Of Teapot Dome, Wind River and Fort Chaffee: Federal Oil and Gas Resources

A Home Study Course For Continuing Professional Development

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Originally published in Natural Resources and Environment, ABA section of Natural Resources, Energy and Environmental Law, Volume 10, Number 10, Summer 1998.

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Foreword

The American Association of Professional Landmen (AAPL) is committed to serving the professional development needs of today’s land professional. The demands on the land professional’s time and financial resources continue to grow unabated. In a continuing effort to address these demands, the AAPL is proud to introduce its sixth home study course, Of Teapot Dome, Wind River and Fort Chaffee: Federal Oil and Gas Resources.

This home study course will benefit all land professionals by giving them an understanding of the evolution of federal oil & gas leasing legislation and regulation. In addition, Registered Land Professionals (RLPs) will earn four continuing education credits and Certified Professional Landmen (CPLs) will earn four recertification credits upon the successful completion of the requirements found in the back of this home study course within the allotted time frame.

Our thanks to Laura Lindley and the American Bar Association for allowing us to reprint this article from the NATIONAL RESOURCES & ENVIRONMENT, Summer 1995, at 1,21.

Robin A. Forte’, CPL
Director of Education
July 1998
Biography

Laura Lindley graduated from Louisiana State University in 1975, with a Bachelor of Science degree, majoring in Environmental Science. She obtained her Juris Doctorate from the University of Denver in 1980. While in law school, she became a member of the Order of St. Ives, a national legal honor society. Also while in law school, she worked as a law clerk for Poulson, Odell & Peterson. She joined the firm as an associate in 1980 and became a partner on 1985. Laura is very active in the Bar activities, having served as Chairman of the Mineral Law Section of the Colorado Bar in 1987-88 and is also very active in the Rocky Mountain Mineral Law Foundation. She has served as the Foundation’s Secretary, as a Trustee from 1989-1994, as Program Chairperson for the 41st Annual Institute and teaches at the biennial Federal Oil and Gas Leasing Short Course. Laura has worked in a variety of legal capacities in the area of oil and gas law, but her major specialty is public land law. Laura has authored articles on administrative appeals, on federal units and on wildlife impacts on oil and gas development for publications of the Rocky Mountain Mineral Law Foundation, an article for the ABA’s *Natural Resources & Environment* on the history of the Mineral Leasing Act and a chapter in the ABA’s soon to be published handbook on the National Environmental Policy Act. She is presently a partner in Bjork, Lindley, Danielson, and Baker in Denver.
Of Teapot Dome, Wind River and Fort Chaffee: Federal Oil and Gas Resources

I do not know, Mr. President, whether you have ever been in the section of California where oil in quantity was first discovered, but a coyote has to carry his rations with him if he expects to stay overnight anywhere upon the Mohave Desert and that section of California lying immediately to the east of it. These men, however, went there . . . and built roads, laid waterpipes, then sunk their shafts and discovered oil. What geologic bureau, what paid Government prospector—if such a thing can be imagined—what impulse or influence except the impulse or influence of gain . . . would ever have driven men into such inhospitable regions, impelled them to expend their money and their time, and incur all of the dangers which inhere in such climatic conditions, except that they knew and were told by the Government that their successful exploitation would be followed by a recognition of their locations?

—Statement of Senator Thomas of Colorado on the floor of the Senate, August 23, 1919

I do not like a leasing bill . . . When the vote is taken on a leasing bill I may hold my nose and vote for it.

—Statement of Senator Ashurst of Arizona on the floor of the Senate, August 23, 1919
As the quoted excerpts from the debates in Congress suggest, the move from a location system to a leasing system for the development of federally owned oil and gas (and certain other ‘fuel and fertilizer’ minerals) was a controversial and hard-fought step. And like most programs for commercial use of public lands, the oil and gas leasing system has been the target of criticism for fraud, both real and perceived, in its implementation of the system although the last major revision of the leasing system, in 1987, appears to have assuaged most critics for the time being.

A review of the decisions of the Department of the Interior (DOI) implementing the Mineral Leasing Act over the last seventy-five years (or a discussion with lawyers who have represented public lands oil and gas producers over the years) disclose that DOI’s role has evolved from one largely devoted to resolving disputes between competing applicants for a lease to one less concerned with the strictures of the Mineral Leasing Act than with the requirements of the National Environmental Policy Act. Nonetheless, like most chapters in the history of public land law, the history of the Mineral Leasing Act is a fascinating reflection of the politics of an era—politics which are surprisingly similar to those prevailing today.

The Temporary Petroleum Withdrawals

Like the earlier gold rush, the first intensive prospecting for oil on public lands occurred in California. The discovery of oil in the mid-1870s in Pico Canyon near Los Angeles prompted intensive oil exploration in southern California, all under the aegis of the placer mining law. Until 1896, the tacit position of DOI had been that oil deposits were locatable under the Mining Law of 1872. However, in *Union Oil Co.*, 23 L.D. 222 (1896), the Secretary of the Interior inexplicably ruled that petroleum was not locatable under the placer provisions of the Mining Law of 1872. However, in *Union Oil Co.*, 23 L.D. 222 (1896), the Secretary of the Interior inexplicably ruled that petroleum was not locatable under the placer mining laws, explaining that oil is classified by scientists as a mineral only “as a sort of distinction from a vegetable product.” *Id.* at 229. Although the *Union Oil* decision was reversed soon thereafter, 25 L.D. 351 (1897), in the meantime, Congress enacted the Oil Placer Act of 1897, which confirmed the applicability of the placer provisions of the Mining Law of 1872 to petroleum lands.

The location and discovery provisions of the Mining Law of 1872 were not well adapted for the physical realities of oil exploration. As discussed in the preceding essay by John Lacy, the prospector has no perfected right to his mining claim until the discovery of a valuable mineral. With petroleum, however, there was rarely any surface exposure of the mineral. Thus, the prospector bore the risk and expense of bringing drilling equipment onto the claim without knowing whether any mineral was present and with no right to the lands until a discovery was made. Of course, the presence of drilling equipment immediately tipped the prospector’s hand so that he was promptly
surrounded by competing claimants. If the prospector did make a discovery of oil, the rush by these surrounding claimants to perfect their own claims by drilling led to wasteful overproduction as each claimant sought to protect his claim from drainage.

