processing Plant for the years 1977 through 1988. * * *

After review of the OIG audit report and appellants' comments on that report, the Tulsa Regional Manager, MMS, informed Conoco * * * of his preliminary royalty underpayment determinations by letters dated August 20, 1985.

Id. at 234.

In analyzing Conoco's contention that MMS should be bound by OIG's earlier audit, the Board noted that, during the time in question, the authority for valuation of production for royalty purposes was vested in the Director, Geological Survey, and those officials under his supervision. Thus, the failure of the earlier OIG audit to challenge the net-back valuation could not constitute approval by the Departmental official with delegated authority to approve valuation of production. Moreover, the Board expressly noted that "[a]ppellants have not presented the Board with any documentation regarding the additional royalty paid as a consequence of the earlier OIG nationwide audit from which it can be concluded that acceptance of the payment constituted a ruling on the issue of valuation of NGLP processed at Grand Chenier
in 1980." Id. at 243. Accordingly, the Board concluded that failure of the OIG nationwide audit of Conoco's payments to challenge the net-back valuation on which royalties were paid did not constitute "an express determination of the proper royalty level" such as would bar, under the Board's decision in *Supron Energy Corp.*, supra, a subsequent MMS audit specifically directed to production processed at Grand Chenier.

The same ruling must follow in this case. The present record is equally devoid of any documentation which would support the conclusion that acceptance of Conoco's tender of additional royalties subsequent to the 1981 OIG audit constituted a ruling on the issue of the valuation of NGLP's processed at Grand Chenier for the period prior to 1981. Therefore, we hold in conformity with our prior decision in *Conoco Inc.*, supra, that MMS was not estopped from reviewing the valuation of NGLP's processed at Grand Chenier prior to 1981.

[8] Cities Service also challenges the application of the Procedure Paper's "yardstick" valuation to those sales of NGLP's which occurred during the period of DOE price control. Appellant notes that the Procedure Paper expressly provides that during those periods in which non-ethane NGLP's were subject to DOE price controls, those prices would be presumed to be the fair market value unless the prices actually received by a lessee were greater. Inasmuch as Cities Service internally consumed rather than sold most of its NGLP's, there was no way in which it could have received prices in excess of the DOE maximum prices. Accordingly, appellant argues that the MMS order should be reversed to the extent that it directed that the "yardstick" prices should be used instead of the DOE maximum prices.

In our recent decision in *Shell Offshore Inc.*, supra, we explored this exact argument. Therein, we noted that the essence of MMS's position was that under 10 CFR 212.83(c)(ii) (1980) appellant, as a refiner, was permitted to allocate increased product costs (which would be recoverable through an increase in maximum permissible pricing under 10 CFR 212.161) "to a particular general refinery product in whatever amounts it deems appropriate." Therefore, MMS argued, the maximum price under which appellant valued the NGLP's should not necessarily be considered the maximum permissible price under DOE regulations because appellant had it within its power to so allocate any increased product costs (and thereby raise the maximum permissible price) to any particular refinery product as appellant saw fit. Thus, MMS concluded that the prices which appellant asserts were the maximum permissible prices under DOE regulations may not, in fact, have been the maximum prices allowable.

In our decision in *Shell Offshore Inc.*, supra, however, we rejected the MMS position which had disallowed appellant's reliance on the maximum DOE prices:
Initially we note that there is nothing in the record submitted to the Board to indicate that appellant did, in fact, allocate such increased product costs in a manner designed to lower its royalty payments. In any event, in *Phillips Petroleum Co.*, 109 IBLA 4 (1989), a panel of this Board held that a similar refusal to accept DOE ceiling prices as representing fair market value must be deemed arbitrary and capricious, given the instructions of the Procedure Paper. Accordingly, to the extent that the decision below instructed appellant to recompute the value of non-ethane NGLP's during the period in which these products were subject to DOE price controls, the decision must be reversed. [Footnote omitted.]

*Id.* at 253. We believe that the decisions in *Shell Offshore Inc.*, *supra*, and *Phillips Petroleum Co.*, *supra*, must control the result in the instant appeal. Accordingly, to the extent that the decision below rejected valuations of non-ethane NGLP's where the value reported was the maximum permissible price under the DOE regulations, the decision herein must be reversed.11

[9] There remains one further modification which we must make in the application of the Procedure Paper herein. As written, the Procedure Paper provided that in those situations in which the "yardstick" valuation applied, the average value of the "yardstick" for that month would be the minimum value accepted by MMS. However, in *Conoco Inc.*, *supra*, we rejected use of the average value of the "yardstick," noting that, since the lowest value of the "yardstick" established a floor price for royalty valuation and such price must, itself, constitute fair market value in order to be acceptable, the floor price rather than the average value of the "yardstick" should be used to recompute the royalty due to the United States. *Id.* at 244. See also *Shell Offshore Inc.*, *supra* at 250; *Cities Service Oil & Gas Corp.*, *supra* at 263; *Union Oil Co.*, 111 IBLA 369 (1989). We hereby modify the instant decision to conform to this holding.

Appellant has requested oral argument before the Board, pursuant to 43 CFR 4.25. In view of our disposition of the instant appeal, the Board has concluded that oral argument would serve no useful purpose and it is hereby denied.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decisions

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11 However, to the extent that appellant has argued that the Table 7 DOE prices were not properly applied to its propane sales because of existing arm's-length contracts establishing a lower price, its contention was properly rejected. Thus, the Director, MMS, noted that appellant had supplied only an incomplete copy of such a contract and that, in any event, the agreement concerned bulk sales and did not specify a specific source of the product. Accordingly, he rejected appellant's contention that these contracts should be interpreted as establishing an arm's-length contract price for propane processed at Grand Chenier and Lake Charles within the meaning of the Procedure Paper. We agree.

While an agreement for the bulk sale of NGLP's might be used as an arm's-length contract for the purpose of comparison with a non-arm's-length contract in order to establish the acceptability of the non-arm's-length contract, as provided for in the Procedure Paper (see *Shell Offshore Inc.*, *supra* at 253-55), it cannot be used to establish that any specific production of NGLP's were sold under an arm's-length contract absent a showing that the production in question was, indeed, transmitted to the purchaser under that contract and was required to be transmitted to the purchaser under that agreement. See generally *Amoco Production Co. v. Hodel*, 627 F.Supp. 1375 (W.D. La. 1986). Appellant has made no such showing here and, in the absence thereof, the Table 7 DOE prices are properly used to value the NGLP's.
December 19, 1990

Appealed from are affirmed in part, reversed in part, and set aside and remanded in part as explained above.

James L. Burski
Administrative Judge

I CONCUR:

John H. Kelly
Administrative Judge

REDA THUNDER, INC., ET AL.

