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Blackhawk Coal Company v. The Utah Division of State Lands and Forestry, Ralph Miles, Director of The Division of State Lands and Forestry, the Utah Board Of State Lands and Forestry, the Utah Department of Natural Resources, Dee Hansen, Executive Director of the Utah Department of Natural Resources : Brief of Appellant

Utah Supreme Court

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IN THE SUPREME COURT OF THE STATE OF UTAH

BLACKHAWK COAL COMPANY, Plaintiff/Respondent, vs. THE UTAH DIVISION OF STATE LANDS AND FORESTRY, RALPH MILES, DIRECTOR OF THE DIVISION OF STATE LANDS AND FORESTRY, THE UTAH BOARD OF STATE LANDS AND FORESTRY, THE UTAH DEPARTMENT OF NATURAL RESOURCES, DEE HANSEN, EXECUTIVE DIRECTOR OF THE UTAH DEPARTMENT OF NATURAL RESOURCES, Defendants/Appellants.	Case No. 880215 Category No. 14

BRIEF OF APPELLANTS

Appeal from the Seventh Judicial District
Court of Carbon County, State of Utah
The Honorable Boyd Bunnell, Judge.

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STATEMENT OF JURISDICTION

This Appeal is from the Court's Memorandum Decision and Declaratory Judgment granting Summary Judgment for the Plaintiffs. The Supreme Court of the State of Utah has jurisdiction to hear this Appeal under Utah Code Ann. §78-2-2(3)(i) and Utah Code Ann. §78-2-2(3)e(iii).

NATURE OF THE PROCEEDINGS BELOW

The Director of State Lands upheld an audit and demand for payment issued by the Division of State Lands. The Plaintiff filed a Declaratory Judgment action challenging the Director's decision. The trial court granted Plaintiff's Motion for Summary Judgment and entered a Judgment reversing the decision of the Director.

STATEMENT OF ISSUES PRESENTED FOR REVIEW

The issues presented on this appeal are as follows:

(1) Whether the trial court erred in entering Summary Judgment authorizing depletion of the trust asset for less than full value in view of Federal and State constitutional law governing school trust lands?

(2) Whether the plain language of the lease may be rewritten by the court because one party claims it is ambiguous?

(3) Whether Plaintiff should be barred from using the doctrine of estoppel to avoid paying monies owed to the school trust fund when it was Plaintiff's duty to report and pay the correct amount of royalties?

RELEVANT CONSTITUTIONAL PROVISIONS AND STATUTES

Utah Enabling Act, §6:

That upon the admission of said State into the Union, sections numbered two, sixteen, thirty-two, and thirty-six in every township of said proposed state, and where such sections, or any parts thereof have been sold or otherwise disposed of by or under the authority of any Act of Congress, other lands equivalent thereto, in legal subdivisions of not less than one quarter section and as contiguous as may be to the section in lieu of which the same is taken, are hereby granted to said State for the support of common schools....

Utah Enabling Act §10:

That the proceeds of lands herein granted for educational purposes, except as hereinafter otherwise provided, shall constitute a permanent school fund, the interest of which only shall be expended for the support of said schools, and such land shall not be subject to pre-emption, homestead entry, or any other entry under the land laws of the United States, whether surveyed or unsurveyed, but shall be surveyed for school purposes only.

Utah Constitution, Article X, §5:

The proceeds of the sale of lands reserved by an Act of Congress, approved February 21st, 1855, for the establishment of the University of Utah, and of all the lands granted by an Act of Congress, approved July 16th, 1894, shall constitute permanent funds, to be safely invested and held by the State; and the income thereof shall be used exclusively for the support and maintenance of the different institutions and colleges, respectively, in accordance with the requirements and conditions of said Acts of Congress. 91 (Article X was amended, effective July 1, 1987 with Section 5 becoming Sections 5 and 7).

Utah Constitution, Article XX, §1:

All lands of the State that have been, or may hereafter be granted to the State by Congress, and all lands acquired by gift, grant or devise, from any person or corporation, or that may otherwise be acquired, are hereby accepted, and declared to be the public lands of the State; and shall be held in trust for the people,

to be disposed of as may be provided by law, for the respective purposes for which they have been or may be granted, donated, devised or otherwise acquired.

Utah Code Ann., §65-1-23:

Except as otherwise provided by law, the State Land Board shall by rules and regulations prescribe the form of application, the form of lease, the annual rental, the amount of royalty and the basis upon which the royalty shall be computed, and such other details as it may deem necessary in the interest of the state.

Utah Code Ann., §65-1-76:

All leases and contracts of every kind entered into by the State Land Board shall before execution by such board be approved as to form by the attorney general.

30 U.S.C. §207(a):

[A] lease shall require payment of a royalty in such amount as the Secretary shall determine of not less than 12 1/2 per centum of the value of coal as defined by regulation, except the Secretary may determine a lesser amount in the case of coal recovered by underground mining operations....

43 C.F.R. §3473.3-2:

2. A lease shall require payment of a royalty of not less than 12 1/2% of the value of the coal removed from a surface mine.

3. A lease shall require payment of a royalty of not less than 8% of the value of the coal removed from an underground mine, except that the (Minerals Management Service) may determine a lesser amount, but in no case less than 5% if conditions warrant.

STATEMENT OF THE CASE

The Utah Division of State Lands audited the payments under its coal leases on school trust lands. One of those leases was held by Plaintiff, Blackhawk Coal Company. Demand was made to Plaintiff to pay royalties found by the audit to have been

underpaid. Plaintiff appealed the decision of the auditors tc the Director of the Division of State Lands. The Director, after a hearing, upheld the audit and the demand for payment. (R.433) Plaintiff then filed this action in the Seventh Judicial District Court asking for a declaration that the State could not collect the unpaid royalties. Plaintiff filed a Motion for Partial Summary Judgment. The trial court granted Plaintiff's Motion for Partial Summary Judgment finding that Plaintiff owed nothing to the State. (Addenda 1 and 2) It is from those Orders that this appeal is taken.

The United States, pursuant to the Utah Enabling Act, granted lands to the State of Utah to be used for the support of the common schools. The State holds the land as trustee. Management of those lands is by the Board of State Lands and the Division of State Lands. Utah Code Ann. §65-1-14.

On February 16, 1960 the State issued to Carbon Development Company coal lease no. 18148. (Addendum 3) The lease authorizes extraction of coal from school trust lands located in Carbon County, Utah. The lease is perpetual, as long as coal is produced in commercial quantities, with a provision for adjustment at the end of each 20-year period. The lease was assigned to the Plaintiff.

The United States Government owns most of the coal-producing lands within the State of Utah; therefore, the royalty charged on federal coal leases generally becomes the prevailing market

royalty rate for coal leases within the State. When State lease no. 18148 was issued by the State, the royalty rate on many federal coal leases was $.15 per ton. The paragraph (Article III Second) requiring the payment of royalty on the subject State lease requires Lessees:

> To pay to Lessor quarterly, on or before the 15th day of the month succeeding each quarter, royalty
>
> (a) at the rate of $.15 per ton of 2000 lbs. of coal produced from the leased premises and sold or otherwise disposed of, or
>
> (b) at the rate prevailing, at the beginning of the quarter for which payment is being made, for federal lessees of land of similar character under coal leases issued by the United State at that time,
>
> whichever is higher....

State lease no. 18148 also requires the Plaintiff to prepare and forward to the State, each quarter, a certified statement as to the amount of production together with other information as required by the State Land Board. (Article III, Third) The State also retained the right to go upon the premises and conduct audits of the lessees' records. (Article XI)

The federal coal lease royalty rate generally remained at $.15 per ton until August 4, 1976. On August 4, 1976 the Federal Coal Leasing Amendments Act of 1976, 30 U.S.C. §§201-209 was enacted by Congress. The Act and the regulations promulgated thereunder, increased the royalty rate on surface mines to 12 1/2% of the value of the coal produced and the royalty rate on underground mines to 8% of the value of the coal produced.

