IN THE SUPREME COURT FOR THE STATE OF ALASKA

MONTE J. ALLEN and DANIEL K. DONKEL, Appellants, vs. ALASKA DEPARTMENT OF NATURAL RESOURCES, DIVISION OF OIL & GAS, Appellee.	)	Supreme Court Case No. S-13096

Trial Court Case Nos. 3AN-05-09272 CI
& 3AN-06-8419 CI Consolidated

APPEAL FROM THE SUPERIOR COURT,
THIRD JUDICIAL DISTRICT AT ANCHORAGE,
THE HONORABLE CRAIG STOWERS, PRESIDING

BRIEF OF APPELLANTS MONTE J. ALLEN AND DANIEL K. DONKEL

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AUTHORITIES PRINCIPALLY RELIED UPON

ALASKA CONSTITUTION:

Article I, Section 7. Due Process

No person shall be deprived of life, liberty, or property, without due process of law. The right of all persons to fair and just treatment in the course of legislative and executive investigations shall not be infringed.

UNITED STATES CONSTITUTION:

Amendment V. Rights of Persons

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

Amendment XIV, Section 1. Rights Guaranteed: Due Process

All persons born or naturalized in the United States and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

ALASKA STATUTES:

Sec. 22.05.010. Jurisdiction.

(a) The supreme court has final appellate jurisdiction in all actions and proceedings. However, a party has only one appeal as a matter of right from an action or proceeding commenced in either the district court or the superior court.

(b) Appeal to the supreme court is a matter of right only in those actions and proceedings from which there is no right of appeal to the court of appeals under AS 22.07.020 or to the superior court under AS 22.10.020 or AS 22.15.240.

(c) A decision of the superior court on an appeal from an administrative agency decision may be appealed to the supreme court as a matter of right.

(d) The supreme court may in its discretion review a final decision of the court of appeals on application of a party under AS 22.07.030. The supreme court may in its discretion review a final decision of the superior court on an appeal of a civil case commenced in the district court. In this subsection "final decision" means a decision or order, other than a dismissal by consent of all parties, that closes a matter in the court of appeals or the superior court, as applicable.

(e) The supreme court may issue injunctions, writs, and all other process necessary to the complete exercise of its jurisdiction.

ALASKA ADMINISTRATIVE CODE:

11 AAC 02.050. Hearings.

(a) The department will, in its discretion, hold a hearing when questions of fact must be resolved.

(b) The hearing procedure will be determined by the department on a case-by-case basis. As provided in 11 AAC 02.030(a)(13), any request for special procedures must be included with the request for a hearing.

(c) In a hearing held under this section

(1) formal rules of evidence need not apply; and

(2) the hearing will be recorded, and may be transcribed at the request and expense of the party requesting the transcript.

11 AAC 88.185. Definitions.

As used in 11 AAC 82 - 11 AAC 88 and unless the context clearly requires a different meaning or unless otherwise defined in these chapters,

(32) "working interest" means the interest held in lands by virtue of a lease, operating agreement, fee title or otherwise, under which the owner of the interest is vested with the right to explore for, develop and produce minerals; the right delegated to a unit operator by a unit agreement is not a working interest;

11 AAC 83.303. Criteria.

(a) The commissioner will approve a proposed unit agreement for state oil and gas leases if he makes a written finding that the agreement is necessary or advisable to protect the public interest considering the provisions of AS 38.05.180(p) and this section. The commissioner will approve a proposed unit agreement upon a written finding that it will

(1) promote conservation of all natural resources, including all or part of an oil or gas pool, field, or like area;

(2) promote the prevention of economic and physical waste; and

(3) provide for the protection of all parties of interest, including the state.

(b) In evaluating the above criteria, the commissioner will consider

(1) the environmental costs and benefits of unitized exploration or development;

(2) the geological and engineering characteristics of the potential hydrocarbon accumulation or reservoir proposed for unitization;

(3) prior exploration activities in the proposed unit area;

(4) the applicant's plans for exploration or development of the unit area;

(5) the economic costs and benefits to the state; and

(6) any other relevant factors, including measures to mitigate impacts identified above, the commissioner determines necessary or advisable to protect the public interest.

(c) The commissioner will consider the criteria in (a) and (b) of this section when evaluating each requested authorization or approval under 11 AAC 83.301 - 11 AAC 83.395, including

(1) an approval of a unit agreement;

(2) an extension or amendment of a unit agreement;

(3) a plan or amendment of a plan of exploration, development or operations;

(4) a participating area; or

(5) a proposed or revised production or cost allocation formula.

11 AAC 83.395. Definitions.

Unless the context clearly requires a different meaning, in 11 AAC 83.301 - 11 AAC 83.395 and in the applicable unit agreements...

(3) "force majeure" means war, riots, acts of God, unusually severe weather, or any other cause beyond the unit operator's reasonable ability to foresee or control and includes operational failure to existing transportation facilities and delays caused by judicial decisions or lack of them;

(4) "paying quantities" means quantities sufficient to yield a return in excess of operating costs, even if drilling and equipment costs may never be repaid and the undertaking considered as a whole may ultimately result in a loss; quantities are insufficient to yield a return in excess of operating costs unless those quantities, not considering the costs of transportation and marketing, will produce sufficient revenue to induce a prudent operator to produce those quantities;

(7) "unit" means a group of leases covering all or part of one or more potential hydrocarbon accumulations, or all or part of one or more adjacent or vertically separate oil or gas reservoirs, which are subject to a unit agreement...

JURISDICTIONAL STATEMENT

On February 15, 2008, the superior court signed the Decision on Appeal in the consolidated appeals 3AN-05-9272 CI and 3AN-06-8419 CI.[1] The Decision on Appeal was distributed to the parties on February 19, 2008.[2] The Decision was subsequently amended and distributed to the parties on February 20, 2008.[3] Appellants filed a timely Motion for Reconsideration of the Decision on Appeal on March 3, 2008.[4] The superior court denied Appellants' Motion for Reconsideration of the Decision on Appeal on April 4, 2008.[5] The Order Affirming the February 15, 2008 Decision on Reconsideration was distributed to the parties on April 7, 2008.[6] The Alaska Supreme Court has jurisdiction over the consolidated appeals pursuant to AS 22.05.010 (c).

PARTIES

Pursuant to Alaska Appellate Rule 204(g), the parties are Monte J. Allen ("Allen"), Daniel K. Donkel ("Donkel"), and the Alaska Department of Natural Resources, Division of Oil & Gas ("the Division", "DNR", or "the Commissioner").

ISSUES PRESENTED FOR REVIEW

1. Whether the Commissioner violated 11 AAC 02.050(a) and the Due Process Clause of the Alaska Constitution and the United States Constitution by refusing Appellants' request for a hearing on their administrative appeal and request for extension

[1] Exc. 001-014.
[2] Exc. 014.
[3] Exc. 001.
[4] Exc. 325-329.
[5] Exc. 330-331.
[6] Exc. 331.

to complete drilling of a test well on ADL 369116 before approving the 2005 Plan of Development for the North Middle Ground Shoal Unit and denying Appellants' request for extension.

2. Whether an unresolved agency appeal involving a competing claim of ownership to an oil and gas lease creates a cloud on title as a matter of law.

3. Whether the Commissioner abused his discretion by failing to grant Appellants a reasonable extension of time to complete test drilling on ADL 369116.

4. Whether DNR breached the covenant of good faith and fair dealing implied in the 2002 Settlement Agreement in Superior Court Case No. 3AN-00-3616 CI.

5. Whether the Commissioner erred in concluding that the 2005 Plan of Development for the North Middle Ground Shoal Unit was in the state's best interest.

6. Whether the Commissioner erred by terminating the North Middle Ground Shoal Unit and ADL 369116 in light of DNR's violation of Appellants' due process rights.

I. STATEMENT OF THE CASE

This appeal arises from two decisions issued by the Commissioner on May 26, 2005 and April 24, 2006, concerning oil and gas lease ADL 369116 contained within what was formerly known as the North Middle Ground Shoal Unit ("NMGSU") located in the Cook Inlet. In the course of rendering these decisions, the Commissioner violated Appellants' due process rights under the Alaska and federal constitutions and abused his discretion under state law. The record, these violations represent a disturbing pattern of

abuses which call into question the integrity of the agency charged with managing the oil and gas industry and which discourages oil and gas development by small oil producers to the detriment of Alaska.

Appellants have appealed the Commissioner's decisions on several grounds. Appellants challenge: (1) the Commissioner's decision to deny them a hearing on their administrative of appeal of the 2005 Plan of Development ("2005 POD") for the NMGSU submitted by Union Oil Company of California ("Unocal") and on their request for a two year extension of the lease; (2) the Commissioner's conclusion that his own failure to resolve a pending appeal involving a competing claim of ownership of ADL 369116 did not result in a cloud on title; (3) the Commissioner's failure to grant a reasonable extension of the lease to offset the time Appellants lost while the agency delayed clearing title; (4) the Commissioner's conclusion that the 2005 POD is in the best interest of the state; and (5) the Commissioner's decision to terminate ADL 369116 and the NMGSU in light of DNR's violation of Appellants' due process rights.