Under the Mining Law of 1872, no royalty was paid on the oil extracted, and the federal government exercised no control over the disposition of petroleum lands to prospectors, which resulted in large areas of petroleum lands in California being appropriated by miners. This event alone might not have led to the development of a leasing system for oil and gas, but its occurrence simultaneously with two other historic developments — the conversion of the Navy from coal to oil for fuel and the emergence of the conservation movement—compelled the adoption of a different system. But first, there was a constitutional challenge to the executive’s authority over the public lands, followed by a decade of sparring in Congress over the appropriate manner for development of federally owned oil resources.

From today’s perspective, the idea that the United States would control the disposition of its natural resources is a given. Yet, at the turn of the century, the conservation concept was considered radical, particularly by congressional delegates from the western states. For example, the withdrawal of lands for forest reserves by President Theodore Roosevelt (at the urging of conservationist and first Forest Service Chief Gifford Pinchot) prompted an amendment to the Appropriations Act for the Forest Service in 1907 prohibiting forest withdrawals in six western states. In anticipation of this move by the western congressmen, Pinchot worked feverishly to prepare proclamations for President Roosevelt’s signature for significant additional forest withdrawals in the six affected states. These proclamations were signed on March 1 and 2, 1907, and President Roosevelt signed the Appropriations Act on March 3, 1907. Although the forest reserves were not withdrawn from entry under the mining law, withdrawals of large amounts of petroleum lands from the operation of the mining law soon followed. Curtis Lindley, the influential author of the mining law treatise, described the conservation movement (as “urged and formulated by President Roosevelt and members of his official family”) as follows:

[N]ational conservation, as we understand it, is a policy of primarily placing the remnant of the public domain other than that portion of it which is essentially agricultural in character, in a state of reservation and subsequently dealing with it or its natural resources in such a manner as will economically yield the best results to all the people. Its principal aim is to obtain a maximum economic production at a minimum of waste; to prevent individuals or aggregations of individuals from securing monopolies; and to exact some equivalent for the privileges granted.
Official concern regarding conservation of oil came to a head on September 17, 1909, when the director of the Geological Survey reported to the Secretary of the Interior that oil lands were passing into private ownership so rapidly that it would “be impossible for the people of the United States to continue ownership of oil lands for more than a few months. After that the Government will be obliged to repurchase the very oil that it has practically given away” . . . See, United States v. Midwest Oil Co., 236 U.S. 459, 466-67 (1915). Largely because of the Navy’s increasing use of oil, President Taft responded quickly to this report by issuing a proclamation, Temporary Petroleum Withdrawal No. 5, on September 27, 1909. This proclamation withdrew over 3 million acres of land in California and Wyoming from any form of settlement or entry for the stated purpose of allowing consideration of “proposed legislation affecting the use and disposition of the petroleum deposits on the public domain.” The President’s authority to make such a withdrawal was hotly disputed at the time. Lindley explained the position, which was held by many miners and many in Congress:

[W]e think it will be readily recognized that the power of withdrawal is not an arbitrary one; that in its exercise the executive cannot impinge upon the powers of congress to regulate and control the disposition of the public lands or establish a definite policy regarding such disposition in advance of some declaration by the legislative branch of the government.

A small group of men in official life, considering that our public land laws as they exist in the statute books were unwise, unsuited to our industrial and economic conditions and should therefore be modified or repealed, may properly recommend to the law-making body modifications in or changes of the system. But this does not establish a public policy, nor authorize the executive to withdraw any part of the public domain from mineral location to await the action of congress on their proposals. Such withdrawal is practically the nullification or absolute suspension of the operation of laws over withdrawn areas, to abide an event which may never happen.

President Taft himself was uncertain about the authority for the petroleum withdrawal and asked Congress for specific authorization. Congress responded with the Pickett Act, signed on June 25, 1910, which authorized the President to withdraw lands from the operation of the public land laws for waterpower sites, irrigation, classification of lands or for “other public purposes” to be specified in the withdrawal order. The Pickett Act, however, did not validate any previous withdrawals and it was not until the Supreme Court’s decision in 1915 that the validity of Temporary Petroleum Withdrawal No. 5 was confirmed, United States v. Midwest Oil Co., 236 U.S. 459 (1915), although the President had ratified the withdrawal under
Following enactment of the Pickett Act, the President withdrew much of the public domain from entry and from location under the mining law for nonmetaliferous minerals. Moreover, several reserves were specifically set aside to conserve oil for naval purposes: Naval Petroleum Reserve No.1 (Elk Hills) and Naval Petroleum Reserve No. 2 (Buena Vista Hills) in California were withdrawn in 1912; Naval Petroleum Reserve No. 3 (the infamous Teapot Dome in Wyoming) was withdrawn in 1915; and Naval Petroleum Reserve No. 4 in Alaska was withdrawn in 1923. In addition, the Naval Oil Shale Reserves in Colorado and Utah were set aside in 1916. When the Mineral Leasing Act was finally adopted in 1920, it specifically excluded from its effect all lands withdrawn for military or naval uses.

It seems curious that President Taft went out on a constitutional limb to make the temporary petroleum withdrawals “in aid of legislation” in 1909, that Congress responded with authorizing withdrawal legislation in 1910, but that mineral leasing legislation was not enacted until 1920. The reason for this delay appears to have been the issue of what to do about prospectors who made investments in withdrawn petroleum lands either in defiance of the withdrawal orders or in the good-faith belief that the withdrawals were unconstitutional. For example, the eminent Oscar Sutro of San Francisco’s Pillsbury, Madison & Sutro, who appeared as counsel for amicus in Midwest Oil, is reported to have advised his clients (among them Standard Oil of California) that the withdrawals were invalid as beyond the authority of the President. The debates in Congress in 1919 contain several references to the almost unanimous view of “some of the best mining lawyers in the United States” that the petroleum withdrawals (prior to the Pickett Act) were unlawful and that prospectors spent time and money developing such withdrawn lands in good-faith reliance on that legal advice.

Another reason for the delay was a philosophical difference (largely along eastern and western lines) about returning the oil lands to the states versus leasing or, if a leasing system was to be adopted, how royalties would be shared with the states. The congressional delegations from the public lands states felt they were being treated unfairly by the eastern states, where the lands were almost all privately owned and thus a part of the tax base. Sen. Charles S. Thomas of Colorado viewed the change from the mining law appropriation system to a leasing system as paternalistic on the part of the federal government and, during one particularly lengthy statement on the Senate floor, exclaimed,

I am not in favor of this bill . . . I do not like to think of Uncle Sam as a great big landlord, an absentee landlord at that, doling out leasehold interests to his children, collecting rent from them and providing for its collection by the appointment of another multitude of officeholders to examine their books, to keep tab upon their activities, to watch their bank
accounts, and to invoke the law or the regulations against them whenever any one of such officeholders shall come to the conclusion that the terms and conditions of the lease are not being strictly observed.