Between January 1, 1979 and the audit, twenty-four (24) coa leases were issued by the United States Bureau of Land Management on lands within the State of Utah. (R.315, 415, 441) Nineteer (19) of those leases required a royalty payment of 8% of the value of coal. (R.315, 415, 441) Only one required a royalty rate of less than 8% and that royalty rate was 5% of the value of the coal. The adjoining States of Colorado, Wyoming and New Mexico have all increased their royalty rate to at least 8% of gross sales value of the coal extracted. (R.423, 425, 431)

Plaintiff was fully aware of the Federal Coal Leasing Amendments Act and the increase in the federal royalty rate. Plaintiff had this knowledge from the leasing of federal lands and litigation involving the increased royalty rate on federal coal leases held by Plaintiff. (R.397, 399) See also Blackhawk Coal Company IBLA 82-519. Plaintiff also holds 11 federal leases in the Price River Complex where state lease no. 18148 is located. Four of those leases have a royalty rate of $.12.5 per ton. Those leases were issued in the 1930's and 1950's. Six of the leases have a royalty of 8% and one has a royalty of 10.4%. Those leases were either issued or adjusted after passage of the Federal Coal Leasing Amendments Act of 1976. (R.396)

In 1981 the State of Utah notified Plaintiff that the State intended to adjust state lease no. 18148. The adjustments included an increase in the royalty rate. Plaintiff objected and argued that the request for readjustment was not timely. (R.280)

The Land Board, after a hearing, upheld the adjustments but delayed enforcement of the adjustment until the Attorney General's office decided whether the request for adjustment was timely. (R.280) This question was being litigated in the federal courts, Rosebud Coal Sales Company vs. Andrus, 667 F.2d 949 (1982), therefore the Attorney General's office deferred issuing an opinion until the federal courts settled the question. In 1983 Plaintiff ceased production so the adjustment was not pursued by the State. The royalties sought to be collected accrued prior to the last quarter of 1983. (R.303)

The lands that the Division of State Lands manages have thousands of mineral leases. The Division does not have the funds or the personnel to monitor each lease or the payments received on those leases. (R.433) Instead the State of Utah, as written in its lease provisions and regulations, requires its lessees to accurately provide information and to pay the correct amounts of royalties. (Addendum 3) Like reporting taxes, it has largely been an honor reporting system. In 1981 the Utah State Legislature appropriated funds for the Division of State Lands to hire an auditor to review income from its mineral leases. (R.412, 433) Richard Mitchell was hired. (R.412) He set up an auditing procedure and started to audit the State's oil and gas leases. (R.412) In 1984 the Auditing Division was expanded and two auditors, Douglas E. Johnson and Ralph Aiello, were hired. (R.415, 427)

In December of 1984 the auditors started to review the State coal leases. The audit included an analysis of the U.S. Bureau of Land Management records on federal coal leases and an examination of the Plaintiff's and other State coal lessee records. The auditors found that the coal lessees had, in certain instances, under reported production and failed to report other vital information. They also found that the royalty rate on federal coal leases had increased to 8% beginning in 1977 but the Plaintiff had failed to report and pay royalties at the prevailing federal rate. (R.415, 4272)

An audit report was prepared and submitted to the Division of State Lands. (R.303, 415, 427) The Director of the Division of State Lands established an audit committee to review the auditors' report. The committee reviewed the lease and the findings of the report. Some adjustments were made to the report and it was approved. (R.415, 433) The report was then sent to the Plaintiff with a request for payment of the delinquent royalties together with interest.

The Plaintiff, upon receipt of the audit report, requested a hearing before the Director of the Division of State Lands. A hearing was held. The Director rejected the appeal and upheld the findings of the auditors. (R.433)

STANDARD OF REVIEW

This appeal is from the trial court's grant of a Motion for Summary Judgment. Summary Judgment is appropriate only when the

pleadings, depositions, interrogatories and admissions on file, together with affidavits, show there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law. Utah Rule of Civil Procedure 56(c). This Court should consider the evidence in a light most favorable to the Defendants, Durham vs. Margetts, 571 P.2d 1332 at 1334 (Utah 1977), and affirm the decision only if the Court determines there is no genuine dispute as to any material issue of fact and that the Plaintiff is entitled to judgment as a matter of law. Briggs vs. Holcombe, 740 P.2d 281 at 283 (Utah 1987). This Court, in reviewing the issues of law, gives no deference to the trial court. Atlas Corporation vs. Clovis National Bank, 737 P.2d 225 at 229 (Utah 1987).

The issues before the Court have been decided against Plaintiff by the Director of State Lands. The Court, when reviewing the decision of the Director, should not override the Director's interpretation of the Division's rules, policies and regulations unless his decision is arbitrary or erroneous. This Court should only inquire as to whether the Director acted in excess of his powers in upholding the audit. McKnight vs. State Land Board, 381 P.2d 726 at 731 (Utah 1963), Atlantic Richfield Company vs. Hinkel, 432 F.2d 587 at 591 (10th Cir. 1970).

The Defendants agree that the controlling issues in the case are issues of law. The Defendants maintain that when the issues of law are correctly decided they are entitled to judgment as a

matter of law. Defendants maintain, however, that there are issues of fact in dispute which preclude entry of summary judgment for the Plaintiff. Defendants request that this Court review the legal issues, that those issues be decided in favor of Defendants, and that the case be remanded with instructions to enter judgment in favor of the Defendants.

SUMMARY OF ARGUMENT

1. The State of Utah, as a condition of statehood, acquired certain lands in trust for the benefit of the common schools. The State has a Constitutional and moral duty to obtain full value from the disposition of those lands. The trial court placed impermissible restrictions on the trust lands in question when it restricted the royalty rate the State could collect from those lands to $.15 per ton rather than allowing the State to collect the contractually required market rate of 8% of value of the coal.

2. The royalty provision in the coal lease is clear and should be given its plain meaning. The requirement that the Plaintiff periodically determine whether the federal royalty rate has changed and that it pay royalties on the changed rate does not create an ambiguity. Such provisions are common in long-term leases to insure that the parties pay according to prevailing market terms. In this case, a fluctuating royalty rate is constitutionally required to insure that the trust fund receives full value for its lands.

3. The Court should use rules of construction to clarify any ambiguity in the lease. The trial court erred when it rewrote the parties' lease by limiting royalties to $.15 per ton. Not even the Plaintiff claims that the royalty rate should always remain at $.15 per ton. The lease should be construed to give meaning to all its provisions including subparagraph (b) of the royalty provision which provides for increases in the royalty rate.

4. Estoppel should not be used by the Court to prevent the trust fund from receiving full value for its assets. The Utah Enabling Act requires the trust to receive full value and requires the State to manage the trust fund in its governmental capacity. To allow estoppel in this case would violate those constitutional requirements and would cost the trust fund in excess of three million dollars.

5. The Plaintiff has suffered no injury, was aware of the facts which caused the royalty rate to increase, and had the duty to pay the correct royalties. The State is only asking that the Plaintiff pay what is required by the lease. Such a request should not be estopped.

ARGUMENT

POINT I. UNDER STATE AND FEDERAL CONSTITUTIONAL LAW THE TRUST ASSETS OF THE STATE SCHOOL TRUST LANDS MAY NOT BE DEPLETED FOR LESS THAN FULL VALUE.

The State lands which are subject to the coal lease in question are school trust lands. The interpretation of the lease and the other issues that were before the trial court were subject to rules of law established by the Utah Enabling Act, Constitutional provisions and case law. The trial court erroneously rejected the law governing school trust lands in its construction of the lease and in its holding that the State was estopped from obtaining fair market value for its trust lands. This argument will first set forth a brief historical background on the purpose and policy of trust lands and will then examine the case law which the trial court should have applied in deciding this case.

A. The Historical Background Provides Essential Perspective.

Utah is one of thirty (30) public land states whose Enabling Act granted lands to be used for the support of schools and institutions. L. Mall, Public Land and Mining Law, 44-47 [3 Ed. 1981]. In Utah vs. Kleepe, 586 F.2d 756 (10th Cir. 1978) rev'd on other grounds 446 U.S. 500 (1980) the Court explained the purpose of the school land grants:

> There were no federal lands within the borders of the original thirteen states when they adopted and ratified the United States Constitution. Thus, virtually all of the lands within their borders were subject to taxation, including taxation necessary for the

> maintenance of their public school systems. When other states were subsequently admitted into the Union, their territorial confines were "carved" from federal territories. The "public lands" owned and reserved by the United States within those territorial confines were not subject to taxation. This reservation by the United States created serious impediment to the "public land" states in relation to an adequate property tax base necessary to permit these states to operate and maintain essential government services, including the public school systems. It was in recognition thereof, i.e., in order to "equalize" the status of the newly admitted states with that of the original thirteen states, that the Congress enacted the federal land grant statutes. The specific purpose was to create a binding permanent trust which would generate financial aid to support the public school systems of the "public land" states.

Id. at 758.

The Utah Enabling Act granted four (4) sections of land in each township for the support of the common schools. Utah Enabling Act §6. The State of Utah, in its Constitution, accepted those lands in trust for the respective purposes for which they had been granted. Constitution of Utah, Article XX.

B. The Law Requires The Receipt Of Full Value From The Disposition Of Trust Lands.

The school land grants constitute a solemn agreement between the United States and the State of Utah. There has been imposed upon the State of Utah:

> [a] binding and perpetual obligation to use the granted lands for the support of public education. All revenue from the sale or lease of the school grants was impressed with a trust in favor of the public schools. No State could divert school lands to other public purposes without compensating the trust for the full market value of the interest taken.

Andrus vs. Utah, 446 U.S. 500 at 523-524, 64 L.Ed.2d 458 at 474,

100 Sup. Ct. 1803 (1981).

Beginning with the case of Trustees of Vincennes University vs. State of Indiana, 55 U.S. 268 at 274 (1852) the Supreme Court of the United States has consistently held that a State holds school lands in trust for the benefit of its schools. Congress and the Courts have placed restrictions on the use of the trust lands so that they are not exploited for private advantage or depleted by State action or inaction. Lassen vs. Arizona, 385 U.S. 458, 87 S.Ct. 584, 17 L.Ed.2d 515 at 522 (1967). (While Lassen dealt with surface rights, recent cases make it clear that these restrictions also apply to mineral interests located in school trust lands. Jensen vs. Dinehart, 645 P.2d 32 at 35 (Utah 1982), Alamo Land and Cattle Company vs. Arizona, 424 U.S. 295, 96 S.Ct. 910, 47 L.Ed.2d 1 at 8 (1976).