117 IBLA 167 Decided December 19, 1990

Appeal from a decision of the Lewistown, Montana, District Office, Bureau of Land Management, approving an amendment to Federal Plan of Operations MTM 77779 and recommending approval of an amendment to Montana State Mine Operating Permit 00095.

Affirmed as modified.


The Board has discretion not to dismiss an appeal for failure to serve copies of appeal documents on an adverse party, as the regulations state merely that such failure will "subject the appeal to dismissal." In the absence of a showing of prejudice on the adverse party, a motion to dismiss for failure to serve is properly denied.


Even though an appellant corporation is not incorporated until after the date of issuance by BLM of the decision it seeks to appeal, its appeal is not properly dismissed for lack of standing if it appears (1) that the appellant corporation succeeded to the interests of an entity that participated in the decisionmaking process and, thus, became a party to the case, and (2) that both the appellant corporation and the earlier entity are adversely affected by BLM's decision.

3. Environmental Quality: Environmental Statements--Mining Claims: Plan of Operations

BLM's FONSI with respect to a proposed expansion of a mining operation will be affirmed if the record establishes that a careful review of environmental problems has been made, all relevant environmental concerns have been identified, and the final determination is reasonable. The record must establish that the FONSI was based on reasoned decisionmaking. Thus, one challenging such a finding must demonstrate either an error of law or fact or that the analysis failed to consider a substantial environmental problem of material significance to the proposed action. The ultimate burden of proof is on the challenging party. Such burden must be satisfied by objective proof. Mere differences of opinion provide no basis for reversal.
4. Environmental Quality: Environmental Statements--Mining Claims: Plan of Operations

Although an EA for a proposed expansion of a mining operation to build a new cyanide heap leaching pad may be "tiered" to an earlier EIS, the earlier document must contain adequate information to address the alternatives. Where the EIS does not address the full extent of cumulative impacts of retention of cyanide in abandoned heaps, and where BLM is actively reviewing this question prior to allowing leaching of ore to begin on the new pad, BLM's decision to allow the permit amendment will be modified to make clear that BLM must consider whether to prepare a supplemental EIS considering cumulative impacts before allowing leaching operations to begin.

5. Indians: Generally--Mining Claims: Plan of Operations

Sec. 2 of the AIRFA does not prohibit BLM from adopting a land use that conflicts with traditional Indian religious beliefs or practices. BLM complies with AIRFA if, in the decisionmaking process, it obtains and considers the views of the Indians, and if, in project implementation, it avoids unnecessary interference with Indian religious practices.

APPEARANCES: Don R. Marble, Esq., Chester, Montana, for Red Thunder, Inc.; Virgil F. McConnell, Sr., pro se; Dean E. Cycon, Esq., New Salem, Massachusetts, for Island Mountain Protectors and Fort Belknap Community Council; Alan L. Joselyn, Esq., Helena, Montana, for Zortman Mining, Inc.; Tommy H. Butler, Esq., Special Assistant Attorney General, for Department of State Lands, State of Montana; Karen Dunnigan, Esq., Office of the Field Solicitor, U.S. Department of the Interior, Billings, Montana, for the Bureau of Land Management; John C. McKeon, Esq., for amicus curiae Phillips County, Montana.

OPINION BY ADMINISTRATIVE JUDGE HUGHES

INTERIOR BOARD OF LAND APPEALS

Red Thunder, Inc., Virgil F. McConnell, Sr., Island Mountain Protectors (IMP), and Fort Belknap Community Council (FBCC) (appellants) have each appealed the June 22, 1990, decision of the Lewistown, Montana, District Office, Bureau of Land Management (BLM), approving the application of Zortman Mining Co. (Zortman) for an amendment to Federal Plan of Operations M-77779 for expansion of the Landusky Mine in Phillips County, Montana. Pursuant to a memorandum of understanding (MOU) between BLM and the Department of State Lands (DSL), State of Montana, BLM also recommended approval of Zortman’s request for amendment of State Operating Permit 00095.1

By order of September 14, 1990, we consolidated the appeals. Two separate statements of reasons were filed, one jointly on behalf of Red Thunder and McConnell, and one jointly on behalf of IMP and FBCC. These statements of reasons raise similar arguments, and, for

1 The MOU, approved in April and May 1984, essentially provides for joint regulation of mining and protection of surface resources by BLM and DSL.
simplicity’s sake, we shall refer to appellants jointly. Zortman, BLM, and DSL have filed answers. Red Thunder has filed a reply brief.\(^2\)

The Landusky Mine permit was originally issued on June 6, 1979, following the preparation by DSL of an environmental impact statement (EIS) pursuant to Montana State law.\(^3\) BLM did not participate in consideration of the original permit, which was issued for patented lands.

The amendment approved by BLM/DSL in June 1990 was the 10th amendment to the mining plan for the Landusky Mine and is thus referred to as Amendment No. 10. BLM\(^4\) did not prepare an EIS prior to approving the amendment, but did prepare an environmental assessment (EA), known as EA No. 10. In addition, following public meetings and receipt of comments, BLM prepared an addendum to EA No. 10, called simply the Addendum. Approval of Amendment No. 10 also involved imposition of 11 stipulations, several of which are at issue here. At the conclusion of the EA when the record of decision (ROD) was completed, BLM made a finding of no significant impact (FONSI).

The Landusky Mine is located just outside the southeast corner of the Fort Belknap Indian Reservation in an area that has been extensively mined in the past. Mining operations there employ large-scale cyanide heap leaching to remove gold and silver from low-grade ore. Although discussed in more detail below, the mining process is summarized as follows:

The project area is within the Little Rocky Mountains of Phillips County, the site of numerous past mining and leaching operations. * * * Pit run ore from the mine [is] trucked approximately three quarters of a mile to the leach site where cyanide solution [is] applied in a closed-circuit leaching process. Ore [is] placed on an impervious barrier, the cyanide solution [is] applied using pvc pipe and irrigation type sprinkler heads. A “pregnant” solution containing gold and silver values [is] recovered from the leach heap and pumped to a precipitation press to remove the gold and silver from solution. The barren solution [is] adjusted for cyanide levels and reapplied to the leach heap. The leached heap materials [are] graded and reclaimed in place. Concentrate from the press [is either] sold unrefined or shipped to a custom smelter. (EIS at 1). Zortman further explains: “The system is ‘closed’ and does not involve any discharge of cyanide solution to the environment. The leach pads include a composite liner system consisting of compacted clay and synthetic membrane * * * to prevent solution loss and possible groundwater contamination” (Zortman Answer: Response to Red Thunder/McConnell at 2).

Over the 11-year history of the mine, different leach pads have been built, loaded, and leached to completion (Zortman Answer, Exh. 1).