Appellants seek relief from this Court for the loss of their property interest in ADL 369116 and the NMGSU. Appellants respectfully request that the Court reverse both the May 26, 2005, and April 24, 2006, decisions of the Commissioner and reinstate their property interests in ADL 369116 and the NMGSU. Appellants also request that DNR be directed upon remand to grant Appellants a two-year extension from the issuance of this Court's decision to complete the drilling of an initial test well on ADL 369116. If for whatever reason, the Court cannot grant any portion of the relief requested based on the

existing record, Appellants request that the Court remand the matter to an impartial forum to conduct a hearing to supplement the record.

II. STATEMENT OF FACTS

A. Background of ADL 369116

On June 24, 1986, Daniel K. Donkel submitted a bid for Tract No. 49-116 on behalf of Danco, Inc. ("Danco").[7] On July 2, 1986, DNR provided notice of the award of ADL 369116 to Danco.[8] DNR issued oil and gas lease ADL 369116 to Danco effective September 1, 1986.[9] On July 5, 1988, Danco assigned 100% of its working interest in ADL 369116 to Amoco Production Co. ("Amoco").[10] A "working interest" refers to "the interest held in lands by virtue of a lease, operating agreement, fee title or otherwise, under which the owner of the interest is vested with the right to explore for, develop and produce minerals…."[11] The assignment was approved by DNR on September 21, 1988.[12] On July 13, 1990, Danco assigned a one-eighth interest in its overriding royalty interest ("ORRI") in ADL 369116 to Allen.[13] An "overriding royalty interest" is defined as "a percentage of the gross production payable to some person other than the lessor or

[7] Exc. 015-016.
[8] Exc. 017-021.
[9] Exc. 022-030.
[10] Exc. 039-041.
[11] 11 AAC 88.185 (32).
[12] Exc. 039-041.
[13] Exc. 042-044

persons claiming under the lessor."[14] DNR approved the assignment of a .125 percent ORRI in ADL 369116 to Allen on February 11, 1991.[15]

On August 28, 1990, Amoco assigned the 100% working interest in ADL 369116 that it had received from Danco to Unocal.[16] On September 2, 1994, Unocal assigned 100% of its working interest in ADL 369116 back to Danco.[17] DNR approved the assignment on September 29, 1994.[18] Finally, Danco assigned 100% of the working interest in ADL 369116 back to Unocal on June 19, 1996.[19]

On September 10, 1996, DNR gave notice that ADL 396116 was committed to the NMGSU, which indefinitely extended the term of the lease under paragraph 4(b) of the lease and under the NMGSU Agreement.[20] Paragraph 4(b) of the September 1, 1986, Lease Agreement provides "[t]his lease will be extended automatically if it is committed to a unit agreement approved or prescribed by the state, and will remain in effect for so long as it remains committed to that unit agreement."[21]

DNR's approval of Unocal's request for unitization of the NMGSU was at least in part based on Unocal's commitment to drill an exploratory well on ADL 369116 by August 31, 1998 and test for natural gas accumulations in the region.[22] Unocal later

[14] 38 Am.Jur.2d Oil and Gas § 215 (1999).
[15] Exc. 047.
[16] Exc. 045-046.
[17] Exc. 048-050.
[18] Exc. 048.
[19] Exc. 051-052.
[20] Exc. 053-054.
[21] Exc. 023.
[22] Exc. 082.

received a drilling extension to December 31, 1999 in exchange for its commitment to gather costly 3D seismic mapping of the region.[23]

On April 27, 1998, Danco dissolved and assigned its ORRI in ADL 369116 to numerous individuals and entities, including Donkel, Robert Bolt ("Bolt"), and Dr. George Kasper ("Kasper").[24] On October 16, 1998, Unocal applied to form the Shallow Tyonek Gas Reserve Participating Area within the NMGSU.[25] The proposed plan was to include both ADL 369116 and ADL 17595.[26]

B. The First Appeal of DNR's Attempt to Terminate ADL 369116 and Settlement Agreement Between the Parties.

Due to a variety of factors, including the difficulty in mobilizing a "jack-up rig" in the Cook Inlet, Unocal was unable to complete the test drilling of ADL 369116 by December 31, 1999.[27] On June 24, 1999, DNR approved the Shallow Tyonek Gas Reservoir Participating Area but excluded ADL 369116 from that area.[28] Though Unocal appealed the June 24, 1999 decision, the Commissioner later affirmed the Division's ruling in a letter dated January 5, 2000.[29]

On August 23, 1999, Unocal submitted an amended Plan of Exploration requesting additional time to review the 3D seismic data gathered and to drill the

[23] *Id.*
[24] Exc.055-065.
[25] Exc. 066-078, Exc. 079-084.
[26] *Id.*
[27] Exc. 080.
[28] *Id.*
[29] Exc. 085-086.

exploratory well on ADL 369116.[30] DNR denied Unocal's Amended Plan of Exploration on September 2, 1999 and notified Unocal that if the exploratory well was not drilled by December 31, 1999, ADL 369116 would contract out of the NMGSU and terminate.[31]

On January 14, 2000, DNR provided notice to Unocal that ADL 369116 was contracted out of the NMGSU.[32] On March 31, 2000, DNR provided notice to Unocal that ADL 369116 had expired.[33] Donkel and other ORRI owners (but not Allen) moved to stay the Commissioner's decision to exclude ADL 369116 from the Shallow Tyonek Gas Reservoir Participating Area (effectively terminating ADL 369116) in an appeal filed before the superior court, *Donkel, et al. v. State*, Case No. 3AN-00-3616 CI.[34] On April 27, 2000, the superior court granted that motion and stayed DNR's decision to terminate the lease.[35]

The principal issue raised in the appeal to the superior court from the June 24, 1999, decision was whether Donkel and the other ORRI owners were entitled to notice and a hearing prior to the Commissioner excluding ADL 369116 from the Shallow Tyonek Gas Reservoir Participating Area.[36] In short, DNR failed to provide a meeting or hearing at which overriding royalty interest owners could participate or present information.[37] The superior court ultimately reversed the Commissioner's June 24, 1999

[30] Exc. 082.
[31] Exc. 079-084.
[32] Exc. 087-088.
[33] Exc. 089.
[34] Exc. 090-094.
[35] Exc. 098.
[36] Exc. 154.
[37] Exc. 155.

decision, concluding that DNR violated its own regulations by failing to provide royalty and ORRI owners with notice and an opportunity to be heard.[38]

Following the conclusion of the appeal, the parties agreed to settle the lawsuit under the following terms (the "2002 Settlement Agreement" or "Settlement Agreement"):

> 6. The North Middle Ground Shoal Unit as approved by the State on August 30, 1996, is reconstituted to included oil and gas leases ADL 17595 and ADL 369116, with Unocal as the unit operator. Subject to the terms and conditions of the approved plans, the North Middle Ground Shoal Unit Agreement will terminate on December 31, 2005, unless extended under Article 12 of the unit agreement . . .
>
> 7. The Plan of Exploration for ADL 369116 will require that the Working Interest Owners undertake and do the following:
>
> (a) On or before October 31, 2003, the Working Interest Owners shall submit to the DNR a written commitment to commence drilling operations for a well ("Initial Test Well") with a bottom hole location within the boundaries of ADL 369116, to a depth sufficient to test the Tyonek and Hemlock Foundations;
>
> (b) On or before December 31, 2004, the Working Interest Owners shall commence actual drilling operations for the Initial Test Well; and
>
> (c) On or before December 31, 2005, the Working Interest Owners shall complete, suspend, or abandon the Initial Test Well.
>
> 8. In the event that the current Working Interest Owners in ADL 369116 (i.e. Union Oil Company of California and Forest Oil Corporation) fail to either submit the written commitment to DNR by October 31, 2003 or commence actual drilling operations as specified in paragraph 7(a) by December 31, 2004, they will transfer their working interest in ADL 369116 to Robert Bolt 33.3%, Daniel Donkel 33.4%, and George Kasper 33.3% with no change to the

[38] Exc. 159.

