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1985

6-11-1985

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Citation Information

Kite, Marilyn S., "Readjustment of Federal Coal Leases" (1985). *Public Lands Mineral Leasing: Issues and Directions (Summer Conference, June 10-11)*.

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Marilyn S. Kite, *Readjustment of Federal Coal Leases*,
in PUBLIC LANDS MINERAL LEASING: ISSUES AND DIRECTIONS
(Natural Res. Law Ctr., Univ. of Colo. Sch. of Law
1985).

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READJUSTMENT OF FEDERAL COAL LEASES

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PUBLIC LANDS MINERAL LEASING:
ISSUES AND DIRECTIONS

A short course sponsored by the
Natural Resources Law Center
University of Colorado School of Law
June 10-11, 1985

PRINCIPAL AUTHORITIES:

Mineral Leasing Act, 30 U.S.C. § 181 et. seq.;

43 C.F.R. § 3451 et. seq.;

43 C.F.R. § 3485;

Rosebud Coal Sales Co. v. Andrus, 667 F.2d 949 (10th Cir. 1982).

FMC v. Watt, 587 F. Supp. 1545, (D.C. Wyo. 1984).

I. History of Coal Leasing

A. Mineral Leasing Act of

1920 - 41 Stat. 437;

30 U.S.C. 181 et seq.

1. The Act made leasing the exclusive means of developing coal from deposits owned by the United States.
2. The Act gave the Secretary of the Interior discretionary authority to issue leases, licenses and prospecting permits.
3. Leases issued by the Secretary of the Interior were for an indefinite term conditioned on diligent development and subject to reasonable readjustment every twenty years.

4. The Act authorized the Secretary to "waive, suspend or reduce" royalties if necessary to achieve maximum resource recovery. 30 U.S.C. § 209.

5. Royalties were established on a cents per ton basis with a five cent minimum, and royalties usually ranged from five to twenty cents per ton.

II. Readjustment and Lease Terms

- A. Indeterminant term leases provided for readjustment at the end of each twenty-year period succeeding the date of the lease. 30 U.S.C. § 207 (1970).

- B. Leases prepared by Interior provided that the Government had the right to "reasonably readjust" royalties and other lease terms at the end of each succeeding twenty year term.
- C. The leases were initially made subject to the Mineral Leasing Act as amended and any regulations effective at the date of issuance. Current leases are also subject to regulations "hereinafter adopted."
- D. Prior to 1976, Interior readjusted leases on a lease-by-lease basis, taking into consideration the particular circumstances of each lease.
- Department of the Interior New Release
(March 17, 1979).

III. Readjustment Procedures; 43 C.F.R. 3451.

- A. "Naked Notice." The BLM sends the lessee a brief notice that the lease will be readjusted at the end of the 20-year period. This notice is sent prior to expiration of the period, and failure to serve the initial notice waives the government's right to readjust. 43 C.F.R. 3451.1(c)(i).
- B. BLM must transmit to the lessee the proposed readjusted terms within two years of the initial notice or waive readjustment. 43 C.F.R. 3451.2; Kaiser Steel Corp., 76 I.B.L.A. 387 (1983).
- C. The lessee then generally has 60 days to file objections to the proposed terms with the BLM. (Note: 30 days to object is required in some leases).

D. BLM then has an indeterminate amount of time to respond. The lessee cannot appeal the readjustment until the BLM issues its final decision. California Portland Cement Co., 33 I.B.L.A. 223 (1977).

IV. Effect on Royalties During Readjustment

- A. The readjusted terms become effective 60 days after they are sent to the lessee by the BLM. 43 C.F.R. 3451.2(c).
- B. The effective date of the readjustment is not affected by any objections filed with the BLM.
- C. The readjusted terms and conditions are effective during appeal unless the authorized officer provides otherwise. 43 C.F.R. 3451.2(e).

D. Upon filing an appeal, however, the obligation to pay royalties and rentals is suspended pending outcome of the "appeal." However, royalties accrue and become payable with interest if the BLM decision is upheld. 43 C.F.R. 3451.2(e).

1. What is "appeal"? BLM maintains that "appeal" refers only to administrative appeal. Royalties are due after the I.B.L.A. decision even if the I.B.L.A. decision is appealed to Federal Court.
2. The Coastal States compromise - Bond posted in lieu of payment of accrued royalties during appeal to the District Court.

3. Payment of royalties if the BLM decision is reversed is not addressed in the regulations. Presumably, the old royalty rate should be paid because District Court reversal voids the attempted readjustment.

V. Procedural Issues During Readjustment:
Timeliness of the Notice

- A. The Mineral Leasing Act and the FCLAA require leases be readjusted "at the end of" the 20 year initial period. The leases also contain similar language. 30 U.S.C. § 207.
- B. The Regulations, however, only require that the "naked notice" be received by the lessee prior to "the end of" the initial period. Actual readjustment often occurs years after the end of the initial period. 43 C.F.R. 3451.1(c)(1).