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\(^2\) Phillips County, Montana, also filed a motion for leave to appear as amicus curiae and a brief addressing the financial consequences of disallowing expansion of the Landusky mine. Although these comments were offered in the context of whether the effect of BLM’s decision should be stayed pending appeal, they also bear on the merits of the appeal. Phillips County’s request to appear as amicus is granted.

\(^3\) The governing law is the State of Montana’s Environmental Policy Act (MEPA), Section 69-6504, R.C.M. 1947.

\(^4\) Unless noted specifically, all further references to BLM’s consideration of mining plan amendments actually refer to joint BLM/DSL consideration under the MOU.
Approving Amendment No. 10 allows construction of the Sullivan Park Leach Pad, which has evidently been completed. However, owing to the imposition of Stipulation No. 9 on the permit, Zortman is not allowed at present to conduct mining on the new pad.

At the center of the present controversy is the issue of the extent to which cyanide solution is left behind following completion of mining when the spent ore is “reclaimed in place” as described in the EIS. In addition to reclamation of the Sullivan Park Pad, reclamation of all the completed pads at the Landusky Mine (called “spent ore heaps”) is at issue, as Stipulation No. 1 to the approval of Amendment No. 10 requires Zortman to continue neutralization of all spent ore heaps until certain low levels of cyanide discharge are established and maintained. Appellants challenge BLM’s handling of the issue of cyanide retention in the spent heaps.

[1] Before considering the merits of the appeal, we take up two procedural matters. Zortman has moved that the appeals be dismissed for failure of the appellants McConnell, IMP, and FBCC to timely serve copies of their notices of appeal and statements of reasons. This motion is denied. The Board has discretion not to dismiss an appeal for failure to serve, as the regulations state merely that such failure will “subject the appeal to dismissal.” 43 CFR 4.413(b); Defenders of Wildlife, 79 IBLA 62 (1984); see James C. Mackey, 96 IBLA 356, 359, 94 I.D. 132, 134 (1987); Tagala v. Gorsuch, 411 F.2d 589 (9th Cir. 1969). The Board avoids procedural dismissals if there has been no showing that a procedural deficiency has prejudiced an adverse party. Indeed, in the absence of such showing, dismissal of an appeal might be deemed an abuse of discretion. See United States v. Rice, No. CIV. 72-467, PHX WEC (D. Ariz. Feb. 1, 1974), reversing United States v. Rice, 2 IBLA 124 (1971). We are unpersuaded that Zortman or any other adverse party was prejudiced by any delay in receiving copies of appellants’ pleadings.

In any event, it is hard to fault appellants for any untimely service of pleadings on Zortman, in view of BLM’s failure to denote Zortman in its decision as an “adverse party” entitled to such service by any appellant. See Beard Oil Co., 105 IBLA 205 (1988). Appellant’s obligation to serve copies of appeal pleadings is technically limited to parties so named. 43 CFR 4.413.

[2] A more serious question is raised by Zortman regarding the standing of appellant Red Thunder to file an appeal here. Under 43 CFR 4.410, the right of appeal to this Board is strictly limited to “[a]ny party to a case who is adversely affected by a decision” of BLM. It is established that, if the would-be appellant lacks standing, the appeal must be dismissed. The Wilderness Society, 110 IBLA 67, 72 (1989).

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4 This Board, by order dated Sept. 14, 1990, lifted a temporary stay of the effectiveness of BLM’s decision approving the plan amendment, clearing the way for completion of the pad.

6 A companion motion to dismiss the appeals of IMP and FBCC for failure to timely file statements of reasons was subsequently withdrawn as unfounded.
There is no dispute that the members of Red Thunder, as users of lands that are being impacted by the Landusky mine, are adversely affected by BLM's decision. However, Zortman has established that Red Thunder, Inc., was not incorporated until July 12, 1990, after the date of BLM's decision (Zortman Memorandum in Support of Request for Recision of Stay, Affidavit of Joscelyn). Thus, Red Thunder did not exist as a legal entity during the time prior to the issuance of the decision, and there is a question as to whether it can properly be held to have been a "party to the case" under appeal.

Red Thunder responds that the people organized as Red Thunder, Inc. were appearing individually and together as Loud Thunder International-Little Rockies Chapter. * * * All that is involved is a name change. Red Thunder members and [its] group appeared and participated as a group at the proceedings. Prior to incorporation as Red Thunder, Inc., the group was not incorporated. All that happened is that the group known as Loud Thunder International-Little Rockies Chapter was incorporated as Red Thunder, Inc. They did participate fully in the proceedings.

(Red Thunder Reply at 41-42). Although Zortman also filed evidence indicating that a group known as Loud Thunder International, Inc., was incorporated in Montana in 1986 (Zortman Memorandum in Support of Request for Recision of Stay, Affidavit of Joscelyn), there is nothing to indicate that Loud Thunder International-Little Rockies Chapter, was incorporated at that time.

The Board routinely allows corporations to file appeals on behalf of its predecessors-in-interest on the presumption that the appellant has succeeded to these interests. We regard Red Thunder's representation that the group known as Loud Thunder International-Little Rockies Chapter was incorporated as Red Thunder, Inc., as an implicit assertion that Red Thunder succeeded to the earlier group's interest. As the earlier group did participate before BLM, it is a party to the case, and Red Thunder, as its successor, may appeal.

[3] Turning to the merits of the appeal, it is well established that the Board will affirm a FONSI with respect to a proposed action if the record establishes that a careful review of environmental problems has been made, all relevant environmental concerns have been identified, and the final determination is reasonable. The record must establish that the FONSI was based on reasoned decisionmaking. Thus, one challenging such a finding must demonstrate either an error of law or fact or that the analysis failed to consider a substantial environmental problem of material significance to the proposed action. The ultimate burden of proof is on the challenging party. Such burden must be satisfied by objective proof. Mere differences of opinion provide no basis for reversal. G. Jon Roush, 112 IBLA 293, 297-98 (1990), and cases cited.

Apart from the issue of whether preparation of an EA, rather than an EIS, was legally sufficient (considered separately below), appellants
generally challenge the adequacy of BLM’s environmental review and the accuracy of its conclusions concerning mining at the Landusky Mine. We have reviewed these challenges and, except as discussed below, reject them. Appellants have generally failed to meet their burden of establishing error in BLM’s FONSI. Several points are addressed below in the context of legal questions. Others require specific comment.

Appellants fault BLM for not considering the effects of cyanide heap leaching on water sources that run into the reservation from the mine through King Creek. The record establishes that BLM has imposed adequate safeguards to ensure that the water quality in King Creek is maintained, including several water monitoring wells. Although the stream is not being monitored on the reservation itself, water in both King Creek and South Big Horn Creek is monitored by wells in several places as it leaves the minesite (Zortman Answer, Exh. 2). Appellants have not shown that this procedure is inadequate to ensure that these streams are not contaminated. Further, appellants have not convincingly countered Zortman’s assertions that analysis from these monitoring wells reveals no degradation of water quality (id. at Exh. 6) or that the reason the streams are not monitored on the reservation is that the Fort Belknap Community Council has not authorized water monitoring on the reservation itself. Id. at 12.

