No. 08-1404

In the Supreme Court of the United States

DEVON ENERGY CORPORATION, PETITIONER

v.

KEN SALAZAR, SECRETARY OF THE INTERIOR

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether the Administrative Procedure Act requires that an agency follow notice-and-comment procedures before interpreting its own regulations in an administrative adjudication where a prior interpretation of those regulations was made by officials who lacked authority to issue binding interpretations of the regulations on the agency's behalf.

2. Whether the Department of the Interior may order a natural-gas lessee to perform a restructured accounting and pay unpaid royalties due to the United States after the entity has partially paid those royalties to the United States.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-23a) is reported at 551 F.3d 1030. The opinion of the district court (Pet. App. 25a-40a) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on December 23, 2008. A petition for rehearing was denied on February 13, 2009 (Pet. App. 62a). The petition for a writ of certiorari was filed on May 14, 2009. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. The United States owns lands that are rich with deposits of natural gas. The United States leases the right to extract and sell that gas to various entities, in-

cluding petitioner. In exchange, lessees agree to pay the United States royalties on the natural gas they produce.

Congress has established the framework for calculating natural gas royalties. Lessees must pay royalties of no less than 12.5% of the "amount or value of the production removed or sold from the lease." 30 U.S.C. 226(b)(1)(A). Department of the Interior (Interior) regulations specify that the "value of production" must be no less than the "gross proceeds" accruing to the lessee minus certain allowable deductions, 30 C.F.R. 206.152(h). Among other things, lessees may deduct from their "gross proceeds" the cost of transporting gas to a point away from the leased site, including to "a gas processing plant off the lease and from the plant to a point away from the plant." 30 C.F.R. 206.156(a).

Interior's regulations, however, specify that lessees must, "at no cost to the Federal Government," "place gas in marketable condition" for sale, *i.e.*, in a state in which the gas is "sufficiently free from impurities and otherwise in a condition that [it] will be accepted by a purchaser under a sales contract typical for the field or area." 30 C.F.R. 206.151, 206.152(i). The regulations therefore prohibit a deduction from "gross proceeds" for the costs incurred by the "lessee to place the gas in marketable condition." 30 C.F.R. 206.152(i).

2. Petitioner leases federal land in Wyoming that produces a type of natural gas known as coalbed methane. Pet. App. 5a. Natural gas produced under those leases is pumped to Central Delivery Points (CDPs)—*i.e.*, approved locations for measuring the royalties due—and it subsequently undergoes a complex series of compression, dehydration, and other processes before its sale. *Id.* at 6a-7a.

When calculating the royalties it owed the United States, petitioner deducted the compression and dehydration costs it incurred after the gas left CDPs, based on its view that those costs constituted transportation costs that may be deducted from gross proceeds. Pet. App. 8a. Petitioner contends that its interpretation was based primarily on two internal Minerals Management Service (MMS) guidance documents issued in late 1995 and a 1996 letter from the MMS Acting Associate Director for Royalty Management to royalty payors (Dear Operator letter). Cf. *id.* at 7a-8a.

3. a. In 2002, petitioner sought guidance from MMS to determine whether petitioner was properly deducting its post-CDP dehydration and compression costs as part of its transportation allowance. In 2003, the Acting Assistant Secretary of the Interior for Land and Minerals Management issued a decision concluding that petitioner's deductions were in error. Pet. App. 9a.

The initial agency decision explained that the costs of dehydration and certain compression processes after gas left the CDPs were not properly deductible "because th[ose] compression and dehydration functions were necessary to put the production into marketable condition." Pet. App. 9a. Petitioner's sales contracts required that petitioner "compress the gas to [the] pipeline pressure" of its purchaser's pipelines in order to allow the gas to flow into those lines and "enable the gas to be 'accepted by a purchaser under a sales contract typical for the field or area.'" *Ibid.* (quoting C.A. App. 88). Likewise, lessees were obligated to "dehydrate gas to the water content required for delivery to the pipeline" in order to sell gas under contracts typical for the field or area, and the Acting Assistant Secretary concluded that petitioner had failed to show that its rele-

vant dehydration processes were "for anything other than what is required to put the production into marketable condition" and "meet pipeline and purchaser requirements." *Id.* at 10a (quoting C.A. App. 91). The decision explained that petitioner had based its contrary interpretation of the relevant regulations on statements in internal MMS guidance documents and the Dear Operator letter that were "either ambiguous, or reflected an incorrect application of the marketable condition rule, or were simply 'inconsistent' with the rule." *Id.* at 9a (internal citations omitted).