> requirements of paragraph 7(c). DNR shall process any assignments applications to effect such transfers of a working interest ownership within 30 days.
>
> . . . .
>
> 12. In the event that no well is drilled as specified in paragraph 7, the North Middle Grounds Shoal Unit Agreement and ADL 369116 will automatically terminate effective December 31, 2005, unless DNR extends the termination date at its sole discretion…39

The Superior Court dismissed the lawsuit based on the 2002 Settlement Agreement.[40] On March 17, 2003, DNR provided notice to Unocal that ADL 369116 was reinstated and committed to the NMGSU, effective December 2, 2002.[41]

On October 21, 2003, nearly one year after the execution of the Settlement Agreement, Unocal provided notice to DNR and to Bolt, Donkel, and Kasper that it did not intend to commit to the test drilling of ADL 369116.[42] Pursuant to the terms of the Settlement Agreement, Unocal assigned a 33.4% working interest in ADL 369116 to Donkel effective December 1, 2003.[43] Forest Oil Corporation subsequently assigned a 16.70% working interest in ADL 369116 to Donkel effective March 1, 2004.[44]

While *Donkel et al. v. State* was pending, DNR took certain actions which materially and adversely affected interested parties' ability to develop ADL 369116. Despite the fact that the superior court had issued a stay of DNR's decision terminating ADL 369116 on April 27, 2000, DNR nonetheless violated the express terms of that

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[39] Exc. 162.
[40] Exc. 168-169.
[41] Exc. 170-171.
[42] Exc. 172-173.
[43] Exc. 185-186.
[44] *Id.*

order and offered land encompassed by ADL 369116 in a competitive sale approximately four months later.[45]

On August 16, 2000, DNR held the bid for Cook Inlet Areawide lease sale.[46] Richard Wagner and Dan Gilbertson (collectively "Wagner") bid on Tract No. 287 which is contained within ADL 369116.[47] On August 28, 2000, DNR gave Wagner notice that he was the high bidder for oil and gas lease ADL 389508.[48] On March 1, 2001, nearly one year after the stay ordered in Case No. 3AN-00-3616 CI, DNR provided Wagner with notice of the award of ADL 389508.[49] The lease for ADL 389508, which included Tract No. 287, was memorialized on April 12, 2001, and became effective May 1, 2001.[50]

On June 1, 2001, DNR acknowledged that it had violated the stay issued in *Donkel et al. v. State*, and consequently revoked oil and gas lease ADL 389508.[51] DNR explained in that letter:

> **DO&G did not have the authority to offer the tract. It was and is subject to a court order precluding DO&G from offering it**. The Superior Court for the State of Alaska issued an order on April 27, 2000 (*Donkel v State of Alaska*, Case No. 3AN-00-3616 Civil. Since DO&G did not have the authority to offer the tract, it did not have the authority to issue the lease. DO&G revokes its award of Tract 287 as well as its lease issuance decision. ADL 389508 is terminated, effective May 1, 2001.

[45] Exc. 098, Exc. 099.
[46] Exc. 099-100.
[47] *Id.*
[48] Exc. 101-102.
[49] Exc. 103-106.
[50] Exc. 108-130; Exc. 107.
[51] Exc. 131-132.

> Donkel v. State of Alaska concerned a former oil and gas lease, ADL 369116. Acreage formerly included in that lease is divided into three tracts for the Cook Inlet Areawide Competitive Oil and Gas Lease Sales: Tracts 284, 285 and 287. Public notice for the Cook Inlet Areawide 2000 Sale notified bidders that the Donkel case involved former lease ADL 369116, and that the court order precluded DO&G from offering the acreage which had been included in the lease. The notice specifically excluded Tracts 284 and 285, but did not exclude Tract 287 from the sale.[52]

Wagner appealed the decision on June 29, 2001.[53] On January 25, 2002, DNR gave notice that the stay ordered in *Donkel, et al.*[54] was released, and gave Wagner notice that it intended to consider his appeal.[55] Inexplicably, it was not until over two years later on August 13, 2004, that the Commissioner took action to resolve the Wagner appeal and then only because of a letter sent by James Gottstein ("Gottstein") advising the Commissioner of the adverse impact that the cloud on title was having on the development of ADL 369116.[56] Gottstein served as counsel for Donkel at various stages during the prior litigation and during negotiations with DNR regarding the NMGSU.

On February 25, 2004, Unocal submitted its 2004 Plan of Development ("2004 POD") for the NMGSU.[57] On May 24, 2004, DNR approved the plan.[58] In the approval, DNR indicated that if an "Initial Test Well is not drilled as specified in the Court order, the NMGSU Unit Agreement and ADL 369116 will automatically terminate effective

[52] Exc. 131 (emphasis added).
[53] Exc. 137.
[54] Exc. 146-147.
[55] *Id.*
[56] Exc. 221-224; Exc. 131.
[57] Exc. 191-193.
[58] Exc. 214-215.

December 31, 2005."[59] Gottstein sought a clarification of the order and requested an extension of the December 31, 2005 deadline on Donkel's behalf to drill a well on ADL 369116 because the cloud on the title created by the unresolved Wagner appeal had already deterred at least one third party from committing to drilling on ADL 396116.[60] Gottstein also called attention to the fact that the lessees of ADL 369116 had not been provided notice of DNR's approval of 2004 POD.[61] In a letter dated August 2, 2004, the Division summarily denied Gottstein's request for an extension.[62] Reminiscent of the position that DNR took with respect to due process in *Donkel, et al. v. State*, the Division explained in that letter that the agency was not required to provide notice of the May 24, 2004 decision to the working interest holders of ADL 369116 because Unocal was the unit operator and as unit operator represented the other working interest holders.[63] A decision denying the Wagner appeal followed thereafter.[64]

On October 22, 2004, Unocal sought approval of its plan to abandon the Baker platform, which was located near the boundaries of ADL 369116.[65] Though DNR approved the plan on January 10, 2005, it noted that "the Commission recognizes that much oil remains in place in the developed reservoirs, deeper exploration opportunities may exist that could only be exploited by the existing platforms, and other beneficial uses

[59] *Id.*
[60] *Id.*
[61] Exc. 261-217.
[62] Exc. 219-220.
[63] *Id.*
[64] Exc. 221-224.
[65] Exc. 225-226.

of the platforms may exist."[66] As a result, DNR encouraged Unocal to "explore options to other operators for beneficial use before complete dismantling is initiated."[67]

C. The 2005 Plan of Development and Request for Extension.

Unocal submitted its 2005 POD on February 22, 2005.[68] In that plan, Unocal indicated that it did not intend to perform any development activities during the plan period (June 1, 2005 to May 31, 2006) and suggested a plan for removal of the Baker platform.[69] Meanwhile, Bolt, Donkel, and Kasper assigned their working interest to Renaissance Resources, Alaska, LLC ("Renaissance") on or about March 22, 2005.[70]

On March 31, 2005, DNR approved Unocal's 2005 Plan of Development for NMGSU.[71] On April 20, 2005, Donkel and Allen formally appealed DNR's approval of the 2005 POD.[72] The basis of their appeal was twofold:

> (a) The plans to abandon the Baker Platform, oil and gas pipelines leaving the platform and various well will have a material, negative impact on the rights and interests and opportunity to explore drill and develop ADL 369116.
>
> (b) The ability of the working interest owners in ADL 369116 to fulfill the drilling commitment of the Initial Test Well has been unreasonably and unfairly disrupted and interfered with due to the cloud on title arising from the delay and bad faith in initial selling and then actions to terminate any interest of Rick Wagner in ADL 389508, covering part of ADL 369116.[73]

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[66] Exc. 227.
[67] *Id.*
[68] Exc. 228-231.
[69] *Id.*
[70] Exc. 232.
[71] Exc. 233-235.
[72] Exc. 240-242; Exc. 243-245.
[73] Exc. 241; Exc. 243-244.

Allen and Donkel both requested a hearing on the disputed issues and a two-year extension to drill the initial test well on ADL 369116.[74] The Commissioner denied this request in a letter dated April 26, 2005.[75] On May 26, 2005, the Commissioner issued a Final Order and Decision affirming his prior decision denying Allen's and Donkel's request for extension and denying their appeal of the 2005 POD.[76] On June 28, 2005, Donkel and Allen filed a Notice of Appeal with the superior court.[77]

On June 26, 2005, Renaissance, then the 100% working interest owner of ADL 369116, requested an extension of the December 31, 2005 deadline to drill on ADL 369116.[78] Though DNR initially indicated that it would consider such a request, it ultimately denied the request and terminated ADL 369116 and the NMGSU.[79]

On February 15, 2008, Judge Stowers issued a decision affirming the Commissioner's May 26, 2005 Final Order and Decision.[80] The superior court did not indicate in that order whether it was also affirming the Commissioner's April 24, 2006, Final Decision and Order which terminated denied Renaissance's request for an extension of the lease for ADL 369116 and terminated the NMGSU (Case No. 3AN-06-8419 CI).[81] The Superior Court previously dismissed two related appeals filed by Gottstein (3AN-06-6003 CI and 3AN-06-8094 CI) which had been consolidated with

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[74] *Id.*
[75] Exc. 246.
[76] Exc. 253-262.
[77] Exc. 267-269.
[78] Exc. 284-285.
[79] Exc. 284287; Exc. 316-323.
[80] Exc. 001-014.
[81] Exc. 316-323.

Allen and Donkel's two appeals.[82] Appellants moved for reconsideration of the superior court's decision, but that motion was denied.[83] This appeal followed.