The EA’s that have been prepared concerning the Landusky Mine are not perfunctory documents, as suggested by appellants, but extensive and reasoned analyses of environmental effects of mining. Although there is a question here as to whether it is legally permissible to conduct environmental review in the procedural context of an EA rather than an EIS, we wish to expressly dispel any impression that BLM’s EA’s are not thorough documents. To the contrary, these EA’s demonstrate that BLM has responsibly undertaken its management duties in connection with the Landusky mine. Zortman has clearly not escaped responsibility for overall environmental impact. BLM has clearly engaged in “reasoned decisionmaking,” and its conclusions are generally reasonable. See G. Jon Roush, supra. As noted below, BLM’s review of Zortman’s responsibilities is ongoing.

As to pollution of ground water, Zortman has provided a hydrological study indicating that underground aquifers are not affected by the operation (Zortman Answer, Exh. 5). Appellants have provided no convincing evidence to the contrary.

7 See, e.g., note 16.

8 Red Thunder has filed pictures of King’s Creek assertedly showing that water in a beaver pond there is “cloudy,” “slimy looking,” and “orangish” and that there is siltation above the beaver dam. No attempt is made to analyze the cause of these conditions or to relate them to mining activities at the Landusky mine (Red Thunder Response, Photographs 10-16). This failure is critical in view of evidence in the record suggesting that King’s Creek is being adversely impacted by tailings left from previous mines unrelated to the Landusky mine operation. E.g., Zortman Answer Exhs. 1 and 2.

Red Thunder also asserts that EA No. 10 at page 15 indicates that groundwater could flow to the north, and that BLM has not addressed this question. The EA indicates only that there “may be” flow to the northeast, which is away from the Reservation. Regardless of whether the flow is toward or away from the Reservation, the record indicates that water quality is to be sampled at locations toward the northeast of the mine.
In effect, appellants challenge BLM’s January 1990 decision to allow permit modification No. 9 without doing an EIS. They cite to a statement in EA No. 9 that no EIS would be required if heap slopes were reduced from 2 horizontal:1 vertical (2H:1V) to 3H:1V. Noting that BLM in fact approved 2H:1V slopes, they question why an EIS was not prepared for permit modification No. 9.

We note that the time for appealing BLM’s decision to allow plan amendment No. 9 has long since expired. The slope angle approved in Amendment No. 10 for reclamation of the Sullivan Park leach pad is 3H:1V, with intervening benches of indeterminate width every 200 feet of slope length (Permit Amendment No. 10, Stipulation 3). Appellants do not challenge this requirement. Thus, the issue of the earlier approved slope angle is not before us.

Nevertheless, we see no impropriety in BLM’s changing its mind regarding the necessity to prepare an EIS for Amendment No. 9. Appellants are correct that BLM noted its concern that there was potential for “reclamation failure on the long 2H:1V slopes of the reshaped heap” in the EA prepared for this amendment (EA No. 9):

> The consequences of failed reclamation on the heap slopes could include precipitation infiltration and periodic discharge of residual solutions from the abandoned heap, and potential plugging of the pad underdrain system. Placement and reduction of ore lifts to 3H:1V would increase the feasibility of successful reclamation, and would allow additional corrective or mitigative measures should reclamation problems be realized.

(EA No. 9 at 28-29). However, BLM did not indicate that these problems could be avoided only by using a 3H:1V slope.

Zortman offers the following explanation for BLM’s eventual decision not to require 3H:1V slopes:

> The reclaimed slope for the Mill Gulch Heap Leach Pad permitted in EA 9, was resolved by negotiation involving DSL, BLM, and [Zortman]. During those negotiations, the agencies expressed that their primary concern was not so much slope angle but slope length. Accordingly, [Zortman] agreed to break up the long slopes with benches every 200 feet. Application of the benching reduces the overall slope angle from [2H:1V] to approximately [2.25H:1V]. The requirement for benching was set forth as a permit condition for Permit Amendment No. 9.

(Zortman Answer at 15). Thus, it is evident that, although BLM may have been concerned at one time during the review process for plan amendment No. 9 that 2H:1V slopes were inadequate, it changed its mind, concluding that any adverse environmental effects could be mitigated by inserting benches, thus lowering the effective slope for the leach pad. Appellants have not shown that BLM’s decision was incorrect. Further, BLM has not ruled out the possibility that “additional action” might be required if problems develop with the slope angle approved by permit amendment No. 9 (Addendum at 21).9

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9 Zortman disputes BLM’s authority to take such action (Zortman Answer at 16-17). It is unnecessary to resolve this issue at this time.
We also reject appellants’ assertions that BLM has improperly failed to analyze the environmental impacts of the mining of sulfide gold and silver ore at the Landusky mine. It is entirely possible that Zortman may never mine the sulfide ore at the Landusky mine. Preparation of an EIS is not required when agencies are merely contemplating a project and it is unclear whether the program will necessarily result in a proposal for major Federal action. Kleppe v. Sierra Club, 427 U.S. 390, 403-06 (1976). Thus, there is no problem with segmenting the environmental review so that the effects of mining non-sulfide (oxide) ore (which has been ongoing for 10 years) are considered independently of the effects of mining sulfide ore. We are well aware that mining sulfide ore would present environmental questions that must be addressed. However, no application has been filed by Zortman requesting permission to mine such ore. Thus, there is no proposed action to be reviewed. Zortman admits that it has begun to prepare baseline information for a sulfide reserves application, but no showing has been made that this collection of information in any way affects the environment. Accordingly, BLM has properly declined to consider the effects of mining sulfide ore at this time.

Finally, appellants have failed to support their allegations that the Montana Gulch leach pad has been built on a former mine site known as the “wind tunnel.” Even putting aside the fact that appellants’ challenge is not timely, in the absence of any supporting documentation suggesting the location of previous mine workings, we reject this allegation as pure speculation. Appellants also make unsubstantiated allegations regarding alleged design flaws with the leach pad and impacts on wildlife. In the absence of convincing supporting evidence, and in view of information to the contrary provided by Zortman, these allegations are also rejected.

Although we generally affirm BLM’s decision, there are two unresolved questions that require specific consideration.

[4] The first concerns BLM’s decision not to prepare an EIS for Amendment No. 10. Section 102(2)(C) of the National Environmental Policy Act of 1969 (NEPA) requires preparation of an EIS in the case of “major Federal actions significantly affecting the quality of the human environment.” 42 U.S.C. § 4332(2)(C) (1988). Appellants have questioned whether BLM erred by granting this permit amendment without preparing an EIS. Several issues must be resolved in answering this question.