In 2004, the Acting Assistant Secretary denied reconsideration in a final agency order that affirmed the initial agency decision in relevant part and directed petitioner to recalculate past royalties in accordance with the order. Pet. App. 10a.

b. Petitioner then filed the present action seeking judicial review of the agency's final decision. The district court entered summary judgment for respondent. Pet. App. 24a-40a.

c. The court of appeals affirmed. Pet. App. 1a-23a. The court concluded that Interior's 2004 "interpretation of [its] marketable condition rule" was controlling because it "reflects a perfectly reasonable construction" that is consistent with the "plain language of the rule." *Id.* at 3a, 12a-13a.

The court of appeals also concluded that it was not necessary for the agency to issue its 2004 interpretation of its royalty regulations through notice-and-comment rulemaking. Pet. App. 15a-23a. The court "agree[d] with [the government]" that the 1995 internal guidance documents and 1996 letter cited by petitioner did not constitute "official or binding [agency] action" and that, without a prior "definitive interpretation" by the agency,

the Administrative Procedure Act (APA), 5 U.S.C. 551 *et seq.*, "does not require notice and comment rulemaking to effect a change in that interpretation." Pet. App. 16a. The court provided two independent bases for that holding. *Id.* at 16a-23a.

First, the court found "much force to [the government's] argument that * * * the guidance documents were far from conclusive in what they said." Pet. App. 17a. That conclusion, the court explained, was reinforced by the fact that petitioner decided to seek formal confirmation from the agency of petitioner's regulatory interpretation—a request that itself undermined petitioner's contention that the agency documents "authoritatively resolved" the relevant questions. *Ibid.* ("It is perplexing, to say the least, that [petitioner] was seemingly confused over the propriety of its royalty accounting if, in its view, the matters at issue had been authoritatively resolved" by the guidance documents).

Second, the court held that "the [a]gency was free to adopt the interpretation at issue in this case without providing an opportunity for notice and comment" because the three guidance documents cited by petitioner did not "constitute[] authoritative and binding interpretations of the marketable condition rule" that expressed the agency's interpretation of its regulations. Pet. App. 17a, 23a. The court explained that the 1996 Dear Operator letter neither spoke for nor was "binding on the agency," *id.* at 18a, and the court found that conclusion to be supported by petitioner's admission that petitioner "does not contend that the * * * letter in and of itself was a binding rule," *id.* at 19a (quoting Pet. Corrected C.A. Reply Br. 14).

Petitioner instead argued that Interior had adopted a regulatory interpretation upon which petitioner relied

"through the cumulative effect of a number of agency actions." Pet. App. 19a (quoting Pet. Corrected C.A. Reply Br. 14). The court rejected that argument, concluding that the agency was bound neither by the fact that two internal guidance documents were issued in 1995 nor by the fact that regulated entities may have followed that guidance. *Id.* at 19a-21a. The court explained that petitioner "readily conceded" at oral argument that (a) the policy board that issued the internal guidance documents in 1995 lacked "authority to issue authoritative guidelines" and (b) the documents themselves "did not have the force of law." *Id.* at 19a. For those reasons, the internal guidance did not constitute "a definitive and binding statement on behalf of the agency." *Id.* at 20a. The court also rejected the view that Interior was "bound by the guidance documents" because "regulated parties followed the advice in the documents" for several years. *Ibid.* Such action by private entities, the court explained, did not transform otherwise non-binding guidance into agency documents with binding, "legal consequences." *Id.* at 21a.

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court of appeals. Further review is unwarranted.

1. a. The informal rulemaking provisions of the APA specify that agencies must generally provide the public with notice of proposed rulemaking and an opportunity to comment on the proposal. 5 U.S.C. 553(b) and (c). Congress, however, exempted several categories of rules, including "interpretive rules," from the APA's notice-and-comment rulemaking requirements, 5 U.S.C. 553(b)(A), and separately specified that the Act's "rule

making" provisions do not apply to legal principles developed in agency adjudications. 5 U.S.C. 551(6) and (7).