Sen. Thomas was not the only one concerned about the development of a bureaucracy to implement a mineral leasing law. Sen. Albert B. Fall of New Mexico complained that it was not so much the payment of royalty to the United States to which he objected as it is the reservation under bureaucratic administration that we object to[]. As must necessarily be the case so long as there is discretion left in the handling of these resources to the Department of the Interior here in Washington, without respect to who may be the Secretary of the Interior at the time, it is worth almost as much as a man’s life is worth to attempt to deal with the department or to develop those resources.

58 CONG. REC. 4257 (daily ed. Aug. 23, 1919). Of course, when Senator Fall himself became Secretary of the Interior under President Warren G. Harding a year later, he bent over backward so that oilmen E.L. Doheny and Harry Sinclair would not have to surmount any bureaucratic hurdles to lease the naval petroleum reserves at Elk Hills and Teapot Dome. See Pan American Co. v. United States, 273 U.S. 456 (1927); Mammoth Oil Co. v. United States, 275 U.S. 12 (1927).

The perorations on the Senate floor in 1919 concerning conservationists could very easily be confused with present-day remarks in Congress in the context of the Endangered Species Act. Senator Thomas went on at length about the evils of conservation, which he and others viewed as an effort by eastern interests to hamper business and commerce in the west for their own self-interest. The following excerpt from Senator Thomas’ remarks is illustrative:

Conservation and reservation are synonymous terms evidently in the minds of the average eastern conservationist . . . I am confident that if the modern policy of conservation had been inaugurated in the early seventies, or immediately after the war, its paralyzing and depressing and retrogressive effects upon the great West would have made it extremely difficult for America either to be able to protect herself or to have rendered such efficient aid in the Great War of the World, because it is not the Geological Bureau of Washington . . . which should be credited with the discovery of the enormous deposits of minerals of all kinds, but the individual who, armed with a hope of profit and sustained by the statutory promise of his Government, risks all his money, his life,
his family, his health, everything in those inhospitable wilds of nature where all her great mineral resources are for the most part deposited.


However, by late 1919, even the western senators seemed resigned to a leasing system for oil and gas (and certain other ‘fuel and fertilizer’ minerals). The Smoot Bill, named for the senator from Utah who chaired the Senate Committee on Public Lands, provided the outline for what became the Mineral Leasing Act of 1920. The debate focused on issues that today seem of only minor importance: attacks by Senator LaFollette of Wisconsin on the Standard Oil Company; whether aliens would be permitted to own interests in federal leases; distribution of the revenues; and the extent of relief provisions for prospectors who entered after the 1909 temporary petroleum withdrawal.

*The Mineral Leasing Act of 1920*

The leasing system as ultimately adopted in the 1920 Act distinguished between known petroleum lands and ‘wildcat’ lands. In “known geologic structures,” leases were to be issued competitively for a fixed term of twenty years with the right to renew and a maximum size of 640 acres. On wildcat lands, a permit system was established. A prospector could obtain a two-year prospecting permit covering no more than 2,560 acres. If a discovery of a valuable deposit of oil or gas was made during the term of the permit, the permittee was entitled to a lease (known as the “A” lease) on up to one-fourth of the permit area, and a preference right for a lease (known as the “B” lease) for the balance of the lands. The prospector was rewarded for his efforts with only a 5 percent royalty obligation on the “A” lease, while the “B” lease was subject to a step-scale royalty ranging between 121/2 percent and 331/2 percent, depending on the volume of production. Both the “A” and “B” leases were for fixed twenty-year terms, but with the right to renew for additional ten-year terms. Revenues from the leasing system were to be allocated as follows: 521/2 percent to the Reclamation Fund, 371/2 percent to the state in which the lands are located, and 10 percent to the federal treasury. The allocation has since been amended and revenues are now distributed (in the lower forty-eight states) 50 percent to the states, 40 percent to the Reclamation Fund, and 10 percent to the U.S. Treasury. 30 U.S.C. § 191.
“Teapot Dome” is a shorthand reference, much like “Watergate” or “Whitewater,” to the secretive events surrounding the leasing of the naval petroleum reserves at Elk Hills and Teapot Dome by then Secretary of the Interior Albert B. Fall. As mentioned, lands withdrawn for naval purposes were not available for lease under the Mineral Leasing Act of 1920, and the naval petroleum reserves were under the jurisdiction of the Secretary of the Navy. Not long after the Harding administration took office, however, Secretary Fall arranged for an executive order transferring jurisdiction over the naval petroleum reserves from the Secretary of the Navy to the Secretary of the Interior. The reason Edwin Denby, then Secretary of the Navy, agreed to this transfer is unclear, but one historian has described Denby as “too stupid to realize his own stupidity.” F. RUSSELL, THE SHADOW OF BLOOMING GROVE (McGrawHill 1968). To be fair, there was some legitimate concern, particularly with respect to the naval petroleum reserves in California where there was much privately owned land within the reserves, that production from those lands was draining the Navy’s oil. On April 7, 1922, Secretary Fall secretly leased the entire Teapot Dome reserve (so-called because of a teapot-shaped rock formation adjacent to the Salt Creek oil field near Casper, Wyoming) to Harry Sinclair’s Mammoth Oil Company. The lease provided for payment of royalties and the construction of oil storage facilities at various ports as directed by the Navy. Shortly thereafter, Fall granted leases covering the Elk Hills reserve to E.L. Doheny’s Pan American Petroleum Company, upon similar terms. Although the reserves were known to contain oil, there was no competitive bidding for the leases and their issuance was cloaked in secrecy. Nonetheless, word of the leases soon got out and the Senate ordered an investigation. It was not until after Fall had left office and President Harding had died, however, that the damning details became public.