First, we must determine whether BLM used an EA that was “tiered” to an EIS prepared in 1979 by DSL in compliance with the State of Montana’s Environmental Policy Act (MEPA), Section 69-6504, R.C.M. 1947, in connection with consideration of the application for the original mining permit, so that no EIS was required for the permit.

10 Zortman indicates that an EIS should be prepared if it submits an application for the development of sulfide materials at the Landusky mine, presuming that a major change in potential environmental effects is determined to exist (Zortman Answer at 7-9).
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amendment. We frequently affirm BLM decisions to prepare an EA rather than an EIS where the EA supplements or is tiered to an earlier EIS. See, e.g., Oregon Natural Resources Council, 115 IBLA 179, 186 (1990). Although an EA for an action may be "tiered" to an earlier EIS, the earlier document must contain adequate information to address the alternative. Id. at 186.

Over the last 11 years, Zortman's permit has been amended 10 times, and the environmental effects of each amendment have been addressed in the context of an EA that was "tiered" to the original EIS. The original EIS considered the environmental impacts of 18-20 years of mining, but foresaw only 530 acres being affected in the life of the operation (EIS at 18). It appears that this acreage has been greatly exceeded (McConnell Statement of Reasons at 4; Red Thunder Response at 2). The failure to consider in the 1979 EIS the extent that the mine has reached does not conclusively establish that BLM's decision to prepare an EA was defective, however.

Under the CEQ regulations, the terms "effects" and "impacts" are synonymous. 40 CFR 1508.8 (1989). The term "effects" includes ecological, esthetic, historic, cultural, economic, social, or health considerations, whether direct, indirect, or cumulative.

We perceive two distinct varieties of possible effects here. First, there are "operational" effects, which abate when mining operations are completed. These effects are associated with actively mining and processing ore and arise from two principal activities: (1) removal and transportation of ore and roadbuilding, including disruption of surface drainages and vegetation, disruption of underground aquifers, siltation of drainages, contamination of water resources that come in contact with rock exposed by mining, noise of operations, visual impacts of opening the ground, and release of dust into the air; and (2) effects of removing gold and silver from the ore at the leach pad using cyanide.


The CEQ regulations describe "tiering" as follows:

"[T]iering" refers to the coverage of general matters in broader [EIS's] (such as national program or policy statements) with subsequent narrower statements or [EA's] (such as regional or basinwide program statements or ultimately site-specific statements) incorporating by reference the general discussions and concentrating solely on the issues specific to the statement subsequently prepared. Tiering is appropriate when the sequence of statements or analyses is: (a) From a program, plan, or policy [EIS] to a program, plan, or policy statement or analysis of lesser scope or to a site-specific statement or analysis; or (b) From an [EIS] on a specific action at an early stage (such as need and site selection) to a supplemental (which is preferred) or a subsequent statement or analysis at a later stage (such as environmental mitigation). Tiering in such cases is appropriate when it helps the lead agency to focus on the issues which are ripe for decision and exclude from consideration issues already decided or not yet ripe." 40 CFR 1502.20 (1989).
solutions, such as release of hydrogen cyanide gas into the air or leakage of cyanide solution into the groundwater or streams, where it might remain in solution.  

Many of these potential adverse operational effects can be and have been successfully prevented by design features and mitigating measures built into the mining plan as approved. When mitigating measures are proposed or required to reduce the environmental effects of the proposed action, a FONSI is properly affirmed. Idaho Natural Resources Legal Foundation, 115 IBLA 88 (1990), and cases cited. Unpreventable adverse operational effects have been adequately considered throughout the history of the Landusky mine and were specifically addressed in the original EIS. In sum, Amendment No. 10 presents no new operational effect that has not been fully considered in the past.

However, there are also possible effects associated with reclaiming the mine site after mining operations are completed, including erosion of reclaimed slopes and related siltation of streams, and release of cyanide gas into the air or leakage of cyanide solution from the reclaimed leach pad. These impacts continue after mining operations are completed and accumulate as a larger area is mined and reclaimed. Thus, they fall within the definition of “cumulative impacts.”

There is presently a substantial question as to what the cumulative impacts will be of leaving cyanide solution in the spent ore on the abandoned leach pads. Although it is inevitable that some amount of cyanide will be left behind, the record clearly establishes that there would be no significant impact if only small concentrations of potentially free cyanide remain, or if the cyanide left behind is so “entrained” in the rock as not to be able to leave the dump site.

According to the Environmental Handbook for Cyanide Leaching Projects, prepared by Radian Corp. for the National Park Service, U.S. Department of the Interior in June 1986, cyanide used for heap leaching consists of an aqueous solution of sodium cyanide (NaCN) containing, among others, cyanide ions (CN\(^-\)), also known as cyanogen. Cyanide ions readily hydrolyze (with hydrogen ions \([H^+]\) in water) to form hydrocyanic acid (HCN). Hydrocyanic acid is a colorless liquid with a boiling point of about room temperature (25.5 [centigrade]. Hydrocyanic acid vapor (HCN gas) is less dense than air, flammable and toxic."

HCN gas forms readily, unless the pH of the solution is kept high, that is, HCN forms readily if the solution becomes acidic. Thus, in order to prevent the formation of toxic HCN gas, "it is important to maintain an elevated solution pH throughout processing operations." Solution pH is controlled by the addition of agents such as lime (CaO) or caustic soda (NaOH). Id. at 2-3. The record indicates that Zortman keeps the pH of the cyanide solution high by adding lime. EIS at 5 and 9. Under the EQ regulations, "cumulative impact" is defined as "the impact on the environment which results from the incremental impact of the action when added to other past, present, and reasonably foreseeable future actions regardless of what agency (Federal or non-Federal) or person undertakes such other actions. Cumulative impacts can result from individually minor but collectively significant actions taking place over a period of time." 40 CFR 1506.7 (1989).

In this regard, we are not impressed with appellants' greatly oversimplified assertion that BLM is allowing a "billion gallons of solution of deadly poison" to be left behind. Although there is some question as to whether potentially unfavorable conditions may exist in reclaimed pads and waste piles at the Landusky mine, the image of a
It is noteworthy that the amendment approved by BLM included a comprehensive mine reclamation plan which applies to all ore heaps at the Landusky mine, requiring cyanide neutralization of all spent ore heaps to continue until a leachate discharge of less than 0.22 mg/liter weak acid dissociable solution (WAD) is maintained over a 6-month period, including a snowmelt and spring runoff period (EA at 79; EA Addendum at 18). Thus, concern was raised about the cumulative impacts of past reclamation from the beginning of consideration of Amendment No. 10.