The duty of the State, in managing mineral rights on trust lands, is to obtain full value for the trust assets:

> The royalty rate set by the state is important because it represents payment for a trust asset which will be gone forever once the mineral is removed from the ground. Therefore, the requirements of the Enabling Act and the trust concept are the most important factors to consider in determining an optimum royalty rate. If the rate is too low the state will be committing a breach of trust by diminishing the trust. Royalty payments are placed in a permanent trust fund, the corpus of which is invested; the trust is kept whole if fair market value is received. If the royalty rate is too low the trust will not be kept whole.

3 State School Trust Lands and Oil and Gas Royalty Rates. Public Land Law Review, 119, 130 (1982). See also Kadish vs. Arizona State Land Department, 747 P.2d 1183 at 1195 (Ariz. 1987). State

vs. Kleepe, supra at 758; State vs. University of Alaska, 624 P.2d 807 at 813 (Alaska 1981).

To enforce this important trust purpose, the Courts have consistently rejected any State statutes, constitutional provisions and Court-imposed doctrines which restrict the State from obtaining full value from the trust lands. In Kadish vs. Arizona State Land Department, supra, the Supreme Court of Arizona held unconstitutional an Arizona statute that fixed a flat royalty rate for mineral leases on state school trust lands. The court noted that federal law is supreme in this field and that:

> [n]either this court, nor the legislature, nor the people may alter or amend the trust provisions contained in the Enabling Act without congressional approval.

Id. at 1185. The court said that the Enabling Act intended to severely circumscribe the power of state government to deal with the assets of the common school fund. It analyzed the court cases dealing with this subject and pointed out that:

> [t]he courts have consistently construed the scope of federal land grants in favor of the government. In dealing with trust land ... all doubts must be resolved in favor of protecting and preserving trust purposes.

Id. at 1195.

The primary case discussing the Utah Enabling Act is State of Utah vs. Kleepe, supra. That case dealt with the State's "in lieu" selections of additional lands to replace lands the State had not received pursuant to the Enabling Act. The Court, after

reviewing the Utah Enabling Act and the historical development of trust lands, stated:

> The school land grant and its acceptance by the state constitutes a solemn compact between the United States and the state for the benefit of the state's public school system.

Id. at 758.

Recent cases from other jurisdictions have consistently rejected attempts to limit the income received by the school trust. In Anderson vs. Board of Education, 256 N.W.2d 318 (Neb. 1977) the Nebraska Supreme Court approved the resale of school trust property after a higher upset bid was received after the first sale. It stated that the constitution:

> imposes on the Board the duty of obtaining the highest price possible for all trust property it may sell.

Id. at 321.

In Oklahoma Education Association vs. Nigh, 642 P.2d 230 (Ok. 1981) the Supreme Court of Oklahoma struck down a law authorizing low-interest loans to farmers from the funds of the school trust fund. In doing so the court said:

> No disposition of such lands or funds can be made that conflict either with the terms and purposes of the grant in the Enabling Act or the provisions of the Constitution relating to such land and funds. The State has an irrevocable duty, as Trustee, to manage the trust estate for the exclusive benefit of the beneficiaries, and return full value from the use and disposition of the trust property.

Id. at 235.

In County of Skamania vs. Washington, 685 P.2d 576 at 582 (Wash. 1984) a state statute which allowed purchasers of timber

from trust lands to default so as to avoid insolvency on the part of timber purchases was held unconstitutional.

In Alamo Land and Cattle Company vs. Arizona, 424 U.S. 295 at 305 (1976), the federal government condemned school trust lands including sections leased as grazing lands. Commenting on the validity of a school trust leasehold made for less than fair value, the court considered a protective provision contained in the New Mexico-Arizona Enabling Act which provided against the initial selling of lease rentals at less than fair value. The United States Supreme Court held that if the lease of trust lands was for a rental of substantially less than the land's then fair value, the lease was void.

The Courts consistently hold that entities, such as the Plaintiff, are charged with knowledge of the trust and are also subject to the duty to obtain full value for the trust. State vs. Phillips Petroleum Company, 258 P.2d 1193 at 1199 (Ok. 1953), State vs. Lamacus, 263 P.2d 426 at 427 (Ok. 1953), Seidel vs. Seward, 133 NW.2d 390 at 391 (Neb. 1965), State vs. Board of Educational Lands and Funds of Nebraska, 65 NW.2d 392 at 397 (Neb. 1954) and Department of State Lands vs. Pettibone, 702 P.2d 948 at 957 (Mont. 1985).

C. Trust Land Law And Policy Should Be Applied To The Facts Of This Case.

The State of Utah has the duty to receive full market value from the disposition of its school trust lands. The market royalty rate on coal leases in the State of Utah is controlled

by the United States which has the vast majority of coa reserves. Lessees require long-term leases because of the capital expenditures involved. It would have been an impermissible restriction on the trust assets if the State would have set a flat $.15 per ton royalty on its long term coal leases. Kadish vs. Arizona State Land Department, supra at 1195. It is equally impermissible for the court to judicially set the royalty rate at a flat $.15 per ton. The State therefore, drafted an escalator clause in its coal lease which tied the royalty provision to the prevailing federal rate. That escalator clause insured that the State would, throughout the term of the lease, receive full market value.

The State also implemented rules and regulations which provide for interest and penalties on delinquent royalty payments. Those provisions further insure that the trust receives full market value; otherwise, the trust would be depleted as a result of the time value of money. Bjork vs. April Industries, Inc., 560 P.2d 315 at 317 (Utah 1977).

The Plaintiff, as a party dealing with the trust and pursuant to the terms of the lease, had the duty to pay the correct amount of royalty. When an audit was performed by the State it showed that the Plaintiff owed to the trust fund in excess of three million dollars. (R.303) The trial court, by refusing to enforce the escalator provision of the lease, by refusing to require the payment of interest on delinquent

royalties, and by amending the lease to limit royalties to $.15 per ton imposed constitutionally impermissible restrictions on the trust fund. That decision, in this case, costs the trust fund, as of the audit, more than three million dollars with an ongoing loss of more than $2.00 per ton for coal produced after the audit. The contract created by the trial court runs directly counter to the law and public policy of this State. Thus, the court below is in the anomalous position of having written a contract which violates "the generally accepted doctrine of this country that every contract in violation of law is void." Baker vs. Latses, 60 Utah 38 at 44, 206 P.2d 533 at 555 (1922). See also, Haddock vs. Salt Lake City, 23 Utah 52, 65 P. 491 (1901) (holding void as against public policy a contract to pay fees for service of legal processes where the fees set in the contract were different from the fees set by statute); Boise-Payette Lumber Company vs. Challis Independent School District, No. 1 of Custer County, 46 Idaho 403, 268 P. 26 (1928) (holding that judicial determinations of public policy must recognize and yield to any applicable legislative enactments).

The instant case should be reversed and remanded to the trial court with instructions that the escalator clause be enforced and that the trust fund receive royalty rates at the prevailing market rate of 8% of the value of the coal removed together with interest as provided by the regulations.

POINT II. THE ESCALATION CLAUSE RELATING TO ROYALTIES IS CLEAR; THE REQUIREMENT THAT THE PLAINTIFF DETERMINE THE PREVAILING FEDERAL ROYALTY RATE DOES NOT MAKE THE CLAUSE AMBIGUOUS.

The Court, as a matter of law, is to give the provisions of a contract their plain meaning as ascertained from the instrument itself. The Court should look to the entire instrument and give meaning to all provisions. Utah Valley Bank vs. Tanner, 636 P.2d 1060 at 1061 (Utah 1981), Hal Taylor Associates vs. Union America, Inc., 657 P.2d 743 at 749 (Utah 1982). The trial court erred when it ignored the plain meaning of the royalty provision and the intent of the parties when entering into the contract and rewrote the lease deleting the escalator provision of the royalty clause.

A reading of the royalty provision in the lease (Article III Second) shows that it is clear and complies with the intent of the parties that the trust lands receive the going royalty rate. It states that the royalty rate will be $.15 per ton (which was the federal rate when the lease was signed) or if the prevailing federal rate increases on similar lands then the royalty rate increases to that new rate. The trial court was apparently under the misconception that because the escalator clause required the Plaintiff to determine the prevailing rate from facts outside the lease that somehow an ambiguity was created. Such a provision is not defective if there is a formula or method to set the price. Ferris vs. Jennings, 595 P.2d 857 at 359 (Utah 1979).

Escalator clauses in long-term mineral leases are common

provisions. Almost all escalator clauses or "favored nation" clauses require the parties to ascertain a fluctuating rate from facts outside the body of the lease. See e.g. Energy Reserves Group, Inc., vs. Kansas Power and Light Company, 459 U.S. 400 at 417 (1983), Amoco Production Company vs. Stauffer Chemical Company of Wyoming, 612 P.2d 463 at 468 (Wyo. 1980), Lonestar Gas Company vs. The Howard Corporation, 556 S.W.2d 372 at 376 (Tx. 1977). The ascertaining of facts outside the lease, to put into effect the lease provisions, does not create an ambiguity. Instead, such provisions are drafted to insure that rates, such as royalty rates, are tied to the market price thereby protecting both parties during the term of the lease.