Unlike the Mining Law of 1872, the Mineral Leasing Act of 1920 has been amended a number of times, although it was not until 1987 that the basic structure of the 1920 Act was significantly altered. The Act of August 21, 1935, abolished the permit system for oil and gas, but retained the distinction between lands within a known geologic structure (KGS), which are to be leased by competitive bid, and lands outside a KGS, which are to be leased noncompetitively to the “first qualified applicant.” As will be discussed later, determining the identity of the first qualified applicant and defining the boundaries of a KGS proved to be difficult for DOI. The Act of August 21, 1935, also eliminated the fixed twenty-year term lease in favor of a lease for a fixed primary term and secondary term for so long as a well capable of producing oil or gas in paying quantities was located on the leasehold.

By the Act of July 29, 1954, federal oil and gas leases became subject to automatic termination for nonpayment of rental, as was generally the case for fee leases. Prior to that, late-paid rental was a debt due the United States but did not result in termination of the lease. As pointed out at the time by the solicitor of the Department of the Interior, this amendment “eliminate[s] the distasteful practice theretofore required of collecting rentals which the lessee failed to pay because he assumed that he surrendered his lease by failing to pay rental.” J.R. Armstrong, Leases and Leasing Practices, 1 ROCKY MTN. MIN. L. INST. 45, 50 (1955). Over the years, the acreage limitation for federal leases was increased a number of times, from a limit of three leases per state (one in any KGS) in 1920 to 246,080 acres under lease or option per state (or 300,000 acres per leasing district in Alaska) in 1960.
Teapot Dome and a Scandal
Continued from previous page

It seems that Fall, who had never been particularly prosperous, was suddenly making substantial improvements to his ranch in New Mexico. He paid eight years’ back taxes on the ranch, built an irrigation system and a small hydroelectric plant, and purchased an adjacent ranch. When Senator Walsh of Montana, who headed the Senate’s investigation, became suspicious of Fall’s newfound prosperity, Fall at first arranged for a wealthy acquaintance, Edward B. McLean, to state that he had loaned Fall $100,000. McLean recanted that story upon questioning by Walsh, and it was eventually disclosed by E.L. Doheny that he had sent his son to deliver $100,000 in cash to Fall, carried in a little black bag. Doheny, who had once prospected with Fall before Doheny made his fortune in oil in California and Mexico, characterized the loan as a modest favor for an old friend and as totally unrelated to the Elk Hills leases. Whether or not that was true, the image of Doheny’s son delivering a satchel full of money to the Secretary of the Interior produced an explosive scandal. Even more sinister, Senator Walsh’s investigation disclosed that Fall’s son-in-law had received from Harry Sinclair, the beneficiary of the Teapot Dome lease, more than $300,000 worth of bonds. The leases to Doheny and Sinclair were eventually canceled as improperly obtained and Albert Fall was convicted of accepting a bribe. To his death, Fall claimed that the payments from Doheny and Sinclair were not bribes and that he leased the naval reserves on the best terms possible for the benefit of the Navy.

Management Act of 1982

Despite numerous amendments over the years, the Mineral Leasing Act’s provisions on royalty have remained brief and unchanged: the lessee is to pay the United States “not less than 12.5 percent in amount or value” of production. Until 1981, this royalty was collected by the Conservation Division of the U.S. Geological Survey (USGS). Revenues from most Indian leases were also paid to the tribe or allottee through the USGS. Periodically, the General Accounting Office (GAO) or a congressional oversight committee would issue a report or hold hearings critical of the government’s royalty accounting system. This criticism escalated in the 1970s as the value of oil and gas rose sharply and, in particular, as allegations of theft of oil from Indian leases on the Wind River Reservation in Wyoming were leveled. A House report issued on September 23, 1982, described the problems with the federal oil and gas royalty system as follows:

1. Royalty accounting procedures have been inadequate to cope with the rapidly expanding volume and complexity of the accounting system; (2) the absence of security in the field has been an open invitation to theft; and (3) the experience and willingness of the States and Indian tribes to assist in the management of the system have not been properly utilized. Until very recently, there has been no capability in the Federal Government to verify production data or sales data with respect to oil produced from a Federal lease allowing industry to operate essentially on an honor system.


In response to these criticisms, on July 8, 1981, Secretary of the Interior James Watt appointed a blue-ribbon panel to study DOI’s royalty and production accounting systems. This Commission on Fiscal Accountability of the Nation’s Energy Resources issued its report in January 1982. The report, commonly called the Linowes Report after the commission’s chair, University...
David F. Linowes, was critical of several aspects of the government’s supervision of production accounting and of royalty payments from federal and Indian leases, and made sixty recommendations for legislative and regulatory changes.

In hopes of preempting some of the criticism he expected to receive upon release of the Linowes Report, Secretary Watt ordered a reorganization of DOI’s royalty accounting program. Secretarial Order No. 3071, issued on January 19, 1982, two days prior to the release of the Linowes Report, abolished the Conservation Division of the USGS and established a new Minerals Management Service (MMS) to which the Conservation Division’s functions were transferred. Order No. 3071 also established a temporary Minerals Management Board comprised of the under secretary of DOI and the assistant secretaries for energy and minerals and for policy, budget and administration, whose job was to supervise the MMS and to “develop appropriate policy and guidelines to implement the approved recommendations and findings” of the Linowes Commission.

By Order No. 3087 dated December 3, 1982, Secretary Watt modified the MMS’ role by transferring all onshore minerals management functions other than royalty administration to the Bureau of Land Management (BLM). MMS is thus responsible for all onshore, offshore and Indian royalty collection, as well as administration of the offshore leasing system, while BLM handles onshore lease issuance and approval and supervision of operations on federal and Indian lands.

Meanwhile, DOI, working with the staff of Sen. James McClure (R.-Idaho), drafted the Federal Energy and Mineral Resources Act of 1982 implementing the Linowes Commission’s recommendations. This proposed bill was transmitted by Secretary Watt to the President on March 24, 1982, just over two months after release of the Linowes Commission report. Such swift bureaucratic action is evidence of the administration’s belief that remedial legislation was necessary to stanch the criticism. Senator McClure introduced the bill as S.2305; a similar but not identical bill introduced in the House, H.R. 5121, was the version ultimately enacted as the Federal Oil and Gas Royalty Management Act of 1982 (FOGRMA), which was signed into law on January 12, 1983. Pub. L. No. 97-451, 96 Stat. 2447 (codified at 30 U.S.C. §§ 1701-1757).