The fact remains that, even after BLM studied the question and even though it purported to conclude that there was no significant cumulative impact from leachate discharge, BLM is evidently not convinced that the concentrations left behind will be safe. In the EA, BLM noted that reclaimed heaps might contain a large volume of residual cyanide that cannot be flushed from the heaps because of "blind-offs" (zones of low permeability inside the heaps) and "preferential flow paths" caused by migration of fine rock (EA at 34-35). BLM noted its concern that, "[a]fter rinsing, not all of the solution within the decommissioned heaps would dewater by gravity drainage," raising the possibility that "contaminated discharge could occur" (EA at 36).

BLM dealt with its concern on this question in the Addendum to the EA:

The potential for blind-offs is not as great as first stated in the EA due to additional data supplied by the operator regarding the amount of fines in the ore. However, the amount of retained solution still stands at more than one billion gallons for all the Landusky heaps. This amount is based on the specific moisture retention of the ore after billion gallons of lethal chemical liquid impounded there, leaking into streams and groundwater and polluting the air, is hardly accurate.

Cyanide rapidly reacts with other chemicals in the environment to become harmless:

"Unlike many pollutants which may accumulate in the environment, cyanide is a very reactive and relatively short-lived contaminant. As such, cyanide is considered to be a transient pollutant. * * * A number of processes have been identified as potentially significant in the natural degradation or depletion of cyanide in effluents from many gold processing operations. These processes are volatilization, oxidation, biodegradation, photodecomposition, and cyanide-thiocyanate reactions. For solutions of high concentration, polymerization and hydrolysis may also be important." Environmental Handbook for Cyanide Leaching Projects, at 5.

Cyanide is only toxic under certain conditions, generally involving high concentrations of the CN⁻ ion in acidic solutions. In the present situation, the record shows that much of the cyanide solution is "entrained" in the rock and is therefore not free to migrate. Further, much of the CN⁻ is "complexed" (joined with) metals (including cobalt and iron) under strong chemical bonds that are very stable, so that the CN⁻ is not capable of converting to toxic HCN.

Thus, the concern is not necessarily with the volume of cyanide liquid solution, but the concentration of CN⁻ present that is capable of leaking into drainages, migrating into the groundwater, or being converted to HCN gas. This concentration is measured as "weak acid-dissociable cyanide" (CN⁻ WAD) and represents the maximum amount of potentially harmful free CN⁻ that may be released.

BLM has established a CN⁻ WAD concentration standard of 0.22 milligrams (mg) per liter for cyanide left in the heaps, greatly below the lower limit for human physiological responses. Zortman has calculated the residual CN⁻ WAD concentration to be 0.08 mg/liter, but, as discussed below, BLM has required that the concentration remaining in abandoned pads and ore heaps be tested as a condition to allowing operations at the Sullivan pad, thus suggesting strongly that it remains unconvinced that this standard has been met.

17 Cyanide retention in the ore heaps and heap neutralization were covered at length in the EA. Following completion of the leaching process, the cyanide solution is to be flushed from the spent ore heaps on the leach pad using fresh water or oxidizing compounds. The flushing is to continue until the effluent solution reaches a level not greater than 0.22 mg/liter, at which time the heap is considered detoxified and ready for reclamation. Prior to reclamation, all fluid is to be drained from the heap, leaving behind residual solution (EA Addendum at 9, 19, and 29; Zortman Answer at 33-34).
rinsing optimistically assumed to be equal to the natural moisture content of the pit-run ore (4%). New calculations, involving rinsing with three circulation volumes, estimate cyanide concentrations in the retained solution at no more than a 2 ppm average compared to the 25 ppm originally stated on page 81 [of the EA]. This calculates to 19,200 pounds of cyanide retained in all the Landusky heaps instead of the 240,000 pounds [indicated] in the EA. This is assuming only minimal development of blind-offs affecting heap neutralization efforts.

(EA Addendum at 9).

Nevertheless, BLM deemed it necessary to require Zortman, as a condition to granting the permit amendment, to undertake a study to research the following:

a) Cyanide concentrations and specific moisture retention in the heaps after neutralization;
b) Development of blind-offs within the heaps and their effect on heap neutralization;
c) Infiltration rates as they relate to reclamation practices;
d) Rates of natural cyanide degradation occurring over time in neutralization heaps; and
e) Long-term seepage from reclaimed heaps to identify volumes, concentrations of metals and cyanide, and rates of natural cyanide degradation and metal attenuation which would occur following release of the solution.

(Operating Permit 00095, Amendment No. 010 (Sullivan Park Expansion), Stipulation No. 9). BLM expressly noted its uncertainty as to whether existing reclamation techniques were adequate: “Study results will be used to determine the need for modification to the approved reclamation procedures or additional environmental analysis.” Id. The results of this study will be critical to determining whether there is an environmental problem associated with reclamation of the heaps.

DSL has recognized that, in view of the need for further study of the concentrations of cyanide retained in the heaps, additional appropriate environmental review will be necessary (DSL Answer at 14). However, BLM’s decision to require further study of the effects of heap leaching on the scale proposed by the Sullivan Park extension fails to make clear that further environmental study documents will be prepared when the study is complete. We therefore modify the decision to make clear that BLM shall determine, after completion of the study ordered by Stipulation No. 9, whether to prepare a supplemental EIS. This

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18 We are well aware that Zortman asserts that BLM’s conclusion that blind-offs may have occurred is flawed. It argues that BLM has not properly considered the effects of the rock types at the Landusky mine, noting that the rock placed on the pads has low clay content and is coarse, with a small percentage of fines. Further, Zortman argues that BLM, in considering the concentration of cyanide left behind, failed to take into account that the concentration of the cyanide initially placed on the heap (500-600 parts per million (ppm)) is greatly reduced by “natural cyanide degradation” that occurs when the heap is “rested” or “idled” after leaching to allow the facility to fully drain. Zortman further asserts that it has core sampled “several heaps where leaching has been completed, but which have not been either rinsed or chemically treated to neutralize cyanide.” Although each heap was sprayed with 500-600 ppm cyanide for several years before being idled, it asserts, “[n]atural degradation and flushing from precipitation events [have] reduced the total cyanide level in the rock by over 99 percent * * * to an average of 3.54 ppm,” and that “[t]he WAD cyanide level * * * in the rock averages 1.68 ppm.” Thus, according to Zortman, BLM’s “estimates of retained cyanide [after heap neutralization] are flawed since they begin with a cyanide level substantially above what will be experienced under field conditions” (Zortman Answer at Exh. 9-3). Zortman asserts that the residual solution retained in the heap will be entrained in the voids and pore spaces of the rock, which will look and feel dry (Zortman Answer at 34, Exh. 8).

BLM will presumably consider such questions in connection with the study it has ordered in Stipulation No. 9 of the permit amendment approval.
determination shall be prepared in conformity with 40 CFR Part 1500 (1989) and Departmental regulations. BLM’s decision shall be subject to appeal.