The royalty provision contained in the contract provides a formula for fixing the payment price. Subsection (b) of the provision states that the royalty payment to be paid by the Plaintiff is determined by the prevailing federal rate on lands of similar character under coal leases issued by the federal government. Plaintiff had the duty to determine any change in the federal royalty rate. The Federal Coal Leasing Amendments Act of 1976 increased the royalty rate to 8% of the value of the coal produced on federal coal leases. The federal government owns the majority of coal reserves in Utah. Since 1979, 19 of 24 coal leases issued by the federal government in the State require a royalty payment of 8% of value. In addition, the adjoining states of Colorado, Wyoming and New Mexico have increased the

royalty rate to at least 8% of the value of coal produced under their leases. Plaintiff, in its Price River Complex, had seven federal leases which had been issued or adjusted since 1980. Six of those leases had an 8% royalty and one had a 10.4% royalty. Those facts when applied to the royalty provision require that a royalty rate of 8% of value be paid to the trust fund.

The plain meaning of the provision is that the royalty rate to be paid by the Plaintiff would change when the federal royalty rate increased. The Plaintiff does not argue that $.15 is the prevailing federal rate for federal leases of land of similar character and concede that the federal rate is higher than the royalty payment they paid prior to 1976. Plaintiff, to avoid paying the correct royalty, instead tries to claim the lease is ambiguous. A reading of the plain language of the lease, coupled with the law governing trust lands, and the change in federal royalty rates support only one construction of the lease. That construction is that the prevailing federal rate on underground coal leases has increased to 8% of value and that Plaintiff must pay royalties at that rate to provide full value to the trust.

POINT III. THE COURT ERRED WHEN IT IGNORED THE LAW REGARDING TRUST LANDS, THE ESCALATOR PROVISIONS OF THE LEASE, AND THE INTENT OF THE PARTIES, AND IMPOSED A FLAT $.15 PER TON ROYALTY RATE.

A. Any Ambiguous Provision Should Be Resolved By Rules Of Construction Instead Of Being Deleted From The Lease.

If the Court determines there is an ambiguity in the lease then the Court should apply certain rules of construction to interpret or clarify the ambiguous provision. The Court should not delete or rewrite the contract. Those rules of construction are: (1) the intent of the parties when entering into the contract controls the meaning of the contract, Utah Valley Bank vs. Tanner, supra at 1061; (2) existing law which affects the provision is considered part of the contract and governs its construction, Robinson vs. Joint School District, 596 P.2d 436 at 438 (Ida. 1979), Farmers Investment Company vs. Pima Mining Company, 523 P.2d 487 at 489 (Az. 1974); (3) consideration should be given to the subject matter, nature and purpose of the contract and the motives of the parties, Nagle vs. Club Fontainbleu, 405 P.2d 346 at 348 (Utah 1965); (4) the contract should be viewed from the perspective of the parties at the time it was signed, DeBouis vs. Nigh, 584 P.2d 823 at 824 (Utah 1978); (5) the court should give the entire contract meaning and not ignore any of the provisions of the contract or rewrite the contract, Hal Taylor Associates vs. Union America, Inc., 657 P.2d 743 at 749 (Utah 1982); and (6) the contract must be construed liberally to protect the public interest, Public Service Company

vs. Denver, 387 P.2d 33 at 36 (Colo. 1963), Restatement o Contracts 2d §207.

If these rules of construction are applied to the royalty provision, the interpretation given by the State is the correct and reasonable one. The State, as trustee, is required to have a royalty provision which provides a maximum value to the trust fund. A royalty rate that would fluctuate as market conditions changed is required. To have set a flat royalty rate would have been unconstitutional. Kadish vs. Arizona State Land Department, supra at 1195. The Federal Government owns the majority of coal reserves in the State of Utah; therefore, the royalty rate charged by the Federal Government constitutes the prevailing market rate in the State of Utah. At the time the lease provision was drafted the federal royalty rate was generally $.15 per ton. The royalty provision, therefore, was drafted setting a minimum royalty of $.15 per ton, but providing an escalator clause tied to the prevailing federal royalty rate. The escalator clause was required by law and the obvious intent of the parties when the contract was entered into was to provide a mechanism whereby the State would always receive the going market royalty rate from its trust lands. When one ties that information and construction to the undisputed facts it shows that the federal royalty rate remained at $.15 per ton until 1976. At that time the Federal Coal Leasing Amendments Act was passed and as a result the royalty rate on federal leases was

increased to 8%. The undisputed facts show that from 1979 to the present all newly issued federal leases in Utah, except for one, were at the rate of 8% or greater. The Director of State Lands properly construed the lease to require payment of royalties at 8%.

B. The Plaintiff Has Never Contended That The Royalty Should Always Remain At $.15 Per Ton.

One of the things that is certain about the royalty provision, in addition to the plain meaning of Subsection b, is that the contracting parties intended that the royalty rate would change if federal royalty rates increased. Plaintiff argues that the Court should look at past practices of the parties to determine the meaning of the royalty provision. The past practices of the parties are of no benefit at all in construing the meaning of the paragraphs involved in this case. The past practice of the parties, paying the rate specified under Subparagraph a, has nothing to do with Subparagraph b which surely must also be given effect. The contract must be construed to give effect to both provisions. Hal Taylor Associates vs. Union America, Inc., supra at 749. The obvious problem with Plaintiff's claim for interpretation of the royalty provision is that it ignores Subparagraph b. That is not interpretation, that is selective blindness.

Plaintiff does not argue that $.15 is the prevailing federal rate for federal leases on land of similar character under coal leases issued by the United States during the time period covered

by the audit. Its silence concedes that the rate is something higher than $.15. However, because Plaintiff does not like the higher rate, Plaintiff claims ambiguity and that it should be allowed to continue to pay at $.15 per ton as provided under Subparagraph a. This has nothing to do with the intent of either party at the time of the execution of the lease. Indeed, that so-called interpretation flatly contradicts the parties' intent at the time it was signed. In this particular case the undisputed facts establish that the prevailing federal rate is 8% of value which is the rate Plaintiff pays to the federal government on most of its other leases. Any changes in the rate can be easily determined by review of Bureau of Land Management records.

C. State Statutes Prohibit The Amending Of The Lease Without The Land Board's Approval.

There is a difference between construing a provision and ignoring it. To ignore and not enforce Subparagraph b of the royalty provision of the lease constitutes a rewriting of the terms of the lease without the necessary approval of the Director, the Land Board or the Attorney General. Morgan vs. Board of State Lands, 549 P.2d 695 at 697 (Utah 1976). Utah Code Ann. §65-1-76 requires:

> All leases and contracts of every kind entered into by the State Land Board shall before execution by such board be approved as to form by the attorney general.

§65-1-23 Utah Code Ann., requires:

> Except as otherwise provided by law, the State Land

> Board shall by rules and regulations prescribe the form of application, the form of lease, the annual rental, the amount of royalty and the basis upon which the royalty shall be computed, and such other details as it may deem necessary in the interest of the state.

The trial court should not be allowed to unilaterally rewrite the parties' lease. If there is an ambiguity, the trial court should be directed to apply proper rules of construction to clarify the ambiguity and give meaning to all of the royalty provisions.

POINT IV. ESTOPPEL IS NOT AVAILABLE IN THIS CASE.

The traditional rule is that the doctrine of estoppel cannot be asserted against a state government in matters affecting public policy, public revenues or when the state is acting in its governmental capacity. Estoppel is not applied in matters where an action is prohibited by a state statute or is the result of unauthorized acts of State officials. Atlantic Richfield Company vs. Hinkel, 432 F.2d 587 at 591 (10th Cir. 1970).

There are many good reasons for this rule including safeguarding public funds and interests which are subject to changes in political opinions and changes in public officials and employees. Utah State University vs. Sutro and Company, 646 P.2d 715 at 718 (Utah 1982). Restrictions on the application of legal doctrines when public lands are involved is common such as in the area of eminent domain, Utah Code Ann. §78-34-3 or adverse possession. There are even greater restrictions and protections when trust funds and trust lands are involved because of the constitutional requirements and important policies.

The trial court's ruling that the State was estopped from enforcing the royalty provisions of the lease was wrong for the following reasons: (a) the important policies and law governing trust lands prohibits the use of estoppel when the doctrine is used to diminish the income received by the trust fund; (b) the State acts in its governmental capacity when managing trust lands and is subject to estoppel in only limited circumstances; and (c)

the undisputed facts will not support a finding of estoppel.

A. The Important Policy Of Receiving Full Value For The Trust Fund Prohibits The Use Of Estoppel.

The trial court erred when it concluded that Defendants were estopped as a matter of law from enforcing the terms of the lease and obtaining full value for the trust fund. Courts which have considered whether estoppel should be applied when it would reduce the income to school trust lands have consistently held that the important public policy of providing full value to the trust lands prohibits the imposition of a defense such as estoppel.

In State vs. Phillips Petroleum Company, 258 P.2d 1193 (Ok. 1953) the clerk for the State failed to reserve minerals when issuing a certificate of purchase for land. The Court, in allowing reformation of the documents restoring the mineral rights to the State, held that the State was acting in a governmental capacity and that it would be a violation of the State's trust responsibilities to allow divestiture of the mineral rights. Furthermore, the court said that the purchaser is charged with notice that the State is acting as a trustee and is charged with notice that the State could only act in compliance with rules and regulations of its position as trustee. The Court held that the doctrine of estoppel did not apply to those acts which were beyond the authority of the State employee when he issued the deed and failed to reserve the mineral rights. Id. at 1199. The State employee in this case had no authority,

either intentionally or accidentally, to set a royalty rate lower than the prevailing federal rate.