III. STANDARD OF REVIEW

When the superior court acts as an intermediate court of appeal in an administrative matter, this Court independently reviews the merits of the agency's decision.[84] No deference is given to the lower court's decision.[85]

An agency's factual findings are reviewed under the substantial evidence standard, under which reversal is appropriate only if the Court "cannot conscientiously find that the evidence supporting [the agency's decision] is substantial." Substantial evidence is "such relevant evidence as a reasonable mind might accept as adequate to support a conclusion."[86]

The substitution of judgment standard applies where the questions of law presented do not involve agency expertise or where the agency's specialized knowledge and experience would not be particularly probative as to the meaning of the statute.[87] This standard permits the Court to substitute its own judgment for that of the agency even

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[82] Exc. 333-334.
[83] Exc. 325-329.
[84] *South Anchorage Concerned Coalition, Inc. v. Municipality of Anchorage Bd. of Adjustment*, 172 P.3d 774, 780 (Alaska 2007); *Robinson v. Municipality of Anchorage*, 69 P.3d 489, 493 (Alaska 2003) (citation omitted); *Amerada Hess Pipeline Corp. v. Alaska Public Utilities Comm'n*, 711 P.2d 1170, 1175 (Alaska 1986).
[85] *ACS of Alaska, Inc. v. Regulatory Comm'n of Alaska*, 81 P.3d 292, 295 (Alaska 2003); *Tesoro Alaska Petroleum Co. v. Kenai Pipe Line Co.*, 746 P.2d 896, 903 (Alaska 1987).
[86] *May v. State, Commercial Fisheries Entry Comm'n*, 175 P.3d 1211, 1216 (Alaska 2007); *Leigh v. Seekins Ford*, 136 P.3d 214, 216 (Alaska 2006) (citation omitted).
[87] *Northern Timber Corp. v. State, Dep't. of Transp., Public Facilities*, 927 P.2d 1281 n. 10 (Alaska 1996); *Tesoro Alaska Petroleum Co.*, 746 P.2d at 903.

if the agency's decision had a reasonable basis in law.[88] Questions of law and issues of constitutional interpretation are reviewed *de novo*.[89]

The rational basis test is used where the questions at issue implicate special agency expertise or the determination of fundamental policies within the scope of the agency's statutory function.[90] When applying the rational basis test, the Court will uphold an agency's decision if it is supported by the facts and has a reasonable basis in law.[91]

IV. ARGUMENT

A. The Commissioner Violated 11 AAC 02.050(a) And The Due Process Clause Of The Alaska And Federal Constitutions.

The requirements of the Alaska Constitution's Due Process Clause, Article I § 7, apply in the administrative setting.[92] This is also true under the Fifth and Fourteenth Amendments to the United States Constitution.[93] A claim for violation of due process requires as prerequisites both state action and the deprivation of an individual interest sufficient to warrant constitutional protection.[94] This Court has previously recognized

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[88] *Id.*
[89] *Simpson v. State, Commercial Fisheries Entry Comm'n*, 101 P.3d 605, 609 (Alaska 2004) citing *Revelle v. Marston*, 898 P.2d 917, 925 n. 13 (Alaska 1995).
[90] *West v. Municipality of Anchorage*, 174 P.3d 224, 226 -227 (Alaska 2007) citing *State v. Pub. Safety Employees Ass'n*, 93 P.3d 409, 413 (Alaska 2004).
[91] *State, Dept. of Admin. v. Bachner Co., Inc.*, 167 P.3d 58, 61 (Alaska 2007) (citation omitted).
[92] *State, Dept. of Health & Social Services v. Valley Hosp. Ass'n, Inc.*, 116 P.3d 580, 583 (Alaska 2005).
[93] *Withrow v. Larkin*, 421 U.S. 35, 46-47 (1975) (basic requirements of due process apply to administrative agencies).
[94] *Estate of Miner*, 635 P.2d 827, 829 (Alaska 1981) citing *Nichols v. Eckert*, 504 P.2d 1359, 1362 (Alaska 1973); *Paul v. Davis*, 424 U.S. 693, 710-11 (1976) (procedural guarantees of Fourteenth Amendment apply when the state seeks to remove or significantly alter interests recognized and protected under state law).

that private contractual rights created by oil and gas leases "are of sufficient importance to warrant constitutional protection."[95]

As lessees of ADL 369116, Appellants were denied due process of law when the Commissioner denied their request for a hearing on their administrative appeal, failed to clear title to ADL 369116 for nearly two and a half years, and denied Appellants' request for a corresponding extension of the lease. As a result of the actions of the State agency, Appellants suffered a diminishment in their property interest in ADL 369116 and ultimately the loss the value of that interest. Appellants seek reversal of the May 26, 2005, and April 24, 2006, decisions and reinstatement of their property rights in ADL 369116 and the NMGSU.

1. The Commissioner's failure to provide Appellants with a hearing after raising substantial questions of fact violated 11 AAC 02.050(a) and denied Appellants due process of law.

Appellants' due process rights were violated when the Commissioner denied their request for a hearing challenging the 2005 POD. Pursuant to 11 AAC 02.050(a), DNR has discretion to hold a hearing when questions of fact must be resolved during the course of an administrative appeal.[96] This Court has previously held that a due process violation results when DNR fails to grant a hearing when presented with substantial and material issues of fact necessary to the determination of the matter.[97] In this regard, when

[95] *ConocoPhillips Alaska, Inc. v. State*, 109 P.3d 914, 924 (Alaska 2005).
[96] 11 AAC 02.050(a).
[97] *White v. State, Department of Natural Resources*, 984 P.2d 1122, 1126 (Alaska 1999) (holding that DNR violated the due process rights of an assignee of oil and gas lease interest by failing to grant a hearing on the factual dispute whether a bottom hole was located on leased land).

the discretion enjoyed by the agency conflicts with the requirements of due process, the former must give way to the latter.[98]

The record reflects that the Commissioner was presented with a myriad of disputed factual issues of material importance placing the agency's discretion in direct conflict with the demands of due process. In response to DNR's approval of Unocal's 2005 POD, Appellants' sent identical letters to the Commissioner appealing the decision and requesting both a hearing and a two-year extension. At that time, Appellants notified the Commissioner that Unocal's plan would have a negative impact on their own ability to explore, drill, and develop ADL 369116. Appellants also provided notice that the working interest owners of ADL 369116 had been impeded by "the cloud of title arising from the delay and bad faith" on the part of DNR in failing to resolve the Wagner appeal.[99] Both letters contained a separately numbered paragraph 4(a) identifying "disputed material facts." Paragraph 4(a) provided:

> Disputed Material Facts: The material facts of the decision which are in dispute by the undersigned include, in addition to others which may be asserted, the following:
>
> (a) Without the ability to review information and data consulted and relied upon in connection with the various abandonment activities, satisfaction and compliance with various criteria in 11 AAC § 83.303 cannot be confirmed and verified.[100]

While paragraph 4(a) may have specifically identified a disputed factual issue, it does not provide an exhaustive list of disputed factual issues in the matter. Paragraph 3 of the

[98] *Id.* n. 10.
[99] Exc. 240-245.
[100] Exc. 241, 244.

same document provides additional disputed issues of fact that were ignored by the Commissioner. Specifically, Appellants alleged in paragraph 3 that 2005 POD would have a material negative impact on the development of ADL 369116 and that the cloud on title caused by the Commissioner's failure to resolve the Wagner appeal impacted their ability to develop the lease. The Commissioner erred by failing to recognize that Appellants were requesting a hearing on both disputed issues.

Despite being alerted to the existence of material facts in dispute, the Commissioner neither convened a hearing nor invited Appellants to supplement the record with additional factual information. Instead, the Commissioner sent Donkel a letter advising him that the information that the Division consulted and relied upon in approving the 2005 POD was a matter of public record.[101] Given that Appellants had not been given the opportunity to supplement that record and no hearing was ever held, the Commissioner issued a final decision of the agency without having made any inquiry into the nature of the factual disputes presented.

In the absence of a fully developed record, the Commissioner could not in fairness and in good faith issue an opinion disposing of the issue whether his own actions interfered with Appellants' ability to develop the lease. As such, Appellants have been denied the opportunity to be heard on an issue which ultimately resulted in the termination of their property interests in ADL 369116. Had Appellants been granted a

[101] Exc. 246.

hearing on the matter, they would have been able to address the specific concerns the Commissioner expressed at page 9 of the May 26, 2008 Final Decision and Order.[102]

Setting aside the obvious conflict of interest in the Commissioner being able to render a fair and impartial decision when sitting as his own judge,[103] the fact remains the Commissioner did not provide Appellants with an opportunity to be heard on the question whether and in what ways the 2005 POD would have a negative impact on development of ADL 369116 and whether the Commissioner's lack of diligence in resolving the cloud on title interfered with investment prospects for the development of the lease. Indeed, the only evidence in the record supports Appellants' argument that they suffered a negative impact from the cloud on title. Appellants' April 20, 2005 letters and Gottstein's June 13, 2004, letter all provided ample notice of an adverse impact and the necessity for a hearing.[104] Because the Commissioner's finding that there was no impact to Appellants from the Wagner appeal is unsupported by any evidence, let alone substantial evidence, the decision should be reversed.