FOGRMA addresses site security, production accounting, recordkeeping, and audit and enforcement responsibilities. Interestingly, it contains no provisions addressing product valuation, so FOGRMA does not alter the basic royalty provision of the Mineral Leasing Act calling for payment of not less than 12.5 percent in amount or value of production. However, the creation of the MMS, as a response to the same issues that prompted the enactment of FOGRMA, resulted in vastly expanded regulations on product valuation. The USGS Conservation Division collected royalties for over sixty
years based on only sketchy regulatory guidelines. It should be remembered, however, that, unlike the MMS, royalty collection was not the only function of the USGS Conservation Division, which also approved drilling permits and unit agreements and supervised operations on federal and Indian leases. Moreover, the value of federal and Indian royalties increased exponentially in the late 1970s and early 1980s. The fact that federal oil and gas revenues had become such a significant contributor to the Treasury, coupled with concerns over lax accounting, prompted Congress to fund the MMS at a level far in excess of anything the USGS had ever seen. The MMS, unlike the USGS, quickly built a large staff of skilled accountants and economists, many attracted from other agencies (including BLM) by the higher civil service ratings for MMS positions. In addition, the MMS received funding to develop a sophisticated computer system for tracking production and royalty payment reports. While the MMS has undoubtedly improved the accuracy of federal and Indian royalty collections, the burden on the royalty payors has been significant: the regulations of the USGS dealing with onshore oil and gas royalty valuation and payment filled five pages in the Code of Federal Regulations; the MMS regulations fill eighty-four pages.

The “Simo” or “Lottery” Leasing System

Just as with the Mining Law of 1872, much of the administration of the Mineral Leasing Act of 1920 involved determining priorities among competing applicants for an oil and gas lease on the same lands. At first, it was simply a matter of “first in time, first in right,” and, assuming the applicant was qualified (a U.S. citizen or a U.S. corporation not in violation of the acreage limitations and otherwise in compliance with the statute and regulations), a lease was issued to whomever was first in line to file an application in the land office.

The post-World War II oil boom swamped BLM with lease applications. During the war, applications averaged about 4,000 per year; in fiscal year 1952, approximately 32,000 lease applications were filed with BLM. Some of this rush was fueled by promoters who advertised the riches to be made from federal oil and gas leases (flush oil production was discovered in the Williston Basin of North Dakota and Montana about this time) and who, for a fee, assisted speculators in filing applications for forty-acre tracts. BLM tried to limit the filing of speculative offers by requiring that every offer describe an area of at least 640 acres. That regulation merely shifted the activity to the “forty-acre merchants,” who obtained leases in rank wildcat areas and then assigned forty-acre portions of each lease to gullible purchasers.

As lands under lease become available again as a result of the cancellation or relinquishment of the prior lease, BLM’s “notation rule,” which originated in the context of the homestead laws, prohibits filing a new application until the fact of termination of the prior lease was noted on the tract book. This rule resulted in all kinds of mischief in areas where leases might have great speculative value even though the lands were not within a
KGS. Tract books were damaged in tugs-of-war between the “watch-dogs of the tract books,” Malone, *Oil and Gas Leases on United States Govt Lands*, 2 INST. ON OIL & GAS L. & TAXATION 309 (1951), fisticuffs were not uncommon, and there were even rumors that certain land office employees could be bribed to tell a lease broker when a particular tract would be noted as available in the tract book. DOI spent much time and many resources adjudicating disputes between competing applicants, such as one by a second-priority applicant who “emphasized the fact that he did not engage in a foot race or a push and tumble act with [the other applicant] in the manner of the early Oklahoma land rushes and apparently felt that he should be rewarded for his gentlemanly conduct with a chance at the lease,” George R. Wickham, A-27892, GFS (O&G) SO-1959-49. To remedy this situation, BLM amended its regulations on December 8, 1959, to require that the description of lands in each lease expiring that month be posted in the land office and all offers for such lands received during a specified five-day period would be deemed to have been simultaneously filed, with a public drawing to determine priorities. Lands not leased under the simultaneous filing system were available for lease “over-the-counter” under the old first-in-time regime. In upholding the regulations that established the simultaneous filing system, Judge Skelly Wright observed:

The history of the administration of the statute furnishes compelling proof, familiar to the membership of Congress, that the human animal has not changed, that when you determine to give something away, you are going to draw a crowd. It is the Secretary’s job to manage the crowd while complying with the requirement of the Act.


The simultaneous filing system, or “simo” or “lottery” as it was popularly known, was premised on the theory that each applicant should have an equal opportunity for success in a particular drawing. Thus, the regulations prohibited any applicant from having an interest in more than one “simo” application for the same tract. Of course, some applicants were unable to resist the temptation to increase their odds of obtaining a choice lease and devised various schemes to evade the “sole party in interest” regulation. Moreover, the lottery attracted many sharp operators who saw it as an opportunity for profit by providing various filing services to persons unfamiliar with the regulations. These filing services often promised extravagant returns for the “investments” of their clients, producing frequent complaints to various state attorneys general. BLM repeatedly amended its regulations in an effort to halt some of the undesirable practices, but invariably the fast buck artists devised new schemes to evade the regulations. These recurrent scandals prompted periodic calls to abolish the simo system.
The Fort Chaffee Scandal

At the same time that the simo system was drawing criticism, DOI took a beating for its perceived inability to designate a KGS. The concept of the KGS as the determinant for competitive leasing was in the Mineral Leasing Act from the very beginning. However, Congress never supplied a definition for a "known geologic structure." DOI defined a KGS as:

[Technically the trap in which an accumulation of oil or gas has been discovered by drilling and determined to be productive, the limits of which include all acreage that is presumptively productive.

43 C.F.R. § 3100.0-5(1)(1983). Whether this was a wise definition is a moot point. BLM’s application of the definition to lands in Fort Chaffee, Arkansas, led to a scandal that changed the definition and, ultimately, the statute.

The tale of Fort Chaffee is a complicated one. Fort Chaffee is a large military reservation lying within the Arkoma Basin of Arkansas, a prolific natural gas-producing area. The lands owned by the United States in Fort Chaffee are acquired lands; that is, lands that had been patented out of the public domain and later reacquired by the United States. Acquired lands are leasable only under the 1947 Acquired Lands Leasing Act; however, that statute incorporates by reference the leasing procedure established by the 1920 Mineral Leasing Act. Originally, lands acquired by the United States for military or naval purposes were excluded from leasing; however, as a part of the Federal Coal Leasing Amendments Act of 1975, the prohibition on leasing acquired military lands was repealed.