In State vs. Northwest Magnesite Company, 182 P.2d 643 (Wash. 1947) the Commissioner of public lands promised the lessee of school trust lands that the lessee could remit royalties on the basis of net profits. That representation was contrary to the statute and the lease. The Court, in holding that the lessee was required to pay royalties in accordance with the terms of the lease, held that the State was acting in a governmental capacity, that estoppel could not be used to enforce the promise of the Commissioner of Public Lands, that Defendant's payment of money did not constitute an estoppel, and that the State was entitled to interest on the unpaid royalties. Id. at 662.

In the case of Department of State Lands vs. Pettibone, 702 P.2d 948 (Mont. 1985), Defendants claimed that they were entitled to certain water rights. The Montana Supreme Court denied Defendants' claim and found that the water rights were part of of the school trust lands of the State of Montana. The Court held that there were three important principals governing school trust lands. Those principals were: (1) the Enabling Act created a trust which the State could not violate; (2) the Enabling Act was to be strictly construed according to fiduciary principles; and (3) the Enabling Act pre-empted State laws and constitutions. It further held that Courts are to be very protective of the trust and emphatic of the need to preserve the value of the trust

corpus. The Court also found that an interest in State land cannot be conveyed without adequate compensation and that any use or management which would devalue State lands is impermissible. It said that anyone who acquires an interest in trust lands does so subject to the trust and that trust lands are subject to a different set of rules than other public lands. Id. at 956.

The holdings in the above cases are consistent with the manner in which this Court has decided issues involving estoppel against the State. The general rule in Utah is that an estoppel cannot be applied against the State if to do so would violate State statute. Utah State University vs. Sutro and Company, supra at 719. In the case at hand, the application of an estoppel would be a violation of both State statutes and the Constitution of Utah. Even if the Court determines that estoppel could apply, the Plaintiff must prove that estoppel is necessary to prevent manifest injustice and the public interest would not be unduly damaged by imposing the defense. Utah State University vs. Sutro and Company, 646 P.2d 715 at 718 (Utah 1982), Celebrity Club, Inc., vs. Utah Liquor Control Commission, 602 P.2d 689 at 694 (Utah 1979). In Utah State University vs. Sutro and Company the Court stated:

> [t]he rule which precludes the assertion of estoppel against the government is sound and generally should be applied, except only in appropriate circumstances as hereinabove stated, where the interest of justice mandates an exception to the general rule. In cases where such an issue arises, the critical inquiry is whether it appears that the facts may be found with sufficient certainty, and the injustice to be suffered

is of sufficient gravity, to invoke the exception. Id. at 720.

The essential policy and public interest in trust land cases is the requirement that the trust fund receive full value for its assets. To allow the application of estoppel in this case would defeat that purpose. As pointed out in Utah State University vs. Sutro and Company and Celebrity Club, Inc., vs. Utah Liquor Control Commission the doctrine of estoppel will not be applied when it would violate such an important public purpose. See also, Western Kane County Service District vs. Jackson Cattle Company, 744 P.2d 1376 at 1378 (Utah 1987) (reversing a ruling based on estoppel and stating "[w]e are extremely reluctant to apply the doctrine of estoppel against the assertion of rights in a public highway by a governmental entity").

In addition, there is no manifest injustice involved. An assertion of manifest injustice requires the Plaintiff to prove with certainty that paying royalties at $.15 per ton is a higher purpose than that of the trust fund receiving full value for its assets. Utah State University vs. Sutro and Company, supra at 718. The injustice in this case is the trial court's application of estoppel giving the Plaintiff a windfall at the expense of the school trust fund.

B. Estoppel Is Applicable Only In Very Limited Circumstances When The State Is Acting In Its Governmental Capacity.

The question of whether the State of Utah acted in its governmental or proprietary capacity when managing school trust lands was considered by the Utah Supreme Court in Duchesne County vs. State Tax Commission, 140 P.2d 335 (Utah 1943). This Court held:

> Here the trusteeship of the fund was vested in the State by the Enabling Act as a condition of statehood, as a condition to the right of the State to be born, and imposed upon the State at its birth by the instrument of its creation as a condition of its life as a government. It must therefore be held by the state in a governmental capacity.

Id. at 343.

This ruling is in line with rulings in other states which have considered the issue as well as the present case law of the State of Utah regarding the distinction between proprietary functions and governmental functions as to which the State retains its immunity. A governmental function has been defined as a function which is performed only by a government entity and is essential to the core of governmental activity. Cox vs. Utah Land and Mortgage Corporation, 716 P.2d 783 at 785 (Utah 1986), Metropolitan Financial Company vs. State, 714 P.2d 293 at 294 (Utah 1986). The Utah Legislature has recently expanded that definition to include non-essential as well as essential governmental activities. Utah Code Ann. §63-30-2(4)(a). The management of school trust lands is an obligation imposed upon

the State by a federal statute and accepted by the Utah Constitution. It is an activity that can only be performed by the State.

As already established, the Court must be extremely reluctant to apply estoppel when the State is acting in its governmental capacity. When public lands are involved, still more restrictive rules govern. For example, adverse possession cannot be applied against public lands. Peterson vs. Johnson, 34 P.2d 697 at 698 (Utah 1934). Great protection is given to trust lands because doctrines such as estoppel or adverse possession defeat constitutional requirements to receive full value for the trust and violate the State's governmental powers. Department of State Lands vs. Pettibone, supra at 952.

It is hard to imagine any other act of the State which would be more governmental in nature than the trust responsibilities imposed by the Enabling Act and accepted by the State in its Constitution and as a requirement to obtain statehood. Estoppel cannot be used to prevent the State from functioning in this important government capacity.

C. The Undisputed Facts Do Not Support A Finding Of Estoppel.

The trial court erred when it concluded that the State was estopped from collecting delinquent royalty payments. Its finding that the Plaintiff had relied on the State's lack of protest and had mined the coal in reliance upon a royalty rate of $.15 per ton was wrong. The facts upon which reliance and

detriment could correctly be founded were disputed by the Defendants. Indeed, the undisputed facts showed that it was the State that relied on the Plaintiff to pay the correct royalty amount. The Plaintiff had the duty to the State to calculate and pay the correct royalty. The State did not have a duty to Plaintiff to collect the correct royalty although it has such a duty to the school trust.

If the doctrine of estoppel were applicable in this case the Plaintiff must prove: (1) a false representation or concealment of a material fact; (2) made with knowledge of the facts; (3) made to a party without knowledge or the means of knowledge of the real facts; (4) made with the intention that the representation be acted upon; and (5) the parties to whom the representation was made, relied or acted upon is injured. Colman vs. Colman, 743 P.2d 782 at 790 (Utah 1987).

One is not entitled to rely on erroneous or unauthorized statements of a government employee. Dansie vs. Murray City, 560 P.2d 1123 at 1124 (Utah 1977), Atlantic Richfield vs. Hickel, supra at 591. If a person has the means to determine the actual facts estoppel does not apply. Morgan vs. Board of State Lands, supra. To claim estoppel against the government, the injury must be substantial. Paying what is owed under the lease is not an injury. Barnes vs. Wood, 750 P.2d 1226 (Utah 1988); Williams vs. PSC, 754 P.2d 41 (Utah 1988); and Utah Department of Transportation vs. Reagan Outdoor Advertising, Inc., 751 P.2d

270 (Utah Ct. App. 1988).

The undisputed facts will not support a finding of estoppel. It was the Plaintiff who was responsible to correctly report the royalty rate and payments. It was the Plaintiff who had substantial dealings with the federal government and who was aware of the increase in the federal royalty rate (R.397-399) and it was the State that relied on the Plaintiff to accurately report and accurately pay the correct royalty amount. (R.433) The undisputed facts support a finding of estoppel against the Plaintiff and not in favor of the Plaintiff.

Plaintiff claimed that the discussions between the parties regarding the lease adjustment and the failure of the State to require adjustment in 1981 operated as an estoppel. Adjustment of the lease is a separate matter provided for in the recital clause of the lease. It has no bearing on the meaning and enforcement of Article III which contains the royalty provisions. After a hearing on July 8, 1981, the State Land Board ordered that certain provisions of the lease be adjusted including increasing the royalty rate initially to 4% and after 5 years to 8%. (R.280) The Land Board, at the request of Plaintiff, agreed to delay implementation of the adjustment until the law was settled on whether the request for adjustment was timely. Plaintiff ceased production in 1983 before those issues were finally resolved. These facts do not support estoppel but rather show that Plaintiff knew that the royalty rate had increased and

that the Land Board felt that Plaintiff should, in fairness to the trust, pay a higher royalty rate.