[5] Secondly, appellants argue that the approval of the mining plan should be set aside because BLM failed to comply with Section 2 of the American Indian Religious Freedom Act of 1978 (AIRFA). Section 2 of AIRFA provides:

On and after August 11, 1978, it shall be the policy of the United States to protect and preserve for American Indians their inherent right of freedom to believe, express, and exercise the traditional religions of the American Indian, Eskimo, Aleut, and Native Hawaiians, including but not limited to access to sites, use and possession of sacred objects, and the freedom to worship through ceremonials and traditional rites.


We note initially that, contrary to appellants’ allegation, BLM obtained the views of the Indians in the project area before allowing the amendment. BLM held public meetings and technical briefings on the reservation prior to approving the amendment and solicited the comments of Indians there. These meetings brought to light concern among the Indians regarding the visual and audio effects of mining on individual and collective ceremonial and traditional rites practiced by members of the Assiniboin and Gros Ventre Tribes.

The only group rite at issue is the Sun Dance, group Indian religious ceremonies held annually for 4 days at the Pow-wow Grounds on the Fort Belknap Indian Reservation. In response to these concerns, BLM imposed a significant ameliorating measure, Stipulation No. 11, providing that blasting will be barred during the period of the annual Sun Dance ceremonies.

There is also the question of the negative impact of noise and visual impacts from the mining operation on the individual Indian religious rite of “vision questing” or “fasting,” which is undertaken by individual Indians and which (unlike the Sun Dance) may be undertaken at any time.19 The case record contains the results of a study by a BLM archeologist, based on a tour taken by him and several Indian people from the Hays and Lodgepole communities on June 8, 1990. This study identifies eight areas considered important “fasting”

19 Appellant McConnell describes these activities as follows:

"Fasting," also called vision questing, involves spending time alone on mountain tops or other isolated, high places. Before one goes on a fast, he or she must first attend a sweat lodge. Then they must go to the mountain top before the end of the same day by walking from the bottom of the mountain. A robe, pipe and staff are taken. Then 4 days and nights are spent on the mountain alone with the Creator and the grandfather spirits. No food or water is taken. The purpose of these fasts is to seek help for sick relatives, friends or people in general, to get names or religious songs, to find medicine, to accomplish manhood, and spiritual reasons. The fasting must be carried on alone and in a quiet, isolated area with no unnatural distractions. Activities such as mining, logging, and road building that create noise and visual disturbances cause problems in the process." (Red Thunder/McConnell Statement of Reasons, McConnell Affidavit at 2).
areas on public lands in the Little Rocky Mountains near the Landusky mine, outside the Fort Belknap Indian Reservation.\textsuperscript{20} Appellants allege that both blasting and the operation of mining trucks and other heavy equipment impinge on fasting and vision questing and that AIRFA therefore bars the granting of the amendment.\textsuperscript{21} Further, appellants fault BLM for not addressing these impacts more thoroughly in the environmental review process. No amelioration was addressed or implemented for effects on individual Indian religious ceremonies.

The impacts of noise from the mining operations appear not to have been addressed in the 1979 EIS.

The EA states as follows concerning “Native American Religious Concerns”:

The Little Rocky Mountains have been identified as an area where Native American religious activities such as prayer, fasting and vision questing are practiced. To date, no specific sites have been identified by Native Americans as religiously significant that would be disturbed by the mine expansion. A class III cultural resource survey of the areas proposed for disturbance did not identify any sites associated with Native American use of the area.

Impacts to Native American religious use would be mainly in connection with visual intrusion should religious activities occur in the mine viewed. Approval of the mine expansion would not add to the already substantial difficulty Native Americans would have conducting religious activities in this area.

The Addendum to EA No. 10 contains responses to some specific questions raised by Indians and Indian groups during the meetings, but does not significantly address impacts on individual religious practices, promising instead only to consider the impacts of blasting when making the permit decision and any new information provided during the June 8 field trip (Addendum at 6-7, 7-8, 11, 15, 15-16, 16).

EA No. 10 addressed impacts of noise levels on residences in Landusky, located from one-half to 1 mile from the mine, noting that noise is associated with mine operation equipment (“haul trucks, dozers and front-end loaders”) and that this equipment was anticipated to remain “the same or very similar” (EA at 21-22). Thus, EA No. 10 implicitly found that the impacts from noise on individual Indian religious practices, some of which may be practiced as close as 1 mile from the mine, would also remain constant.

\textsuperscript{20} This report is stamped as a “draft” and denoted as “proprietary data.” The material was placed in the case record and has been referred to by BLM in official documents on the permit process. Thus, we do not see how it can properly be considered to be a draft. As to the proprietary nature of the report, BLM stated: “The following [report] documents the location and the fundamental importance of the areas or sites considered to be sacred by Native Americans of the Fort Belknap Reservation who follow the traditional ways of the Assiniboin and Gros Ventre Tribes * * * . Locations of and reasons for the importance of these cultural resources are given. The native people who were willing to risk provision of this information did not ask that their privacy be protected, but professional ethics dictates that this be done. Accordingly, their identities are not disclosed. The information they provided is very sensitive, and must be treated with the respect for the continued cultural viability of these people. The locations of the cultural resources, or the reasons for the importance of these resources [are] not to be made available to the general public.”

\textsuperscript{21} The issue of “light pollution” from artificial lights at night was also raised by an Indian commenter but not addressed by BLM (Addendum at 7-8). This issue has not been raised on appeal.

\textsuperscript{22} The EA also repeats at page 41 that “[a] class III cultural resource survey of the areas proposed for disturbance did not identify any sites associated with Native American use of the area.”
Concerning visual impacts, the EA notes that the “addition of the Sullivan Park heap would constitute an additional intrusion into the already altered landscape” (EA at 41). The EIS had earlier noted that the “natural visual and esthetic resources” of the area had been “heavily influenced by past mining activities,” including road construction disturbance from exploration and mining (EIS at 72). It concluded as follows:

The proposed mining operations will not [significantly] impact the visual character of the area. The area has experienced large amounts of mining and exploration activity in the past that has altered the natural visual resources. Reclamation of the areas disturbed by the proposed operation will beneficially affect the visual character of the area since reclamation will involve areas that are presently unreclaimed. (EIS at 102). We do not entirely credit this statement. The record reveals that, during its operation phase, the Landusky mine is gradually removing an entire mountain peak from the Little Rockies. Although, in the long run, reclamation may greatly reduce it, there is undeniably at present adverse visual impact. Similarly, we do not doubt that day-to-day operation of the Landusky mine imposes some audio impact on areas identified by Indians as religious sites. One such area is located only approximately 1 mile from the Landusky mine, on a direct sight line to it (BLM report entitled Sacred Sites in the Little Rocky Mountains, Exh. 1). Further, it is undisputed that these effects are disruptive to individual Indian religious practices.