Another issue of material fact raised, by implication if not explicitly, in Appellants' April 20, 2005 letters is whether the approval of the 2005 POD is in the state's best interest. DNR's best interest determination is premised in part on its finding that the unit is incapable of producing oil and gas in paying quantities. Appellants vehemently disagree. There are known oil and gas accumulations underlying ADL

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[102] Exc. 261.

[103] *State v. Lundgren Pac. Const. Co.,* 603 P.2d 889, 896 (Alaska 1979) ("[a] 'fair tribunal is a basic requirement of due process.'") quoting *In re Murchison*, 349 U.S. 133, 136 (1955).

[104] Exc. 216-217.

369116, which were discovered when Pan Am Petroleum Corp. drilled well No. MGS 18743 in the 1960's.[105]

As recognized by the United States Supreme Court, "[p]rocedural due process imposes constraints on governmental decisions which deprive individuals of "liberty" or "property" interests within the meaning of the Due Process Clause of the Fifth or Fourteenth Amendment."[106] However, the United States Supreme Court has also explained that "Due Process is flexible" and calls for procedural protections according to the demands of the situation.[107] Though this Court's jurisprudence provides guidance as to the interaction of the Due Process Clause of the Alaska Constitution and 11 AAC 02.050(a), it does not address the interaction between DNR's discretion to convene a hearing and the Due Process Clause of the federal constitution.

In determining what procedural safeguards are necessary to protect an individual's due process rights under the federal constitution, federal courts generally apply the test articulated in *Matthews v. Eldridge*. Under this test, the Court first considers the interest that will be affected by the official action; second, the risk of an erroneous deprivation of such interest through the procedures used and the probably value if any of substitute procedural safeguards; and finally the government's interest, including the function involved and the fiscal and administrative burdens that the additional or substitute procedural requirements would entail.[108] Alaska has adopted this same standard.[109]

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[105] Exc. 74; Exc. 284-285; Exc. 349-350.
[106] *Matthews v. Eldridge*, 424 U.S. 319, 332 (1976).
[107] *Id. citing Morrissey v. Brewer*, 408 U.S. 471, 481 (1972).
[108] *Id.* at 334-35.

Application of the *Matthews v. Eldridge* test in this instance weighs in favor of an evidentiary hearing. The private interest involved (a property right based in contract) is substantial, both in terms of the cost of the underlying lease and the effort and resources expended by Appellants to develop the lease. The risk of deprivation of Appellants' property rights in this case is also significant. Appellants requested a hearing, in part, to address the impact of the Commissioner's failure to proceed in good faith to clear title to ADL 369116. The risk of abuse of the administrative and adjudicative process is greatest when a public official is charged with sitting as judge of his or her own actions. As such, the protections of an evidentiary hearing, including the ability to present evidence and cross-examine witnesses, were necessary to ensure that the decision would be fair and impartial in all respects. Here, the evidentiary hearing, was necessary to develop the record regarding the impact of the Commissioner's own inaction in resolving the Wagner appeal on the development of ADL 369116 and to address the impact of the 2005 POD on development of ADL 369116. Due process demands that, at a minimum, any opportunity to be heard be meaningful.[110] Under the circumstances, Appellants were entitled to the full panoply of protections afforded by an evidentiary hearing. By denying Appellants a hearing on the matter, the Commissioner denied Appellants both an impartial forum and a meaningful opportunity to be heard.

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[109] *See, e.g., Seth D. v. State, Dept. of Health and Social Services, Office of Children Services*, 175 P.3d 1222, 1227 (Alaska 2008) (applying the *Matthews v. Eldridge* test).
[110] *Alyeska Pipeline Service Co., State, Dept. of Environmental Conservation*, 145 P.3d 561, 570-71 (Alaska 2006).

Finally, under the circumstances, the burden to the state would have been minimal. The cost of a limited hearing on the matter is insignificant when measured against the costs to the parties in prosecuting the subsequent appeals that resulted from the Commissioner's violations of due process and when measured against the costs to the people of this state who have a vested interest in the development of the oil and gas reserves in Cook Inlet. By consistently favoring a minimalist approach to due process, DNR has unnecessarily delayed development of ADL 369116 to the detriment of Appellants' property interests and to the State as a whole.

Application of the *Matthews v. Eldridge* test weighs in favor of an evidentiary hearing under both the state and federal constitutions. To the extent that the Court does not otherwise order the reinstatement of Appellants' rights in ADL 369116 and the NMGSU, justice mandates that a fair and impartial hearing be set upon remand to resolve the myriad issues of fact raised in this dispute, and that Appellants be allowed to develop the record to demonstrate the denial of their property interests without due process.

2. The Commissioner's unreasonable delay in resolving the Wagner appeal resulted in a denial of due process.

Apart from the due process violation that resulted from the Commissioner's denial of Appellants' request for a hearing and extension of the lease, the Commissioner violated Appellants' due process rights by delaying the final resolution of the Wagner appeal by over two years. Because the Commissioner denied Appellants' request for a hearing on this matter and did not otherwise permit supplementation of the record, there is only limited evidence in the record on the impact of the Commissioner's failure to

resolve the cloud of title DNR created with respect to ADL 369116 when it offered a portion of that lease for sale in direct violation of a standing court order. Nonetheless, the evidence in the record supports the conclusion that the delay resulted in prejudice to Appellants' property interest and contributed to their inability to drill the initial test well by the deadline established in the 2002 Settlement Agreement.

Recently, this Court addressed the question whether there can be a deprivation of a property interest due to a deficiency in a proceeding where an applicant's claim is untimely denied.[111] In *Brandal*, the appellant filed an application for a limited entry permit to fish in a purse seine fishery. The application was initially denied and a hearing later convened to review the applicant's qualifications. At the close of the hearing, the hearing officer recommended that the applicant be denied the limited entry permit. The applicant was provided an interim permit pending a final decision from the agency. Inexplicably, the Commercial Fisheries Entry Commission took twenty-two years to issue a final decision in the matter. Because the applicant had the benefit of an interim permit during that time, he could show no prejudice resulting from the delay. Though the facts of *Brandal* did not allow for the conclusion that delay without prejudice could constitute a violation of due process, the Court left open the possibility that such a case might exist.

Here, the record reflects that the Commissioner failed to render a decision on the Wagner appeal for nearly two years after the stay in Case No. 3AN-00-3616 CI had been

[111] *Brandal v. State, Commercial Fisheries Entry Commission*, 128 P.3d 732 (Alaska 2006).

lifted. In light of the fact that DNR previously acknowledged that it had issued the Wagner lease in violation of a standing court order, the final resolution of the appeal presented no complexities for which the additional two years was necessary or reasonable. Indeed, it was only after Gottstein called attention to the deficiency that the Commissioner took any action to resolve the matter. Unlike the applicant in *Brandal*, Appellants were not issued interim relief. Instead, they were placed in the unenviable position of having to put together a drilling program with a clouded title.

There was adequate evidence in the record for the Commissioner to conclude that prejudice resulted from the delay at the time the Commissioner denied Appellants' request for extension; however, to date, Appellants have not been given the opportunity to present evidence at a hearing on the matter. At the time DNR cleared title to the lease, more than half of the three-year extension on the lease had passed. This delay jeopardized Appellants' ability to mobilize the necessary investment and drilling equipment by the December 31, 2005 deadline. The facts of this case justify a holding that the Commissioner's 21 month delay in resolving a routine administrative appeal resulted in a denial of due process warranting reversal of the Commissioner's May 26, 2005 and April 24, 2006 decisions.

In the alternative, if the Court concludes that there is inadequate evidence of prejudice shown in the present record, Appellants request that this case be remanded to

an impartial hearing officer or to the agency with an order to convene a hearing on the matter.[112]

B. The Commissioner's Failure To Resolve A Pending Agency Appeal In A Timely Fashion Created A Cloud On Title To ADL 369116 Adversely Impacting Development Of The Lease.

The Commissioner denied Appellants' request for a reasonable extension of the lease based on his unsupported belief that his own delay in resolving the Wagner appeal did not have an adverse impact on Appellants' ability to develop the lease. The Commissioner reached this conclusion after denying Appellants a hearing on the matter and in all respects without providing Appellants a meaningful opportunity to be heard. Specifically, the Commissioner observed that the unresolved Wagner appeal did not impact Appellants' ability to seek approval for proposed operations on ADL 369116.[113] This curious statement demonstrates that either the Commissioner fundamentally misunderstood the legal concept of clouded title or that he ignored the obvious impact that a cloud on title would have on Appellants' ability to develop the lease, or both. To the extent that the Commissioner applied an incorrect legal analysis or relied on flawed reasoning, in contradiction of the record, the May 26, 2005 Decision should be reversed and Appellants' rights in ADL 369116 restored.