Plaintiff also claims it would have not have mined the State coal lease if the royalty rate had been increased and alleges that it will incur a loss if required to pay the increased royalty rate. Defendants disputed those allegations. Plaintiff listed on its books a royalty of $1.10 per ton while only paying the State $.15 ton. (R.400) All costs are passed on by Plaintiff to its parent companies and eventually the utilities and consumers in the Midwest. Journal of Energy Law, Vol. 8, An Economic Analysis of Utility - Coal Company Relationship's (1987); In re Indiana and Michigan Electric Company, 40 P.U.R. 4th 537 (Indiana Public Service Comm. 1981). Also during the time period in question, Plaintiff was entering into leases with the Federal Government for lands in the same mine complex and was paying 8% royalties on those leases. (R.396) Plaintiff will only be required to pay what the lease requires. Such does not constitute injury. Barnes vs. Wood, supra, Williams vs. PSC, supra. If this Court determines that the doctrine of estoppel could apply in this case, then the matter should be remanded to the trial court for trial with Plaintiff having the burden to prove it has met the elements required for estoppel.

CONCLUSION

The law requires that the State of Utah receive a maximum return on its disposition of school trust lands. The State implemented that requirement by linking the royalty rate on the lease to the prevailing federal royalty rate. The decision of the trial court imposes improper restrictions on the trust lands. The State asks this Court to reverse the decision of the trial court and remand the case with instructions to enter judgment in favor of the State of Utah upholding the decision of the Director of State Lands.

Respectfully submitted this 20 day of July, 1988.

NIELSEN & SENIOR
Attorneys for Appellant

By: _____
Clark B. Allred

By: _____
Gayle F. McKeachnie

ADDENDUM

IN THE SEVENTH JUDICIAL DISTRICT COURT FOR CARBON COUNTY
STATE OF UTAH

BLACKHAWK COAL COMPANY, Plaintiff, vs. THE UTAH DIVISION OF STATE LANDS AND FORESTRY, RALPH MILES, DIRECTOR OF THE DIVISION OF STATE LANDS AND FORESTRY, THE UTAH BOARD OF STATE LANDS AND FORESTRY, THE UTAH DEPARTMENT OF NATURAL RESOURCES, DEE HANSEN, EXECUTIVE DIRECTOR OF THE UTAH DEPARTMENT OF NATURAL RESOURCES, Defendants.	MEMORANDUM DECISION ON MOTION FOR PARTIAL SUMMARY JUDGMENT Civil No. 14943

The plaintiff has moved the Court for partial summary judgment and has supported the same by their Memorandum of Legal Points and Authorities, Affidavits and supporting documents. The defendants have objected to the Motion and have filed their Memorandum of Legal Points and Authorities and supporting documents and Affidavits. The Court finds that there is no dispute as to the material facts in this case and has concluded therefrom that the plaintiff is entitled to partial summary judgment as prayed for and grants the plaintiff's Motion.

The factual situation is nearly identical to the fact situation as shown in Carbon Case No. 14890, Plateau Mining Company v. The Division of State Lands and Forestry, et al.,

and the Court has attached hereto a copy of its opinion in that case to show the reasoning of the Court and the legal analysis used by the Court in reaching its decision in this case.

The factual situation in this case is more supportive of plaintiff's motion than were the facts in the Plateau Mining case in that there was an attempt by the defendants to renegotiate the lease in question to a percentage of gross value of coal produced in 1981. That attempt was never pursued by defendants and even withdrawn in January of 1982. Plaintiff, at that time, was informed by John T. Blake, Mineral Resources Specialist of the State of Utah, Natural Resources and Energy Department, Division of State Lands and Forestry, as follows: "Should Blackhawk Coal Company choose to reject my invitation for lease adjustment, they may continue to operate under the original Lease Agreement until otherwise advised."

The plaintiff responded in a letter to Mr. Blake on January 7, 1982, as follows: "Blackhawk will continue to pay to the State, on a quarterly basis, the royalty of $.15 per ton in compliance with Article III(a) of the original Lease Agreement, since the provisions of Article III(b) of this Agreement are inapplicable at the present time."

Thereafter, plaintiff paid and defendant accepted without comment or objection the $.15 a ton in accordance with Article III(a) of the Lease.

The attorney for the plaintiff is directed to prepare a formal judgment in accordance with this decision.

DATED this 21ST day of April, 1988.

BOYD BUNNELL, District Judge

IN THE SEVENTH JUDICIAL DISTRICT COURT FOR CARBON COUNTY
STATE OF UTAH

PLATEAU MINING COMPANY, a Delaware Corporation, and CYPRUS WESTERN COAL EQUIPMENT COMPANY, a Delaware Corporation, Plaintiffs, vs. THE UTAH DIVISION OF STATE LANDS AND FORESTRY; RALPH MILES, DIRECTOR OF THE DIVISION OF STATE LANDS AND FORESTRY; THE UTAH BOARD OF STATE LANDS AND FORESTRY; THE UTAH DEPARTMENT OF NATURAL RESOURCES; DEE HANSEN, EXECUTIVE DIRECTOR OF THE UTAH DEPARTMENT OF NATURAL RESOURCES, Defendants.	MEMORANDUM DECISION ON MOTIONS FOR SUMMARY JUDGMENT Civil No. 14890

The plaintiff seeks a partial summary judgment from the Court declaring that the royalty provision contained in the State Lease of the defendants is ambiguous and that it should be construed in light of the parties course of performance; that the lease is not self-executing so as to place a legal obligation on plaintiffs to pay a higher rate of royalty after the State accepted without qualification the payment of the stated rate of $.15 per ton of coal produced; that the defendants may not retroactively apply their new policy imposing a royalty rate of 8%; that the defendants are estopped

from demanding payment of royalties on coal mined during the audit period at a rate higher than that paid by plaintiffs and accepted by defendants; that the defendants have waived their right to demand a higher royalty rate than the one accepted during the audit period; and that the ruling of the State relative to imposing interest and penalties cannot be legally enforced.

The defendants have objected to the granting of the Motion and have submitted their own Motion for Summary Judgment asking the Court to dismiss the Complaint for failure to state a cause of action; ordering the plaintiff, Plateau Mining Company, to pay the delinquent royalty payment as determined on the basis of 8% of gross sales value during the audit period; ordering that the plaintiff, Plateau Mining Company, owes interest on delinquent royalty payments at a rate set by the Board of State Lands and, further, ordering that the plaintiff, Plateau Mining Company, owes penalties on delinquent royalties pursuant to the regulation set by the Board.

Each of the parties have submitted their Memorandums of Legal Points and Authorities and have presented to the Court Affidavits and Exhibits which the Court has read and considered and the Court heard oral arguments from the parties on February 16, 1988, and took this matter under advisement and rules on the Motions as hereinafter stated.

Certain undisputed facts are, for the most part, agreed upon by the parties as set forth in their respective memorandums, and the Court will not attempt to detail all of those undisputed facts. There is no dispute as to the fact that the plaintiff, Plateau, and their predecessors in interest mined coal under a lease from the State of Utah during the period April 1, 1979, to December 31, 1984, referred to as the "audit period"; that the Lease was entered into on March 15, 1965, and that the Lease provides as follows:

> "Article III, Second: To pay to Lessor quarterly, on or before the 15th day of the month succeeding each quarter, royalty
>
> (a) at the rate of 15¢ per ton of 2000 lbs of coal produced from the leased premises and sold or otherwise disposed of, or
>
> (b) at the rate prevailing at the beginning of the quarter for which payment is being made, for federal leases of land of similar character under coal leases issued by the United States at that time,
>
> whichever is higher. . . ."

That the lease was on a standard form provided by and prepared by the State Land Board, and that throughout the audit period the plaintiff, Plateau, or their predecessors in interests, filed quarterly with the lessor (State) on a form provided by the State a report of the coal mined under the Lease and a calculation of the royalty due on the basis of 15¢ per ton. The payment was received and retained by the State without question or objection throughout the audit period and prior thereto from sometime in 1965.

The royalty reporting form was provided by the Utah Board of State Lands and under the title Royalty Data it has two columns. One is headed ¢/T Basis, and the other is headed Percentage Basis. Plateau and their predecessors in interest filled in the column entitled ¢/T Basis and paid the amount of royalty shown to be due under that column at 15¢ per ton and left the other column blank.

After the term of the lease had expired, December 1984, in approximately February of 1985, the State undertook, for the first time, an audit of the royalty payments. The audit was completed on or about May 29, 1985, and a demand was sent to the plaintiffs for delinquent royalties in October of 1985.

It was the conclusion of the audit that the federal government, during the audit period, was imposing a royalty on coal leases of 8% of the value of the coal removed. Based upon the audit, the State made a demand upon the plaintiffs for the payment of an additional $2,991,613.44 for delinquent royalties, interest and penalties based upon 8% of Gross Sales Value of coal removed.

Based upon an examination of the Lease and the parties attempts to comply with its terms, and particularly the expressed attitude of the various individuals whose responsibility it was to enforce the Lease for and on behalf of

the State, the Court finds that as a matter of law the royalty provision as contained in Article III, paragraph Second (b) of the lease is ambiguous.

The royalty provision is divided into two parts. Part (a) is definite and precise and is capable of definitive determination and provides for 15¢ per ton on coal produced from the leased premises.

Part (b) leaves the amount due based on several factors not immediately capable of definitive determination. The ambiguity arises as much from what is not stated and provided as from what is stated. In other words, at the beginning of the reporting quarter what is the prevailing federal rate and who makes that determination, the lessor or the lessee, and what factors are to be included in making a determination as what federal rate prevails and in what area is it prevalent? Who makes the determination that the land in the State Lease and the land in the Federal Lease are similar in character and what is the basis for determining similarity? What time period is used to determine federal leases "issued... at that time" and who makes that determination? Even if a prevailing federal rate is established, does it apply to the "value of the coal removed" as stated in the federal regulation or to the "gross sales value" as used by the State auditor in his assessment, and who makes that determination?