The APA thus makes clear that Interior's regulatory interpretation in its final adjudicatory decision in this case is not subject to the APA's notice-and-comment rulemaking requirements. Indeed, even if the agency's adjudicatory decision could qualify as rulemaking, Section 553 specifically exempts "interpretive rules" from the Act's notice-and-comment requirements. That alone would justify the court of appeal's judgment. The APA, as this Court recently confirmed, "sets forth the full extent of judicial authority to review executive agency action for procedural correctness," and, because the statute does not specify that "all agency change be subjected to more searching review," there is no basis for courts to impose additional procedural hurdles for an agency to cross. *FCC* v. *Fox Television Stations, Inc.*, 129 S. Ct. 1800, 1810 (2009) (*Fox Television*) (citing *Vermont Yankee Nuclear Power Corp.* v. *NRDC*, 435 U.S. 519, 545-549 (1978)).

Although some courts of appeals concluded before *Fox Television* that an agency decision interpreting a regulation in a manner inconsistent with the agency's prior interpretation of that regulation must be issued using notice-and-comment procedures, Pet. 11-12, 14, the court of appeals correctly held that that court-imposed requirement for interpretive changes has no application here. Pet. App. 15a-23a. The court accepted petitioner's written and oral concessions that the informal guidance and letter proffered by petitioner as prior agency interpretations were authored by "individuals who had no authority * * * to issue authoritative guidelines on behalf of the agency." *Id.* at 3a, 19a. In the absence of a prior binding interpretation by the

agency itself, the court rejected the contention that notice-and-comment procedures were necessary before the agency interpreted its regulations in the first instance. *Id.* at 23a.

b. Petitioner contends (Pet. 9-19) that this Court should grant review to resolve a division of authority on whether notice-and-comment procedures must be used when an agency changes its prior interpretation of a regulation. Contrary to petitioner's contention, review is unwarranted.

First, although petitioner is correct that several courts of appeals have divided over whether such interpretative changes trigger notice-and-comment obligations (Pet. 11-12, 14), that question is not presented in this case. Indeed, the very proposition that petitioner embraces was first adopted by the District of Columbia Circuit in *Alaska Professional Hunters Ass'n* v. *FAA*, 177 F.3d 1030, 1033-1035 (D.C. Cir. 1999) (following dicta in *Paralyzed Veterans of Am.* v. *D.C. Arena L.P.*, 117 F.3d 579, 586 (D.C. Cir. 1997), cert. denied 523 U.S. 1003 (1998)), and the court of appeals in this case expressly held that the proposition it adopted in *Alaska Professional Hunters* was inapplicable because it applies only when an agency changes course from a prior binding interpretation by the agency. Pet. App. 22a-23a. The court of appeals concluded, based on petitioner's oral and written concessions, that there was no prior binding interpretation by the agency here.[1]

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[1] Petitioner does not discuss its concessions that the internal guidance documents and letter cited by petitioner were authored by officials with "no authority * * * to issue authoritative guidelines on behalf of the agency." Pet. App. 3a, 19a. Instead, petitioner now appears to assert (Pet. 3-4, 16 & n.6) that those officials did, in fact, have such authority, citing to materials never presented to the court of appeals. Peti-

Second, even if the question were presented in this case, review by this Court would be premature because the courts of appeals that have followed *Alaska Professional Hunters* have yet to determine whether the logic of their decisions remains viable after this Court's recent decision in *Fox Television*. *Fox Television* should now eliminate any doubt that courts cannot properly impose procedural requirements to govern an agency's change in position—like the judge-made rule imposed by *Alaska Professional Hunters*—where, as here, those requirements are not imposed by the APA itself.

c. Petitioner argues (Pet. 15-19) that the decision below conflicts with *Shell Offshore Inc.* v. *Babbitt*, 238 F.3d 622 (5th Cir. 2001), which concluded that notice-and-comment procedures were necessary where an agency adopted an unwritten but "long established and consistently followed practice" reflecting one interpretation of a regulation and later changed that interpretation. *Id.* at 630. Although the decision below is in tension with *Shell Offshore*, it does not conflict with that decision. *Shell Offshore* premised its decision on the existence of what it deemed to be a longstanding official practice of the agency reflecting an unwritten interpre-