In May 1977, Texas Oil & Gas Corp. (TXO) filed over-the-counter noncompetitive lease applications covering 78,000 acres on Fort Chaffee. At that time, BLM had not yet amended its regulations to conform with the 1975 amendment to the 1947 Acquired Lands Leasing Act. Thus, the regulations still prohibited the leasing of acquired military lands. At first, DOI took the position that acquired military lands were not available for lease until after BLM had promulgated conforming regulations. However, BLM later changed its view, and issued leases covering approximately 33,000 acres to TXO, effective July 1, 1979. The balance of TXO’s noncompetitive lease offers were rejected as covering lands within a KGS.

TXO was not the only company interested in leasing Fort Chaffee. Arkla Exploration Company (Arkla), the exploration subsidiary of a powerful Arkansas-based natural gas company, was anxious to increase its gas reserves. Recall that these applications were filed in the late 1970s, after the 1973 oil embargo and after the passage of the Natural Gas Policy Act of 1978, which authorized high incentive prices for new sources of natural gas. Arkla filed a protest to the issuance of the leases to TXO and, in addition, strong congressional pressure was brought to bear on DOI. Senator Dale
Bumpers (D-Ark.), long a critic of the federal noncompetitive leasing system, fired off a series of letters in August 1979 to Secretary of the Interior Cecil Andrus challenging the validity of the TXO leases, not only because of the question regarding whether the lands were open to lease at the time TXO filed its offers, but also because, in his view, the lands should not have been leased noncompetitively. Sen. Bumpers also requested that the Secretary of the Interior declare a moratorium on the issuance of any noncompetitive leases nationwide. Hearings on the noncompetitive leasing system in general and the Fort Chaffee leases in particular were held by the Senate Subcommittee on Energy Resources in September 1979. Shortly after those hearings, Arkla filed a protest to the lease issuance with DOI and filed suit in federal court in the District of Columbia, challenging the TXO leases. Arkla (whose chief executive officer Thomas "Mac" McLarty later served for a time as President Clinton's chief of staff) was represented by Jim Guy Tucker of Little Rock, now governor of Arkansas.

Not to be outdone in the congressional pressure department, TXO sought assistance from members of the Texas delegation. Reps. Jim Wright and Martin Frost and Sen. Lloyd Bentsen wrote to Secretary Andrus in September 1979, describing a dispute between Arkla and TXO over an application by TXO to build a pipeline in Arkansas. Arkla retaliated with letters to Secretary Andrus from influential members of the Louisiana delegation (Senators Russell Long and J. Bennett Johnston).

On the evening of November 1, 1979, the night before a hearing in the District of Columbia federal court on a temporary restraining order sought by TXO, Secretary Andrus ordered the TXO leases rescinded because the offers were filed prior to the effective date of the regulation implementing the 1975 amendment to the statute. By order dated February 29, 1980, Secretary Andrus suspended the issuance of all noncompetitive oil and gas leases, not just those covering acquired military lands.

The litigation in the District of Columbia focused on the validity of TXO’s lease offers because they were filed after the amendment of the statute opening acquired military lands to leasing but prior to the conforming amendment of the regulation. Reversing the district court, the Court of Appeals for the District of Columbia Circuit ruled that the leases were properly issued to TXO because the statute (meaning the Federal Coal Leasing Amendments Act of 1975) opened the lands to leasing and an implementing regulation was thus unnecessary. *Texas Oil and Gas Corp. v. Watt*, 683 F.2d 427 (D.C. Cir. 1982).

The issue of whether the Fort Chaffee lands should have been classified KGS was never raised in the District of Columbia litigation. Rather, Arkla returned home to raise its KGS challenge to TXO’s leases in the federal court for the Western District of Arkansas. The State of Arkansas intervened in that action, and the court found that Arkansas had standing because it
receives 50 percent of the revenues from federal leases within its borders.

Both the district court and the Court of Appeals for the Eighth Circuit held that the KGS classification procedure used by the USGS for the Fort Chaffee lands was arbitrary and capricious. *Arkla Exploration Co. v. Watt*, 562 F. Supp. 1214 (W.D. Ark. 1983), *aff’d sub nom, Arkla Exploration Co. v. Texas Oil & Gas Corp.*, 734 F.2d 347 (8th Cir. 1984). It appears that the USGS used a strict “step-out” method to determine whether any of the Fort Chaffee lands were within a KGS, notwithstanding the fact that the Fort Chaffee lands had not been available for lease and “three out of every four drilled sections north and south and two out of every three drilled sections east and west” of the Fort Chaffee lands were “in commercial production.” 562 F. Supp. at 1219. Under the step-out method, which the court found was used by the USGS to clearlist the Fort Chaffee lands, only lands within one section (one mile) of a producing well were deemed to be within a KGS. The effect was thus to create a “doughnut” of KGS lands around the perimeter of Fort Chaffee, with the unexplored center remaining non-KGS lands available for noncompetitive leasing.

In the course of upholding the cancellation of TXO’s leases, the Eighth Circuit stated that Congress intended that a KGS mean “domes and anticlines which contained producing wells,” 734 F.2d at 359, and that the KGS classification must consider the presence of “competitive interest,” 734 F.2d at 360. While the decisions of the U.S. District Court and the Eighth Circuit may be criticized as going beyond the permissible bounds of judicial review of agency action under the Administrative Procedure Act, the *Arkla* decision had the immediate effect of throwing the DOI’s KGS clearlisting process into disarray. BLM (who, by now, had succeeded to the USGS, as the agency responsible for KGS determinations) soon issued several KGS determinations that covered much larger areas than had typically been the case prior to *Arkla*. Challenges to these KGS determinations by disappointed noncompetitive applicants were unsuccessful. See, e.g., B.K Killion, 90 IBLA 378 (1986).

As mentioned above, Secretary Andrus ordered a moratorium on issuing noncompetitive leases in 1980. That moratorium was lifted in 1981 but soon thereafter another KGS scandal erupted. In 1983, fourteen noncompetitive leases were issued for lands in the Amos Draw area of the Powder River Basin in north central Wyoming. Although there were designated KGS lands in the vicinity, the lands in these fourteen leases were clearlisted as not within a KGS. On November 23, 1983, BLM determined that the existing discrete KGS lands in the area actually all overlay a common reservoir, and expanded and consolidated those KGS lands to cover close to 30,000 acres. Had that consolidation been made a few months earlier, the fourteen noncompetitive leases could not have been issued. Rumors, widely reported in the press and in the promotional literature of various filing services, circulated that those fourteen leases were immediately assigned by
the winning applicants to oil companies for millions of dollars. Indeed, of the four winning applicants who were willing to disclose the sale price of their leases to the U.S. General Accounting Office, one reported the lease sold for $7.7 million and one for $5.7 million. The idea that those princely sums could have gone to the U.S. Treasury and to the states only fueled the movement for revision of the noncompetitive leasing system.