For these reasons, the Court has concluded that sub-paragraph (b) is not self-executing as to create a legal obligation on the lessee since the identifiable factors necessary for self-execution could not independently be ascertained by either party.

Sub-paragraph (b) was written by the State for its benefit and since it is not self-executing, it would require some affirmitive action on their part to bring the provision of that sub-paragraph into an enforceable position other than a retroactive audit after having accepted the provisions of sub-paragraph (a) without objection or comment.

Under these circumstances, the Court must look to the prior conduct of the lessor and the lessees under the Lease over a period of years that show that they chose to ingnore the provisions of sub-paragraph (b), and to calculate the royalty under sub-paragraph (a).

Since the State by an established course of conduct for many years adopted a construction of the Lease that provided for 15¢ a ton, they are now precluded from asserting a different construction of the Lease where they took no sufficient or positive action to establish their now asserted construction to an ambiguous lease provision.

Because of the above legal conclusion, it would not be necessary for the Court to go further, but as a further

ground for what the Court's final conclusion and ruling will be, the Court will address other issues presented.

The Court is of the opinion that regardless of whether the status of the land is School Trust Land or not, the State acts in its proprietary capacity when it enters into a contractual lease that is authorized under law and that the doctrine of equitable estoppel may be applied against the State and its Land Board as any other contracting individual.

The Court has concluded as a matter of law that the State is estopped from demanding payment of royalty based upon the 8% of value figure. The undisputed facts show that the State was aware of the provisions of sub-paragraph (b) of Article III of their own Lease and were made aware by the quarterly payments submitted by Plateau and its predecessors in interest that those provisions were being ignored by leaving that reporting column blank and by accepting, throughout the auditing period, without question or objection, royalty based upon 15¢ a ton. If the provisions of sub-paragraph (b) were going to be used, the State had a duty to speak which they did not do. By their conduct and failure to perform this duty, they induced plaintiffs to believe that 15¢ a ton was the acceptable royalty and plaintiffs, in reliance thereon, continued to mine coal under the Lease which they would not have done had they known that the defendants were going to

insist upon the 8% of value provision. The great injustice that would result to plaintiffs if we now allow the defendants to assert this position, is quite obvious since the record shows that to allow the imposition of the greater royalty, the plaintiffs would show a substantial loss on all mining activity under the State Lease.

Even if the conclusion is reached that the defendants were acting in a governmental capacity, they would still be estopped from asserting the new royalty rate. No substantial adverse effect on public policy will result if the defendants are estopped from applying this newly determined royalty retroactively. The State can still proceed to lease coal lands on any terms it feels profitable and that will give the State the maximum return. They still have the power to revise the wording of their coal leases to do away with any ambiguity and to carry out any legally established policy.

Further, the record shows that the plaintiffs would not have entered into certain stock purchases and transfers on the terms that were then agreed to had they known of the State's position and the contemplated change in the royalty provision as previously accepted, and that the plaintiffs would suffer at this time great economic loss as a result.

The Court further finds that the State had no right under the Lease to impose interest, except on delinquent

payments at the legal rate, or any penalty. A legally binding lease cannot be altered or added to by by rules and regulations adopted subsequently.

The Lease does state that it is subject to such operating rules and regulations as may be hereafter approved and adopted. Such a provision could not be interpreted to mean changes to or additions of monetary payment. "Operating Rules" has reference to method of mining and can have no other logical interpretation. Since the amount claimed by the State is not subject to definitive determination, any interest that may be due could not commence to run until demand is made.

For the reasons stated above, the Court grants plaintiffs' Motion for Partial Summary Judgment as prayed for and denies defendants' Motion for Summary Judgment.

The attorney for the plaintiff is directed to prepare a formal order in accordance with this opinion.

DATED this 24th day of February, 1988.

BOYD BUNNELL, District Judge

CERTIFICATE OF MAILING

I hereby certify that I mailed true and correct copies of the foregoing MEMORANDUM DECISION ON MOTION FOR PARTIAL SUMMARY JUDGMENT by depositing the same in the United States Mail, postage prepaid, to the following:

Clark B. Allred
Gayle F. McKeachnie
NIELSEN & SENIOR
Special Assistant Attorney General
363 East Main Street
Vernal, Utah 84078

David L. Wilkinson
UTAH STATE ATTORNEY GENERAL
David S. Christensen
ASSISTANT ATTORNEY GENERAL
124 State Capitol
Salt Lake City, Utah 84114

Hugh C. Garner
HUGH C. GARNER & ASSOCIATES, P.C.
Attorneys at Law
136 South Main Street, Suite 700
Salt Lake City, Utah 84101

A. John Davis
PRUITTT, GUSHEE & FLETCHER
Attorneys at Law
36 South State Street, Suite 1800
Salt Lake City, Utah 84111

DATED this 21st day of April, 1988.

Administrative Secretary

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Attorneys for Plaintiff

IN THE SEVENTH JUDICIAL DISTRICT COURT OF CARBON COUNTY

STATE OF UTAH

BLACKHAWK COAL COMPANY, Plaintiff, v. THE UTAH DIVISION OF STATE LANDS AND FORESTRY, RALPH MILES, Director of the Division of State Lands and Forestry, THE UTAH BOARD OF STATE LANDS AND FORESTRY, THE UTAH DEPARTMENT OF NATURAL RESOURCES, DEE HANSEN, Executive Director of the Utah Department of Natural Resources, Defendants.	JUDGMENT Civil No. 14943

Plaintiff has filed its Motion for Partial Summary Judgment, together with its Supporting Memorandum of Points and Authorities; Defendants have filed their Memorandum in

Opposition to Plaintiff's Motion. Plaintiff is represented by Hugh C. Garner; Defendants are represented by their counsel Gayle F. McKeachnie and Clark B. Allred. The court having considered the memoranda and exhibits submitted by the parties and having previously, on April 21, 1988, issued its Memorandum Decision on Motion for Partial Summary Judgment,

NOW THEREFORE, HEREBY ORDERS, ADJUDGES AND DECREES as follows:

1. Plaintiff owes no royalties, penalties or interest to Defendants on State of Utah coal lease No. ML-18148 as demanded in Defendants' October 15, 1985 Royalty Audit Report.

2, The judgment signed by this court in this case is a final order and judgment from which an appeal may proceed.

3. Each party shall bear its own costs and attorneys' fees in connection with this case.

DATED this 11th day of ~~April~~ May, 1988.

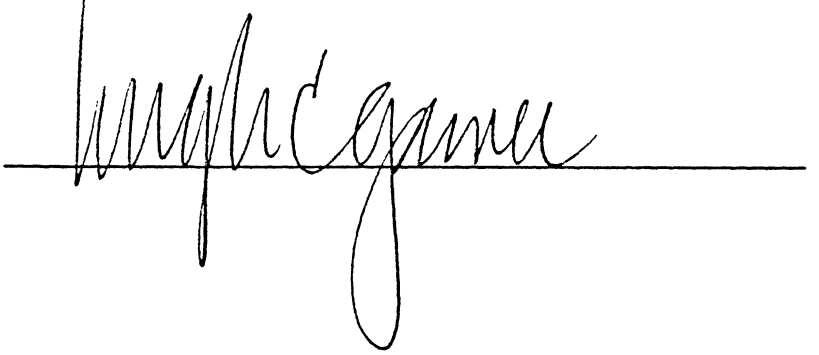
BY THE COURT:

BOYD BUNNELL
District Court Judge

The above judgment was prepared by Hugh C. Garner of and for Hugh C. Garner & Associates, P.C., attorney for Plaintiff, and was, prior to execution by the court and pursuant to Rule 2.9, Rules of Practice in the District Courts and Circuit Courts of the State of Utah, submitted to the following on this 26th day of April, 1988.

David L. Wilkinson, Esq.
David S. Christensen, Esq.
124 State Capitol
Salt Lake City, Utah 84114

Gayle F. McKeachnie, Esq.
Clark B. Allred, Esq.
Nielsen & Senior
363 East Main Street
Vernal, Utah 84078



MINERAL LEASE APPLICATION

MINERAL LEASE NO. 18148

GRANT: School

NO. 1618

Utah State Lease for

COAL

THIS INDENTURE OF LEASE AND AGREEMENT entered into in duplicate this 16th day of February, 1960, by and between the STATE LAND BOARD, acting in behalf of the State of Utah, hereinafter called the Lessor, and

CARBON DEVELOPMENT COMPANY
P. O. Box 506
Helper, Utah

party of the second part, hereinafter called the Lessee, under and Pursuant to Title 65, Utah Code Annotated, 1953.