[112] *Alaska Public Interest Research Group v. State*, 167 P.3d 27, 46 (Alaska 2007).
[113] Exc. 261.

1. As a matter of law, an unresolved agency appeal arising from a competing claim of ownership to an oil and gas lease creates a cloud on title on the lease.

The question of whether a cloud on title was created by the Commissioner's failure to resolve the Wagner appeal in a timely manner presents a question of law to which the Court applies its independent judgment.[114] It is well established that "[a] cloud on title is an outstanding claim or encumbrance which, if valid, would affect or impair the title of the owner of a particular estate."[115] The test for whether there is a cloud on title is whether the owner would be required to offer evidence to defeat an action based on the alleged cloud.[116] It is not the law in this state that only recorded instruments or encumbrances give rise to clouds on title.[117] The appropriate inquiry is whether Appellants could be asked for proof of marketable title by other private individuals and/or companies in the course of putting together a drilling program.

Under the circumstances, it is reasonable for any third party dealing with Appellants to request evidence from them explaining the status of DNR's issuance of a competing lease on a portion of the land contained within ADL 369116. Given the tremendous expense and risk involved in developing an oil and gas lease, it is reasonable to expect that any party investing in or financing development of ADL 369116 would perform their own due diligence going well beyond a simple title search. Indeed, there is

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[114] *Tesoro Alaska Petroleum Co.*, 746 P.2d at 903.
[115] *Nielson v. Benton*, 903 P.2d 1049, 1052 (Alaska 1995) (citing *Newpar Estates v. Barilla*, 161 N.Y.S.2d 950, 952 (N.Y.Sup.Ct.1957)).
[116] *Id.*
[117] *Id.* at 1053 n. 6 (specifically rejecting the argument that only recorded instruments or encumbrances should give rise to clouds on title).

evidence in the record that at least one prospective participant in the development of ADL 369116 was deterred from committing to a drilling program by the existence of the unresolved appeal. Consequently, as a matter of law, the unresolved Wagner appeal created a cloud on title to ADL 369116.

In the appeal before the superior court, DNR took the position that because the revocation of the Wagner lease was effective immediately it could not have affected Appellants' ability to develop the lease.[118] DNR also argued that "the Wagner appeal letter cannot reasonably be said to cloud title to ADL 369116 because (1) the appeal letter was not recorded; (2) the Wagner lease, ADL 389508, directly violated a court order staying termination of ADL 369116; (3) ADL 389508 was promptly revoked; and (4) after issuance of the revocation of the ADL 389508 and the filing of the Wagner appeal letter, the Superior Court issued an order December 2, 2002 reinstating ADL 369116."[119]

The above arguments made in defense of an erroneous decision from the Commissioner are without merit. The fact that Wagner's appeal was not recorded does not mean that there was no cloud on title.[120] This is true not just under Alaska law but under law specific to the oil and gas industry.[121] Thus, the fact that Wagner did not record his claim does not change the fact that his claims clouded the title to ADL 369116.

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[118] Appellee's Brief in Case No. 3AN-05-9272 CI at 2.
[119] *Id.* at 22.
[120] *Nielson,* 903 P.2d at 1053 n. 6.
[121] *In Re Stroud Oil Companies, Inc.*, 110 S.W.3d 18, 27 (Tex. App. 2002) (holding that "a document need not be recorded to constitute a cloud on title")

DNR also took the extraordinary position that since it did not have authority to issue the Wagner lease, the lease was void *ab initio*, and thus never clouded title.[122] It is undisputed that DNR's issuance of the Wagner lease directly violated a court order, but this does not change the fact that Wagner had the right to pursue his claims to that lease even after the settlement was reached in Case No. 3AN-00-3616 CI. Wagner was not a party to the Settlement Agreement and was in no way precluded from pursuing such claims. Regardless of whether that claim would ultimately have failed, the claim itself was a cloud on title until there was a final order, not subject to appeal, revoking Wagner's claim.

Similarly, the fact that DNR "promptly revoked" Wagner's lease did not clear the cloud on ADL 369116. Again, the fallacy in DNR's position is that the revocation of the Wagner lease did not extinguish Wagner's right to pursue his claim against the lease to this Court if necessary. Wagner's competing claim against the lease was not extinguished until the day he let his right to appeal the Commissioner's decision to the superior court lapse – approximately two years later. Until this event occurred, there was a cloud on the title to ADL 369116.

Finally, the fact that the superior court reinstated ADL 369116 does not change the fact that title to the lease was clouded. Reinstating Donkel and Allen's rights to ADL 369116 had absolutely no effect on the cloud created by Wagner's claims.

None of the arguments raised by DNR in the appeal before the superior court alter the reality that the unresolved Wagner appeal constituted a cloud on title as a matter of

[122] Appellee's Brief in Case No. 3AN-05-9272 CI at 22.

law. Because it is unclear what legal standard, if any, the Commissioner applied to the analysis of this issue, reversal of the May 26, 2005 decision is warranted. Again, this is yet another example of where the agency's compliance with the requirements of due process would have provided both a legal and factual basis for the Commissioner to issue an appropriate decision. The Commissioner provided no opportunity for Appellants to present evidence or argument on the matter prior to issuing the final decision of the agency.

2. Evidence exists in the record supporting the claim that the cloud on title impacted Appellants' ability to develop a test well on ADL 369116.

The impact of the Commissioner's failure to resolve the Wagner appeal in a timely fashion cannot be measured against whether DNR would have been dissuaded from approving a plan of development for ADL 369116, notwithstanding the cloud on title. This would achieve an absurd result rendering the concept of clouded title meaningless. Instead, the impact of the Commissioner's failure to clear title must be evaluated by examining whether it interfered with Appellants' ability to develop a drilling program for ADL 369116. The only evidence in the record on this point suggests that there was such interference.

At page 1 of his June 13, 2004, letter, Gottstein notified the Commissioner of an occurrence where the cloud on title adversely impacted Appellants' ability to put together a drilling program for the lease. Gottstein wrote:

> The problem is real because it is my understanding that a company decided against a drilling program in Cook Inlet to include ADL 369116 because of the cloud on title created by the Division. My

> understanding is that not only was ADL 369116 affected, but that the drilling of another lease is not occuring {sic} because of the continuing cloud on ADL's title created by the Division.[123]

The above letter was part of the record when, Allen and Donkel called the Commissioner's attention to disputed material issues necessitating a hearing and a reasonable extension on April 20, 2005. There is no evidence in the record refuting Gottstein's statement or evidence that DNR performed an independent inquiry.

The Commissioner should be keenly aware of the substantial costs of moving drilling equipment up to the Cook Inlet from the continental United States and other destinations in the world. However, given that the Commissioner never convened a hearing on the matter or invited any evidentiary supplementation, the present record is all but silent with respect to development costs associated with drilling a test well on ADL 369116. As a practical matter, a working interest owner will not be able to obtain the requisite financing to purchase, lease, or transport such equipment when the ownership of the underlying lease is in controversy.

Appellants acknowledge that the record in this matter is somewhat limited, but that is because their request for a hearing was denied and they were not otherwise permitted to supplement the record before the agency. That notwithstanding, there is evidence in the record that the clouded title adversely impacted Appellants ability to put together a drilling program.

Furthermore, that the Commissioner appears to have framed the issue in terms of whether the cloud on title interfered with Appellants' ability to negotiate with the agency

[123] Exc. 216-217.

suggests that he applied the wrong legal standard. The correct inquiry is whether the cloud on title impacted Donkel's ability to solicit investment and/or financing vis-à-vis private companies and individuals to develop a drilling program.

If there was any question as to whether the cloud on title resulted in harm to Appellants, then due process would have dictated that the Commissioner convene a hearing on the matter. Because the Commissioner based his denial of the two-year extension on an erroneous legal conclusion and factual assumptions unsupported by the record, the May 26, 2005, decision should be reversed as to this issue.

C. The Commissioner Abused His Discretion And Violated 11AAC 83.303 By Failing To Grant Appellants A Reasonable Extension Of Time To Complete Test Drilling.

The Commissioner abused his discretion and acted in an arbitrary and capricious manner by failing to consider the criteria listed in 11 AAC 83.303(a) and (b) before denying Appellants' request for a reasonable extension of the lease and by not giving adequate consideration to the impact that his failure to clear title to the lease had with respect to Appellants' ability to comply with the December 31, 2005, drilling deadline. Accordingly, Appellants request that the Court reverse the May 26, 2005, Decision as it pertains to the denial of the request for extension.