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tioner's newly found contention comes too late. Not only did petitioner forfeit it by failing to raise it below, but petitioner affirmatively waived the argument by conceding the officials' lack of authority in the court of appeals. The court of appeals accepted that concession, Pet. App. 3a, 19a (discussing oral and written concessions), and no further review is warranted to consider that fact-bound determination. Cf. C.A. Pet. for Reh'g 2 (repeating concession that "[t]he regulatory interpretation that [petitioner] and others followed was not authored by an official authorized to promulgate rules binding on the agency"); cf. also Pet. 16 n.6 (attempting to distinguish prior decisions regarding similar Interior documents on the ground that the "parties in those cases" "presumably" did not raise the materials cited by petitioner for the first time at Pet. 3-4).

tation of agency regulations. The court in *Shell Offshore* did not decide whether it would reach the same result if that practice was based on decisions of subordinate officials who lack authority to issue a regulatory interpretation on the agency's behalf. Because that question was not raised or resolved in *Shell Offshore*, *Shell Offshore* does not conflict with the decision below.

d. This case would present a poor vehicle for resolving the first question presented for the additional reason that petitioner has not contested the court of appeals' conclusion that prior administrative interpretations of the regulations at issue do not appear to "conclusive[ly]" resolve the interpretive question disputed by the parties. Pet. 16a-17a; see also Gov't C.A. Br. 37-40 (explaining that the internal guidance and letter were ambiguous in this regard). Thus, even if the officials who issued the pertinent internal guideline documents and letter had authority to interpret the agency's regulations on the agency's behalf, Interior's final decision in this case did not trigger notice-and-comment obligations under *Alaska Professional Hunters* because it did not conflict with prior regulatory interpretations. See *MetWest Inc.* v. *Secretary of Labor*, 560 F.3d 506, 509-512 (D.C. Cir. 2009) ("[S]o long as a new guidance document 'can reasonably be interpreted' as consistent with prior documents, it does not significantly revise a previous authoritative interpretation.") (quoting *Air Transp. Ass'n* v. *FAA*, 291 F.3d 49, 57-58 (D.C. Cir. 2002)); see also *Darrell Andrews Trucking, Inc.* v. *Federal Motor Carrier Safety Admin.*, 296 F.3d 1120, 1126-1127 (D.C. Cir. 2002); *Shell Offshore*, 238 F.3d at 629 (stating that "the APA requires an agency to provide an opportunity for notice and comment before substantially altering a *well established* regulatory interpretation" (emphasis add-

ed)). Moreover, because the question whether the particular guidance documents at issue here were ambiguous has been overtaken by the agency's subsequent, authoritative interpretation of its regulations in this case, the question has no prospective importance and does not warrant this Court's review.

2. Petitioner argues (Pet. 19-23) that certiorari is warranted to determine whether Interior properly required petitioner "retroactively to recalculate royalties owed to the Government." Pet. 19 (emphasis omitted). Review is not warranted on that question. Petitioner did not challenge the retrospective impact of the agency's order in this case in its opening brief on appeal; the government's response explained that petitioner did "not argue that Interior may never require a royalty payor to recalculate the royalties it paid in past years" (Gov't C.A. Br. 44); and petitioner did not subsequently challenge the government's assertion. Indeed, petitioner's appellate briefs did not even cite the retroactivity decisions on which petitioner now relies (Pet. 20-22), and the court of appeals accordingly did not address any retroactivity-based contentions. Because the second question presented was not raised or passed upon below, further review is unwarranted.[2]

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[2] Although petitioner quotes (Pet. 19) from the court of appeals' statement that this case "arises from a final [agency] order * * * requiring [petitioner] retroactively to calculate royalties owed to the Government," Pet. App. 2a, that introductory statement before the court's legal analysis does not reflect a holding, and nothing in the opinion reflects a determination regarding the retrospective recalculation of royalties. In any event, Congress has expressly authorized Interior to order restructured accountings and collect underpaid royalties, 30 U.S.C. 1711(c)(1), 1724(d)(4)(B)(i), and that authorization undermines petitioner's apparent contention that such collection efforts are unlawful. See *BP Am. Prod. Co.* v. *Burton*, 549 U.S. 84, 87, 100-101 (2006).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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