The Oil and Gas Leasing Reform Act of 1987

Senator Bumpers led the effort to adopt a competitive oil and gas leasing system after the Fort Chaffee debacle. He introduced legislation in each Congress beginning with the 97th Congress (1981). Senator Bumpers’ legislation was strongly opposed by independent oil and gas producers who felt that, without noncompetitive leasing, the major integrated oil companies would control all of the prospective federal acreage. This opposition kept the bill from moving until the 99th Congress. In the second session of the 99th Congress, Senator Bumpers modified his bill so that lands that did not receive a minimum bid of $35 per acre would become available for noncompetitive leasing for a one-year period. This nod to the independent producers by preserving some lands for noncompetitive lease blunted the industry’s criticism of the Bumpers bill.

While the difficulties with KGS classifications and abuses in the simo system were the primary triggers for legislation amending the Mineral Leasing Act of 1920, there was also concern in some quarters regarding the environmental effects of oil and gas exploration and production on the federal lands. Congressman Seiberling (D-Ohio) vigorously supported a zoning approach to determine which federal lands would be made available for oil and gas leasing, much like the suitability determination required for coal leasing under the Federal Coal Leasing Amendments Act of 1975, H.R. 4741, 99th Cong., 2d Sess. (1986). In addition to Seiberling’s bill, Representatives George Miller (D-Cal.) and Morris Udall (D-Ariz.) introduced bills in the 99th Congress containing land use planning provisions. As the industry began to accept the idea of revisions to the noncompetitive leasing system, concerns grew that any amendment to the Mineral Leasing Act would open up the statute to other amendments that would significantly reduce the amount of federal lands available for oil and gas leasing.

By late 1986, it became clear that Senator Bumpers’ bill had gained enough momentum that the western states senators could no longer block it. The Bumpers bill passed the Senate on October 17, 1986, but without the environmental provisions sought by the House. Thus, the 99th Congress adjourned without a leasing reform act.

Hearings on the leasing reform bills in the 100th Congress disclosed that oil and gas producers had become frustrated with BLM’s administration of the leasing system, with delays in making KGS determinations, and with
the designation of KGS lands which were much larger than in the past resulting in a *de facto* competitive leasing system. To be fair, DOI surely felt “damned if we do, damned if we don’t” as criticism from GAO, the Office of the Inspector General and congressional oversight committees was nearly constant, while the oil industry, which by 1987 was in a shambles, complained that the unavailability of federal lands for lease was contributing to the decimation of the domestic industry. Debate over the environmental protection provisions of a leasing reform bill continued in the first session of the 100th Congress. By then, there were at least four bills pending, containing a variety of provisions: Senator Bumpers’ S.66, Senator Melcher’s (D-Mont.) S. 1388, Representative Miller’s H.R. 933, and Representative Rahall’s (D-W. Va.) H. R. 2851. The bill that finally emerged in the closing hours of the session was a compromise pounded out in conference among Senators Bumpers, Melcher and Wallop (R-Wyo.), and Representatives Miller, Udall and Rahall. The resulting Federal Onshore Oil, and Gas Leasing Reform Act (or FOOGLRAl for those hopelessly addicted to acronyms) was enacted as a part of the Omnibus Budget Reconciliation Act of 1987, and was signed into law on December 22, 1987.

The Reform Act abolished the KGS concept that had been an original part of the 1920 legislation. Instead, all lands are to first pass through a competitive screen that serves as the market test for interest in the lands. The list of lands that will be offered for sale must be posted in BLM (and the local Forest Service office for National Forest lands) at least forty-five days prior to the sale. Oral bid auctions are to be held in each BLM state office at least quarterly, and the high bid for a tract is presumed to be fair-market value; BLM does not make an evaluation of the adequacy of the bid as it did for sealed bid sales of KGS lands.

Lands that do not receive the national minimum acceptable bid (now set at $2 per acre) become available for noncompetitive leasing for a period of two years following the date of the sale. This two-year “recycle” period, as it was called during consideration of the Reform Act, allows a limited noncompetitive leasing program but insulates the government from lost revenues in the event new information about an area sparks competitive interest sometime after the lands were offered for sale and received no bids.

Any noncompetitive offers filed during the month in which the lands had been offered for competitive sale must describe the lands by reference to the parcel number used on the sale notice to identify the lands. All noncompetitive offers filed the day after the competitive lease sale are deemed to have been simultaneously filed and a drawing is held to determine the priority among those noncompetitive applicants. Once the month is over in which the sale was held, a noncompetitive lease applicant may configure the lands in the lease application as he chooses and is not bound by the parcel description contained in the sale notice.
A noncompetitive offer can be filed for lands that have not yet been offered for competitive bid, but the lands described in the offer must first be offered at a competitive sale and draw no minimum acceptable bid before the noncompetitive lease application will be considered. If no minimum acceptable bid is received, the earliest pre-sale offer for the lands obtains priority for issuance of a noncompetitive lease. By filing a pre-sale offer, a party can force BLM to place the lands on the competitive sale first and, at the same time, establish priority for the noncompetitive lease should no bids be received at the sale. Of course, the existence of the presale offer is a public record, so filing the pre-sale offer may have the effect of stimulating interest in the area.

Next to the abolishment of the KGS system and adoption of a largely competitive leasing system, the most significant change under the Reform Act was to vest formal control in the Forest Service over whether to offer national forest lands for lease and, if so, on what terms. Prior to the Reform Act, BLM and the Forest Service agreed, through a memorandum of understanding, that BLM would not offer National Forests or Grasslands for lease without the consent of the Forest Service. The Reform Act formally codified this arrangement. The Forest Service has adopted its own oil and gas leasing regulations which require it to first determine which lands are "administratively available" for lease (i.e., which lands have not been withdrawn from leasing). This is referred to as the "(d)" decision as it appears in 36 C.F.R. § 228.102(d). The administratively available lands are then reviewed to determine which specific parcels should be offered for lease (the "(e)" decision). Industry representatives have urged the Forest Service to make the "(d)" and "(e)" decisions in one NEPA document and this course is being followed by the Forest Service in most cases.