It is axiomatic that an agency is bound by the regulations it promulgates and is required to provide an adequate explanation of its decisions.[124] 11 AAC 83.303(c) provides:

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[124] *Trustees for Alaska, Alaska Center for Environment v. Gorsuch,* 835 P.2d 1239, 1244 (Alaska,1992) citing 2 Kenneth C. Davis, *Administrative Law Treatise* § 7:21 at 98

> (c) The commissioner will consider the criteria in (a) and (b) of this section when evaluating each requested authorization or approval under 11 AAC 83.301 - 11 AAC 83.395, including
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> (1) an approval of a unit agreement;
>
> (2) an extension or amendment of a unit agreement;
>
> (3) a plan or amendment of a plan of exploration, development or operations;
>
> (4) a participating area; or
>
> (5) a proposed or revised production or cost allocation formula.[125]

The above regulation prescribes a non-exhaustive list of situations in which the Commissioner must apply a multi-factor analysis. This list includes, but is not limited to, evaluating a request for an extension or amendment of a unit agreement or a plan or amendment to a plan of exploration. Though this Court has yet to have the opportunity to construe this regulation in the context of a working interest holder's request for extension of a lease, the impact of a denial of a request for extension is generally of such significant importance to the lessee and to the state as a whole that the agency should be required to provide a full explanation of its decision.[126] To ensure that the agency is not acting in an arbitrary and capricious manner, the Commissioner, at a minimum must consider the factors listed in 11 AAC 83.303 (a) and (b) in addition to the surrounding facts and circumstances when rendering a decision whether to deny a request for

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(2d Ed.1979); *Lindhag v. State, Dept. of Natural Resources*, 123 P.3d 948, 953 (Alaska 2005)

[125] 11 AAC 83.303 (c).

[126] *Lindhag*, 123 P.3d at 953; *Ship Creek Hydraulic Syndicate v. State*, 685 P.2d 715, 717-18 (Alaska 1984).

extension. As this Court observed in *Ship Creek Hydraulic Syndicate*, "[t]he very essence of arbitrariness is to have one's status redefined by the state without an adequate explanation of its reason for doing so."[127]

Here, neither the May 26, 2005, Decision, nor the record as a whole, provides any indication that the Commissioner considered the factors listed in 11 AAC 83.303 (a) and (b) when determining the fate of Appellants' interest in ADL 369116. On page 9 of that decision, the Commissioner notes that the Wagner appeal in no way interfered with Appellants' right to seek approval for proposed operations in ADL 369116.[128] Given that the Commissioner denied Appellants a meaningful opportunity to be heard on this issue, he lacks an adequate basis in fact to make this statement.

The Commissioner also notes that the "2000 Sale notice included a statement that tracts which formerly comprised ADL 369116 were not available for lease in no way compromised Appellants' right to develop the lease."[129] Conveniently, the Commissioner fails to attach any significance to the fact that not only had DNR offered one of the tracts comprising ADL 369116 for lease at the 2000 public sale, but it accepted a bid on the tract and finalized a lease agreement with Wagner in May 2001, all of which constituted action in violation of a standing court order. Furthermore, the Commissioner utterly overlooks the fact that an unresolved competing claim of ownership to a portion of the lease could conceivably impact Appellants' ability to

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[127] *Ship Creek Hydraulic Syndicate*, 685 P.2d at 717-18 quoting L. Tribe, American Constitutional Law, § 10-7 at 502-03 (1978).
[128] Exc. 261.
[129] *Id.*

assemble the necessary investment to complete the test drilling. Certainly, Gottstein's June 14, 2005, letter and Appellants' April 20, 2005, letters appealing the approval of the 2005 POD put the Commissioner on notice that the agency's inaction was impacting Appellants' ability to put together a drilling program.

Finally, in the May 26, 2005, Decision, the Commissioner concluded in effect that because Appellants did not claim that the Wagner appeal clouded title to the lease while the matter was before the superior court in Case No. 3AN-00-3616 CI, they were later barred from doing so before the agency. This conclusion is does not reflect a well-reasoned understanding of the record of the case or the law of this state.

It is wholly irrelevant whether Appellants failed to call the superior court's attention to the pending Wagner appeal at the time the superior court adopted the parties' stipulated Settlement Agreement. The terms of the Agreement were clear that Donkel, Bolt, and Kasper were not working interest owners at that time. Unocal and Forest Oil Corporation were the working interest owners of ADL 369116 and the NMGSU. It was not until late October 2003 that Unocal provided notice that it would not commit to the test drilling, thus triggering the assignment of the working interest to Donkel, Bolt, and Kasper. Donkel, Bolt, and Kasper had no reason to believe that Unocal and Forest Oil would not develop ADL 369116 as they were entitled to do under the Settlement Agreement.

As part of the Settlement Agreement, DNR had an implied obligation to provide clear title to ADL 369116 to both the working interest and royalty interest holders. As of December 2002, Appellants had no way of knowing that DNR would fail to perform its

obligations under the Settlement Agreement until mid-August 2004 and only then after the Commissioner was specifically requested to act on the matter by Gottstein.

The reasons the Commissioner proffered for denying Appellants' request for extension conflict with the only evidence presented in the record – a record which suffers greatly as a result of the Commissioner's decision to deny Appellants a hearing on disputed factual issues raised. As such, the decision is arbitrary and capricious and should be reversed.

It is also noteworthy that under the terms of the original lease agreement, Appellants would also have been entitled to an extension of the lease. The lease agreement at issue is a contract of adhesion drafted by DNR. As such, any ambiguities contained in this commercial contract must be construed in favor of Appellants.[130] Appellants maintain there has been a well on the lease since the 1960's, when Pan Am Petroleum Corp. drilled well No. MGS 18743.[131] Paragraph 4(d) of ADL 369116 provides for an automatic extension of the lease if there is a well on the leased area capable of producing hydrocarbons in paying quantities.[132] As recently as January 2000, DNR acknowledged that the acreage under ADL 369116 is underlain by gas.[133] Indeed, the Pan American MGS State 18743 #1 well, drilled in 1964 (currently located on ADL 369116) flowed gas at 3.4 MMCF per day and was

[130] *See Uncle Joe's Inc. v. L. M. Berry and Co.*, 156 P.3d 1113, 1118 (Alaska 2007); Restatement (Second) of Contracts § 206 cmt. a (1981).
[131] Exc. 074; Exc. 284-285; Exc. 344-350.
[132] Exc. 023.
[133] Exc. 350.

certified by the State as capable of producing paying quantities based on that data.[134] 11 AAC 83.395 defines "paying quantities" to mean "quantities sufficient to yield a return in excess of operating costs . . .."[135] Though there is no evidence in the record supporting the Commissioner's conclusion in his January 5, 2000 letter that the well was ever plugged and abandoned (as opposed to being left in suspended status), by DNR's own admission, paying quantities still exist beneath ADL 369116.[136] The issue whether the well on ADL 369116 was plugged as of May 2005 presents yet another disputed question of material fact. Further, paragraph 4(d) provides that in order to terminate a lease with a well on it, the State must provide at least six months' notice to the lessee to place the well into production. The record does not reflect that notice was provided prior to termination of the lease. Hence, DNR violated paragraph 4(d) and breached the underlying lease agreement when it terminated ADL 369116.

DNR also breached the underlying lease agreement when it terminated ADL 369116 in violation of paragraph 4(f) of that Agreement. Paragraph 4(f) provides that "[i]f the state determines that the lessee has been prevented by a force majeure, after efforts made in good faith, from performing any act that would extend the lease beyond the primary term . . ." and "[i]f the force majeure occurs during an extension of the primary term . . . the lease will not expire during the period of the force majeure plus a reasonable time after that period . . .."[137] Paragraph 34(7) defines a

[134] *Id.*
[135] 11 AAC 83.395(4).
[136] Exc. 350.
[137] Exc. 023.

force majeure to include "judicial decisions or lack of them."[138] Under the circumstances, DNR should have reasonably concluded that its own delay in rendering an adjudicative decision on the Wagner appeal would have triggered a force majeure extension under the lease and that Appellants should not, in fairness, be punished for the Commissioner's delay.