However, BLM is not required by AIRFA to preclude other public land use simply because Indians may not be in agreement with that use. The Blackfeet Tribe, 103 IBLA 228 (1988). Recent case law in similar situations and the legislative history of AIRFA confirm that it was not intended to protect Indian religious activities to the exclusion of conflicting land-use considerations. In Wilson v. Block, 708 F.2d 735 (D.C. Cir.), cert. denied, 464 U.S. 956 (1983), the Hopi and Navajo Indian Tribes attempted to prevent development of a ski area on the San Francisco Peaks in the Coconino National Forest, Arizona. They alleged, as appellants do here, that such development would seriously impair the use of the peaks for their traditional religious practices. The D.C. Circuit Court of Appeals rejected this contention after reviewing the legislative history of AIRFA:

AIRFA requires federal agencies to consider, but not necessarily defer to, Indian religious values. It does not prohibit agencies from adopting all land uses that conflict with traditional Indian religious beliefs or practices. Instead, an agency undertaking a land use project will be in compliance with AIRFA if, in the decisionmaking process, it obtains and considers the views of Indian leaders, and if, in project implementation, it avoids unnecessary interference with Indian religious practices. [Italics supplied.]

Id. at 747.

The Supreme Court recently considered both the issue of the restrictions on land development imposed by AIRFA and the issue of protection of Indian religious practices under the Constitution. Lyng v.
Northwest Indian Cemetery Prot. Assn., 485 U.S. 439 (1988). The Forest Service (FS), U.S. Department of Agriculture, having studied the effects of the project (including effects on practice of Indian religion) in an EIS, and having imposed measures to limit these effects, decided to construct a paved road through Federal land within the Chimney Rock area of the Six Rivers National Forest and to harvest timber there. As in the instant case, this area had historically been used by certain American Indians for religious rituals that depend on privacy, silence, and the undisturbed natural setting. The Indians asserted the road would have adverse effects on Indian religious practices, and the Ninth Circuit had permanently enjoined FS from proceeding with these projects, citing the Free Exercise Clause of the First Amendment.23

The Supreme Court reversed. Quoting from Bowen v. Roy, 476 U.S. 693, 700 (1986), the Court ruled: "The Free Exercise Clause affords an individual protection from certain forms of governmental compulsion; it does not afford an individual a right to dictate the conduct of the Government's internal procedures." The Court found "no reason to doubt that the logging and road-building projects * * * could have devastating effects on traditional Indian religious practices * * * intimately and inextricably bound up with the unique features of the Chimney Rock area," and assumed "that the threat to the efficacy of at least some religious practices is extremely grave." But, even assuming that constructing the road would "virtually destroy the Indians' ability to practice their religion," the Court ruled that "the Constitution simply does not provide a principle that could justify upholding [the Indians'] legal claims. However much we might wish that it were otherwise, government simply could not operate if it were required to satisfy every citizen's religious needs and desires." Id. at 451-52. Noting that the Indians' need for privacy, intense meditation, and undisturbed naturalness during their religious practices "could easily require de facto beneficial ownership of some rather spacious tracts of public property," the Court concluded that "[w]hatever rights the Indians may have to the use of the area, however, those rights do not divest the Government of its right to use what is, after all, its land." Id. at 453 (italics in original).

As to AIRFA, the Court announced a ruling in accord with that of the D.C. Circuit in Wilson v. Block, supra. However, it stressed that "[t]he Government's right to the use of its own land * * * need not and should not discourage it from accommodating religious practices like those engaged in by the Indian respondents." It noted that FS had planned many other ameliorative measures to minimize the road's impact on the Indians' religious activities, such as choosing the route that best protects sites of specific rituals from adverse audible intrusions, and reducing the visual impact of the road on the

23 The Free Exercise Clause of the First Amendment provides that "Congress shall make no law * * * prohibiting the free exercise" of religion.
surrounding country.\textsuperscript{24} The Court concluded that providing such solicitude is adequate to meet the requirements of Section 2 of AIRFA. \textit{Lyng} at 454-55.

The Court was also clear to reject the Indians' argument that AIRFA itself prohibits the Federal Government from infringing their religious freedom by enacting their interpretation of the First Amendment into statutory law. According to the legislative history, it held, the purpose of AIRFA was simply to ensure that "the basic right of the Indian people to exercise their traditional religious practices is not infringed without a clear decision on the part of * * * the administrators that such religious practices must yield to some higher consideration." \textit{Id.} at 455 (quoting 124 Cong. Rec. 21444 (1978) (italics supplied). Thus, implicitly, if there is careful agency review leading to a clear decision that religious practice must yield, the requirements of AIRFA are met.

It cannot be doubted at this point, 10 years after initiation of the impacts now complained of, and nearly 100 years after the area was opened to mining,\textsuperscript{25} that the Department has made a clear decision that the specified individual Indian religious practices may not prevent mining, which is a legitimate use of Federal lands. Accordingly, we hold that AIRFA provides no legal basis to block mining at the Landusky mine.

Appellants have not suggested any means (other than banning mining entirely) by which visual and audio impacts of the operation on individual religious practices can realistically be ameliorated. Operations at the Landusky mine are not the first in the area and are certainly not alone in disturbing the individual meditation practiced by the Indians. Many other modern-day activities, including some reportedly practiced by the Indians themselves, are bound to do so.\textsuperscript{26} We perceive nothing further that BLM could have considered to ameliorate impacts on individual Indian religious practices.

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 as modified.

\textbf{DAVID L. HUGHES}  
\textit{Administrative Judge}

\textsuperscript{24} Specifically, FS selected a route that avoided archeological sites and was removed as far as possible from the sites used by contemporary Indians for specific spiritual practices. The timber harvest plan provided for one-half mile protective zones around all the religious sites that had been identified. \textit{Lyng} at 445.

\textsuperscript{25} Zortman states that the "land where the [Landusky] Mine is located and where facilities are to be developed under Permit Amendment No. 10 was sold by the Tribe to the United States Government in 1896. It was the U.S. Government's explicit intent at that time to facilitate mining in the Little Rockies. Whatever uses the south side of the mountains were being put to by Native Americans was changed then, not by the advent of the current [Landusky] mine." (Zortman Answer at 26).

\textsuperscript{26} Zortman states that appellants' "claims of harm to 'sacred' regions are inconsistent with what the Native Americans themselves have done to the region. Mission Peak, for example, may be called sacred by some but that did not prevent the Tribe from clear cutting a broad corridor through the trees to the Peak's apex to mark the Reservation boundary, nor did it inhibit timber sales and logging on the Peak's north flank." (Zortman Answer at 26).
I concur:

Franklin D. Arness
Administrative Judge