- C. In Rosebud Coal Sales Co. v. Andrus, 667 F.2d 949 (10th cir. 1982) the Tenth Circuit held that the language "at the end of" should be given its plain meaning. The Court did not, however, explicitly decide whether "naked notice" of intent to readjust is sufficient, or whether actual readjustment must occur at the end of the initial period.
- D. As a result, Interior was unable to readjust many leases subject to readjustment at the time of Rosebud because of late notices. This has created a competitive disadvantage among producers.
- E. BLM has, on occasion, waived its right to readjust by failing to send notice of terms within two years.

F. Current dispute over interpretation of Rosebud: does actual readjustment have to occur prior to the end of the period or is mere notice enough?

FMC v. Watt

VI. The Federal Coal Leasing Amendments Act (FCLAA)

- A. In 1975 Congress enacted the FCLAA in response to widespread concern about the Federal Coal Program.
- B. FCLAA made a number of sweeping changes in the federal coal program, including new royalty rates, provisions for terminating non-producing leases and creating "Logical Mining Units" for consolidation of coal deposits under separate leases.

C. The most significant aspect of FCLAA impacting coal lease readjustment is § 7 of the Act, which provides that leases "shall" bear a 12½ percentum royalty, based on the fair market value of coal as determined by the Secretary. 30 U.S.C. § 207. Section 207 has also shortened the readjustment period from every twenty years to every ten years.

VII. Post FCLAA Readjustments: the Royalty Dispute

A. The Department of the Interior has taken the position that the 12½ percent royalty required by § 7 of FCLAA must, as a matter of law, be applied to all coal leases subject to readjustment. 43 C.F.R. § 3451.1.

- B. Interior now refuses to adjust royalties on a lease-by-lease basis. Instead, all leases are automatically readjusted to a 12½ percent royalty, regardless of the individual circumstances of the lease.
- C. The Coal Industry, however, believes the Secretary has misinterpreted the FCLAA and the Act does not mandate automatic imposition of a 12½ royalty on all pre-FCLAA leases subject to readjustment. Further, industry believes the lease contract establishes a commercial relationship under which the lease terms, e.g. reasonable readjustment, cannot be abrogated by regulations.

- D. The Coal Industry contends that pre-FCLAA leases should be readjusted according to the terms of the lease; i.e., in a "reasonable" manner.

VIII. Current Litigation

- A. The Secretary's decision to require 12½ percent minimum royalties on all readjustment leases was challenged by FMC Corporation in the Federal District Court for the District of Wyoming. FMC v. Watt, C.A. No. C83-0347.
- B. The District Court held in favor of FMC, and remanded to the Agency for a "reasonable" readjustment for FMC's royalty. The case is now on appeal to the tenth circuit. C.A. No. 84-2175, 84-2208.
- C. Lone Star Steel Company v. Clark, C.A. 84-173-C (D.C.E.D. Okl. 1984).

Lone Star has raised the timeliness issue, the commercial contract issue and the reasonable readjustment issue. Lone Star's leases were readjusted almost two years after the end of the initial lease period. Royalties were raised from fifteen cents/ton to 12½% of value. Lone Star is also arguing that the readjustment violates its contractual rights under its original leases.

- D. Gulf Oil Corporation and the Pittsburg & Midway Coal Mining Co. v. Clark, (D.C. New Mexico), Gulf and Pittsburg have raised the commercial contract issue, the timeliness issue and the reasonable readjustment issue.
- E. Coastal States Energy Company v. Watt, C.A. C83-0730J (D.C. C.D. Utah), Coastal States has raised the timeliness issue, the commercial

contract issue, the reasonable readjustment issue is challenging and other readjusted lease provisions including a monthly royalty payment, deletion of a provision providing credit for rentals against royalties and bonding requirements.

IX. Requests for Royalty Reduction

43 C.F.R. 3485.2(c); 30 U.S.C. § 209

- A. Under 30 U.S.C. § 209 the Secretary of the Interior has statutory authority to reduce royalty rates if necessary to achieve "maximum recovery" of the resource.

- B. BLM takes the position that coal companies can request reduction after the royalty is readjusted to 12½ percent and, at the same time, that appeal of readjustment may not be ripe because of availability of royalty reduction. Present BLM policy and proposed regulations prohibit consideration of royalty reduction until after readjustment. Interior Memorandum M-36920, December 11, 1979; Proposed Guidelines, 50 Federal Register No. 30, p. 6062 (February 13, 1985).
- C. Present BLM policy permits royalty reduction only for three years and only if there is a showing of substantial hardship, including operating losses, etc.

- D. Proposed Guidelines: New guidelines for royalty reductions have been proposed. See, 50 Fed. Reg. No. 30, p. 6062.
- E. The new Guidelines still require either 1) overall operating losses; or, if the lease is not yet developed, 2) verifiable information showing the mine will operate at a loss; or 3) that a lease is certain to be by-passed if royalty rates are not reduced.

X. Conclusions - Current Issues and Trends

- A. Imposition of 12½ percent royalty will encourage development of free coal rather than federal coal.
- B. Inadequacy of royalty reduction procedure to deal with maximum recovery of coal and high cost producers.

C. Pending Legislation - S.372 - Federal Coal Leasing Amendments Act of 1985 introduced by Senator Johnson. Provides 12½% royalty for readjustments accruing after effective date.