WITNESSETH: That the Lessor, in consideration of the rents and royalties to be paid and the covenants to be observed by the Lessee, as hereinafter set forth, does hereby grant and lease to the Lessee the exclusive right and privilege to mine, remove, and dispose of all of the said minerals in, upon, or under the following described tract of land situated in Carbon County, State of Utah, to-wit:

All of Section Thirty-two (32), Township Twelve (12) South, Range Nine (9) East, Salt Lake Meridian,

containing a total of 640.00 acres, more or less, together with the right to use and occupy so much of the surface of said land as may be required for all purposes reasonably incident to the mining, removal, and disposal of said minerals, according to the provisions of this lease, for the period ending ten years after the first day of January next succeeding the date hereof and as long thereafter as said minerals may be produced in commercial quantities from said lands, or Lessee shall continue to make the payments required by Article III hereof, upon condition that at the end of each twenty (20) year period succeeding the first day of the year in which this lease is issued, such readjustment of terms and conditions may be made as the Lessor may determine to be necessary in the interest of the State.

ARTICLE I

This lease is granted subject in all respects to and under the conditions of the laws of the State of Utah and existing rules and regulations and such operating rules and regulations as may be hereafter approved and adopted by the State Land Board.

ARTICLE II

This lease covers only the mining, removal, and disposal of the minerals specified in this lease, but the Lessee shall promptly notify the the Lessor of the discovery of any minerals excepting those enumerated herein.

ARTICLE III

The Lessee, in consideration of the granting of the rights and privileges aforesaid, hereby covenants and agrees as follows:

FIRST: To pay to the Lessor as rental for the land covered by this lease the sum of fifty (50) cents per acre per annum. All such annual payments of rental shall be made in advance on the 2nd day of January of each year, except the 1960 rental which is payable on the execution of this lease. All rentals shall be credited against royalties for the year in which they accrue.

SECOND: To pay to Lessor quarterly, on or before the 15th day of the month succeeding each quarter, royalty

(a) at the rate of 15¢ per ton of 2000 lbs. of coal produced from the leased premises and otherwise disposed of, or

(b) at the rate prevailing, at the beginning of the quarter for which payment is being made, for federal lessees of land of similar character under coal leases issued by the United States at that time,

whichever is higher, and, commencing with the year beginning the January 1 following two years from the date hereof, to pay annual royalty of at least $1.00 multiplied by the number of acres hereby leased regardless of actual production, provided that Lessor may, at any time after the tenth anniversary date hereof, increase the minimum annual royalty by not to exceed 50%.

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THIRD: To prepare and forward to the State Land Office, on or before the 15th day of the month next succeeding the quarter in which the material is produced, a certified statement of the amount of production of all of the leased substances disposed of from said lands, and such other additional information as the State Land Board may from time to time require.

FOURTH: To keep at the mine office clear, accurate and detailed maps on tracing cloth, on a scale not more than 50 feet to the inch, of the workings in each section of the leased lands and on the lands adjacent, said maps to be coordinated with reference to a public land corner so that they can be readily and correctly superimposed, and to furnish to the Lessor annually, or upon demand, certified copies of such maps and such written statements of operations as may be called for. All surveys shall be made by a licensed engineer and all maps certified to by him.

FIFTH: Not to fence or otherwise make inaccessible to stock any watering place on the premises without first obtaining the written consent of Lessor, nor to permit or contribute to the pollution of any surface or subsurface water available or capable of being made available for domestic or irrigation use.

SIXTH: Not to assign this lease or any interest therein, nor sublet any portion of the leased premises, or any of the rights and privileges herein granted, without the written consent of the Lessor being first had and obtained.

ARTICLE IV

The Lessor hereby excepts and reserves from the operation of this lease:

FIRST: The right to permit for joint or several use such easements or rights-of-way upon, through, or in the land hereby leased as may be necessary or appropriate to the working of these or other lands belonging to or administered by the Lessor containing mineral deposits or for other use.

SECOND: The right to use, lease, sell, or otherwise dispose of the surface of said lands or any part thereof, under existing State laws or laws hereafter enacted, insofar as said surface is not necessary for the Lessee in the mining, removal, or disposal of the leased substances therein, and to lease mineral deposits, other than those leased hereby, which may be contained in said lands so long as the recovery of such deposits does not unreasonably interfere with Lessee's rights herein granted.

ARTICLE V

Upon failure or refusal of the Lessee to accept the readjustment of terms and conditions demanded by the Lessor at the end of any twenty-year period, such failure or refusal shall work a forfeiture of the lease and the same shall be canceled.

ARTICLE VI

In case of expiration, forfeiture, surrender or other termination of this lease, all underground timbering supports, shaft linings, rails and other installations necessary for the support of underground workings of any mines, and all rails or head frames and all installations which cannot be removed without permanent injury to the premises and all construction and equipment installed underground to provide ventilation for any mines, upon or in the said lands shall be and remain a part of the realty and shall revert to the Lessor without further consideration or compensation and shall be left by the Lessee in the lands.

All personal property of Lessee located within or upon the said lands, and all buildings, machinery, equipment and tools (other than the installations to become the property of Lessor as above provided), shall be and remain the property of Lessee and Lessee shall be entitled to, and may, within six (6) months after such expiration, forfeiture, surrender or other termination of said lease, or within such extension of time as may be granted by Lessor, remove from the said lands such personal property and improvements, other than these items which are to remain the property of the Lessor as above provided.

Lessee shall, upon termination, of this lease or abandonment of the leased premise for any reason, seal to Lessor's satisfaction all or such part of the mine openings on the premises as Lessor shall request be sealed.

ARTICLE VII

It shall be the responsibility of the Lessee to slope the sides of all operations of a surface nature to an angle of not less than 45° or to erect a barrier around such operation as the State Land Board may require. Such sloping or fencing shall become a normal part of the operation of the lease so as to keep pace with such operation to the extent that such operation shall not constitute a hazard.

ARTICLE VIII

Lessee shall not sell or otherwise dispose of any water rights acquired for use upon the leased premises except with Lessor's written permission. Upon termination of this lease for any reason, all such rights acquired by application to the Utah State Engineer shall revert to the Lessor as an appurtenance to the leased premises, and all such rights acquired by other means shall be offered to Lessor in writing for purchase at Lessee's acquisition costs, provided that Lessor shall be deemed to have rejected such offer if it does not accept the same within thirty days after receipt thereof.

ARTICLE IX

All of the terms, covenants, conditions, and obligations in this lease contained, shall be binding upon the heirs, executors, administrators, and assigns of the Lessee.

ARTICLE X

Lessee may terminate this lease at any time upon giving three (3) months' notice in writing to the Lessor and upon payment of all rents and royalties and other sums due and payable to the Lessor, and upon complying with the terms of this lease with respect to the preservation of the workings in such order and condition as to permit of the continued operation of the leased premises.

ARTICLE XI

Lessor, its officers and agents, shall have the right at all times to go in and upon the leased lands and premises, during the term of said lease to inspect the work done and the progress thereof on said lands and the products obtained therefrom, and to post any notices on the said land that it may deem fit and proper; and also shall permit any authorized representatives of the Lessor to examine all books and records pertaining to operations under this lease, and to make copies of and extracts from the same, if desired.

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ARTICLE XII

This lease is issued only under such title as the State of Utah may now hold, and that in the event the State is hereafter divested of title, the Lessee shall not be liable for any damages sustained by the Lessee, nor shall the Lessee be entitled to or claim any refund of royalties or rentals or other monies theretofore paid to the Lessor.

If the Lessee shall initiate or establish any water right for the leased premises, such right shall become an appurtenance of the leased premises, and, upon the termination of the lease, the Lessee shall convey the right to the Lessor.

STATE OF UTAH
STATE LAND BOARD

By ..... DIRECTOR

LESSOR

Leland D. Quinn Jr.

CARBON DEVELOPMENT COMPANY, a Corporation

By: ..... President

LESSEE

STATE OF UTAH
COUNTY OF } ss. LESSEE'S INDIVIDUAL ACKNOWLEDGEMENT

On the ..... day of ..... 19....., personally appeared before me .....

the signer of the above instrument, who duly acknowledged to me that ..... executed the same.

Given under my hand and seal this ..... day of ..... 19.....

My commission Expires:

..... *Notary Public, residing at:*

STATE OF UTAH
COUNTY OF CARBON } ss. LESSEE'S CORPORATE ACKNOWLEDGEMENT

On the 10th day of March 19 60, personally appeared before me James J. Diamanti

who being duly sworn did say that he is an officer of Carbon Development Company and that said instrument was signed in behalf of said corporation by resolution of its Board of Directors, and said James J. Diamanti acknowledged to me that said corporation executed the same.

Given under my hand and seal this 10th day of March 19 60

My commission Expires:
2/9/60

Notary Public, residing at: Helper, Utah

STATE OF UTAH
COUNTY OF SALT LAKE } ss.

On the 23 day of March 19 60, personally appeared before me Frank J. Allen, who being by me duly sworn did say that he is the Director of the State Land Board of the State of Utah and that said instrument was signed in behalf of said Board by resolution of the Board, and said Frank J. Allen acknowledged to me that said Board executed the same in behalf of the State of Utah.

Given under my hand and seal this 23 day of March 19 60

My commission Expires: 8/14/62

..... *Notary Public, residing at:*

MAILING CERTIFICATE

I hereby certify that I mailed four true and correct copies of the foregoing Brief of Appellants to Hugh C. Garner, HUGH C. GARNER & ASSOCIATES, 136 South Main Street, Suite 700, Salt Lake City, Utah 84101 and A. John Davis, PRUITT, GUSHEE & FLETCHER, 363 South State Street, Suite 1850, Salt Lake City, Utah 84111 on this 20 day of July, 1988.

Clark B. Allred