In addition to the significant changes in the structure of the leasing system, which was the primary thrust of the Reform Act, the Act also affects lease operations on federal lands. As with the leasing decision for National Forest lands, the Reform Act also vested authority in the Secretary of Agriculture (which authority is actually exercised by the Forest Service) to regulate all surface-disturbing operations on National Forest lands. Consequently, an application for a permit to drill (APD) on lands the surface of which is administered by the Forest Service must be approved by both the Forest Service, as to the surface use aspects, and BLM, as to downhole concerns.

The Reform Act also added a new public notice requirement before an APD, may be approved. Notice of a proposed APD must be posted in the "appropriate local office of the leasing and land management agencies" for at least thirty days prior to its approval. Consequently, a lessee facing imminent lease expiration must plan sufficiently in advance so that its APD is filed in time to allow for the thirty-day posting prior to agency approval.
Although BLM had always required reclamation of drillsites even prior to the Reform Act, that Act specifically directs the Secretaries of the Interior and Agriculture to post bond or establish other surety “to ensure the complete and timely reclamation of the lease tract, and the restoration of any lands or surface waters adversely affected by lease operations after the abandonment or cessation of oil and gas operations on the lease.” For the time being, at least, the Forest Service has agreed that the bond required by BLM prior to the commencement of surface-disturbing operations is adequate to ensure reclamation of National Forest lands. Although the legislative history of the Reform Act does not contain any evidence that BLM or the Forest Service had difficulty in obtaining post-abandonment reclamation of drillsites, Congress added a severe penalty for anyone failing to reclaim. The Secretary shall not issue a lease or approve an assignment of a lease to any person or entity, or affiliate of that entity, who has “failed or refused to comply in any material respect with the reclamation requirements and other standards established under this section for any prior lease to which such requirements and standards applied,” 30 U.S.C. § 226(g). A few entities have been placed on a list of nonqualified lessees because of failure to reclaim. BLM. Washington Office Instruction Memo No. 93-341 (Sept. 3, 1993).

The Reform Act also contained a number of less significant amendments to the Mineral Leasing Act. For example, in an effort to combat the forty-acre merchants, the Reform Act authorizes the Secretary (in his discretion) to disapprove an assignment of less than 640 acres outside Alaska or less than 2,560 acres in Alaska. The Reform Act also adds a lengthy new provision (section 41) establishing hefty civil and criminal penalties for fraudulent acts. The broad language of the prohibitions in section 41 could, theoretically, trap the unwary. For example, section 41 makes it unlawful for any person to “seek to obtain or to obtain any money or property by means of false statements of material facts or by failing to state material facts concerning” the value of any federal lease, the availability of lands for lease or the provisions of the Act and its implementing regulations. Among other remedies, both the Attorney General and the states are authorized to seek civil penalties of not more than $100,000 for each violation against any person who is violating the prohibitions of section 41. If a state brings the action it is entitled to keep any penalty recovered. A disgruntled would-be purchaser of federal leases could conceivably entreat its state’s attorney general to commence an action against a nonresident lessee who sold leases to a third party.

The three statutes discussed in this article have undeniably formed the basis for development of onshore federal oil and gas resources since 1920. However, they are by no means the only legislation affecting oil and gas operations. The land use planning requirements of the Federal Land Policy and Management Act and the National Forest Management Act play a large role in determining what federal lands will be available for lease and upon what terms. The National Environmental Policy Act and the questions of if,
when, and how its requirement for environmental impact statements applies to the onshore federal leasing system have wreaked havoc with the administration of the system. See, eg., Conner v. Burford, 848 F.2d 1441 (9th Cir. 1988), cert. denied sub nom. Sun Exploration and Production Co. v. Lujan, 109 S. Ct. 1121 (1989); Park County Resource Council v. USDA, 817 F.2d 609 (10th Cir. 1987); Sierra Club v. Peterson, 717 F.2d 1409 (D.C. Cir. 1982). Other statutes with which oil and gas producers must comply (and which BLM and the Forest Service must enforce) include the National Historic Preservation Act, the Endangered Species Act, the Migratory Bird Treaty Act, and the Oil Pollution Act of 1990. Indeed, the fist seems to go on ad infinitum (or ad nauseam, depending on your point of view). How the federal oil and gas leasing system may change in the future is (as in the past) a function of the political winds and legislative compromise. At the moment, House Speaker Gingrich’s Contract with America, with its emphasis on cutting the federal budget and devolution of responsibilities to the states, has prompted calls to turn over the royalty collection program to the states and, in some quarters, recommendations that the federal lands be conveyed to the states — a suggestion reminiscent of the debates on the Mineral Leasing Act in 1919. One conclusion is certain: Most anything that may be suggested to improve the federal oil and gas leasing system in the next century will have been discussed at some point during this century.
Bibliography

Although not the only sources for this article, I have relied particularly on the following excellent histories:

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Instructions and Questions
For Continuing Education or Recertification Credits

This home study course has been designed to provide the reader with an understanding of the Teapot Dome Scandal. Upon satisfactory completion of the following questions as determined by the AAPL Director of Education, the Registered Professional Landman (RPL) or Certified Professional Landman (CPL), as the case may be, will be:

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On a separate sheet(s), please list each of the following six questions with your corresponding answers. Answer the questions as thoroughly as possible. If possible, please use a computer or a typewriter for this assignment. However, if that is not possible, please write or print legibly. When you have completed the questions and answers to your satisfaction, please forward them with a short cover letter to the AAPL Director of Education, c/o AAPL, 4100 Fossil Creek Boulevard, Fort Worth, Texas 76137-2791. This home study booklet is yours to keep.

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Questions

1. Describe two of the objections to a leasing system for federal oil and gas, which were discussed in Congress during the first two decades of the 20th century.

2. Outline the original oil and gas leasing provisions of the Mineral Leasing Act of 1920.

3. Explain the importance of the Linowes Report.

4. Discuss two elements of the noncompetitive leasing system, which led to its almost complete abolition in 1987.

5. Discuss the role of the Forest Service in making oil and gas leasing and development decisions on National Forest Lands.

6. Discuss the Teapot Dome Scandal including the players’ and the illegalities involved.