On appeal before the superior court, DNR argued that the language of the lease agreement was superseded by paragraph 13 of the Settlement Agreement and is therefore irrelevant.[139] This argument is without merit. The Court construes language containing a waiver of rights narrowly.[140] Paragraph 13 of the Settlement Agreement contemplates a situation where the State fully performs under the agreement but the other parties do not. Such was not the case here. Paragraph 13 provides in relevant part:

> Upon termination of the North Middle Ground Shoal Unit Agreement and ADL 369116 for failure to meet the requirements of paragraphs 11 and 12, the acreage within ADL 369116 will become immediately available for lease by the state. In such event, notwithstanding any contrary provisions of any statute, regulation, or agreement, Appellants specifically waive any rights under existing statute, regulations, or agreements, which would preclude immediate termination of the unit and the lease.[141]

DNR failed to perform fully under the Settlement Agreement when it delayed clearing title to the lease for over one half of the term of the lease extension

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[138] Exc. 028; *see also* 11 AAC 83.395(3).
[139] Exc. 335-348.
[140] *Denardo v. Calasta Corp.*, 111 P.3d 326, 333 (Alaska 2005) citing *Godfrey v. Hemenway*, 617 P.2d 3, 8 (Alaska 1980).
[141] Exc. 162.

negotiated in the Settlement Agreement. In violation of their due process rights, Appellants were denied the opportunity of a hearing to further develop the record on this issue. Nonetheless, there is evidence in the record that the cloud on title had a negative impact on Appellants' ability to put together a drilling program by the December 31, 2005 deadline established under paragraph 7 of the Settlement Agreement. Consequently, DNR cannot as a matter of law rely on any wavier of rights contained in the Settlement Agreement.[142] Equitably, Donkel's waiver of rights would only be effective had the state performed its implied obligation to clear title and had not otherwise breached the implied covenant of good faith and fair dealing. Because DNR did not perform a material obligation under the Settlement Agreement, it should be estopped from relying on any waiver of pre-existing rights contained in paragraph 13.[143]

Fairness dictates that DNR not be able to take advantage of any waiver found in paragraph 13 when its own inaction created the obstacle to Appellants' performance under the settlement agreement. As such, the terms of the lease agreement remain applicable notwithstanding the Settlement Agreement.

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[142] *See Grace v. Insurance Co. of North America*, 944 P.2d 460, 464 (Alaska 1997). (holding an insured's failure to comply with an obligation under the contract if a material breach on the part of the insured was shown); *Kennedy Associates, Inc. v. Fischer*, 667 P.2d 174, 178 (Alaska 1983) (holding that "in general, the non-occurrence of a condition precedent precludes an action by the promisee to enforce the contract").

[143] *Cf. Yates v. Halford*, 73 P.3d 1236, 1241 (Alaska 2003); *McCormick v. Grove*, 495 P.2d 1268, 1269 (Alaska 1972) ("A trial court may in its discretion refuse to enforce the forfeiture provisions of a contract if the equities of a particular situation so dictate.").

D. DNR Breached The Covenant Of Good Faith And Fair Dealing Implied In The 2002 Settlement Agreement In Superior Court Case No. 3AN-00-3616 CI.

The Settlement Agreement between DNR and Donkel[144] is a contract and like any contract, it contains an implied covenant of good faith and fair dealing.[145] This implied covenant requires that DNR act in good faith and not act to deprive Appellants of the explicit benefits of the contract.[146] As part of the implied covenant of good faith and fair dealing, DNR was required to proceed in good faith to clear title to ADL 369116. As this Court has observed, "[w]here a duty of one party is subject to the occurrence of a condition, the additional duty of good faith and fair dealing . . . may require . . . refraining from conduct that will prevent or hinder the occurrence of that condition or . . . taking affirmative steps to cause its occurrence."[147]

DNR breached the covenant of good faith and fair dealing by waiting almost two years to issue a final decision in the Wagner appeal all the while leaving Appellants (Donkel, in particular) with clouded title to the lease. The Commissioner's response to Appellants' arguments concerning the cloud on title is twofold. First, the Commissioner effectively denies that a cloud on title ever existed. For the reasons discussed in Section IV(B), *supra*, the Commissioner's explanation is flawed because it is inconsistent with record and Alaska law. Second, the Commissioner attempts to shift the blame to

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[144] Unlike Donkel, Allen was not a party to Case No. 3AN-00-3616 CI and therefore was not a party to the Settlement Agreement reached in that case.
[145] *See Exxon Corp. v. State*, 40 P.3d 786, 797-78 (Alaska 2002).
[146] *Ramsey v. City of Sand Point*, 936 P.2d 126, 133 (Alaska 1997).
[147] *Casey v. Semco Energy, Inc.*, 92 P.3d 379, 384 -385 (Alaska 2004) quoting *Gordon v. Foster, Garner & Williams*, 785 P.2d 1196, 1199 n. 6 (Alaska 1990) (citation omitted).

Appellants concluding that the failure to object to the cloud on title resulted in some kind of waiver of rights. At the time the Settlement Agreement was signed, Donkel's working interest ownership rights were contingent on Unocal and Forest Oil Corporation not committing to developing the lease. Donkel had no way of knowing that Unocal and Forest Oil would change their position one year later or that DNR would delay the final resolution of the appeal for more than another year and a half after the Settlement Agreement was signed. Under the circumstances, in order to comply with its obligation to proceed in good faith, DNR would have had to clear title to the lease within a reasonable time following the execution of the Settlement Agreement—not over one and a half years into a three-year lease extension.

DNR also breached the implied covenant of good faith and fair dealing when it terminated the lease in violation of paragraphs 4(d) and 4(f) of the original lease agreement. As previously discussed, DNR breached the terms of the underlying lease agreement by failing to extend the term of the lease as required by paragraphs 4(d) and 4(f) of the lease agreement governing ADL 369116. Paragraph 4(d) provides for an automatic extension of the lease agreement if there is a well on the lease capable of producing oil and gas in paying quantities. Appellants maintain that there has been a well on ADL 369116 since the 1960's.

Similarly, paragraphs 4(f) and 34(7) of the lease agreement together provide that in the event of a delay caused by a judicial decision or the lack of a judicial decision, Appellants are entitled to a reasonable extension of the lease. In this case, the delay in the judicial or adjudicative decision is solely attributable to the Commissioner's failure to

render a final decision on the Wagner appeal in a timely fashion. As such, DNR breached is covenant of good faith and fair dealing at the same time it breached paragraph 4(f) of the lease agreement.

Finally, DNR breached the covenant of good faith and fair dealing by failing to exercise its discretion to extend the term of the lease to offset the interruption to Appellants' operations caused by the cloud on title. Because DNR failed in its implied duty to resolve the Wagner appeal in a timely fashion, it was not objectively reasonably for it to hold Appellants accountable for the agency's own mistake.

To date, DNR has provided no explanation for the delay. As previously discussed, the legal and factual issues surrounding Wagner's appeal were not complicated. DNR had already admitted that the Division did not have the authority to offer the tract because of the court order in *Donkel, et al. v. State*. All DNR needed to do to dispose of the Wagner appeal was to issue a decision reaffirming the grounds for its termination of the lease. Had Appellants been provided with clear title to ADL 369116 at the time the Settlement Agreement was signed or shortly thereafter, they could have used the full two years following Unocal's notice of non-commitment to garner the private support and equipment necessary to develop the lease. As a result of DNR's inaction, Donkel was denied benefits guaranteed by the Settlement Agreement.

Though the question of DNR's bad faith with respect to the Wagner appeal was raised by Allen and Donkel in their April 20, 2005 letters to the Commissioner, the Commissioner failed to address these claims in its May 26, 2005 Decision or at any time thereafter.

As was previously discussed, Appellants were not provided a hearing on this or any of the other issues they raised. Due to the fact that Appellants' claim for breach of good faith and fair dealing calls into question the propriety of an agency action, Appellants are required to raise it as an administrative appeal.[148] Because DNR has failed to objectively scrutinize its own actions throughout the course of this appeal, Appellants respectfully request that this issue be remanded to an impartial forum to develop a record on the question whether DNR breached its covenant of good faith and fair dealing.[149]

E. The Commissioner Erred By Concluding That Unocal's 2005 POD Was In The State's Best Interest.

1. The Commissioner did not specifically identify which criteria listed in 11 AAC 83.303(b), he any, it considered before rendering the final decision of the agency.

An administrative agency must make findings of fact and conclusions of law regarding all issues that are both "material" and "contested."[150] If these findings or conclusions are insufficient to permit intelligent appellate review, the matter must be remanded to the agency for further deliberation.[151] Findings are adequate to permit appellate review when at a minimum, they show that the agency considered each issue of significance, demonstrate the basis for its decision, and are sufficiently detailed.[152] Consistent with this principle, 11 AAC 83.303 imposes an obligation upon the

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[148] *See, e.g., Fairbanks N. Star Borough v. State*, 826 P.2d 760, 762 (Alaska 1992); *see also Fedpac Int'l, Inc. v. State, Dep't of Revenue*, 646 P.2d 240, 241 (Alaska 1982).
[149] *See State v. Lundgren Pac. Constr. Co.*, 603 P.2d 889, 890 (Alaska 1979).
[150] *Bolieu v. Our Lady of Compassion Care Ctr.*, 983 P.2d 1270, 1275 (Alaska 1999).
[151] *Lindhag*, 123 P.3d at 953.
[152] *Id.*

Commissioner to specifically consider the list of factors contained in 11 AAC 83.303 (a) and (b) before approving a plan or amendment of exploration, development or operations.[153] Neither the March 31, 2005 letter from the Director of the Division nor the Commissioner's May 26, 2005 Decision approving the 2005 POD permit intelligent appellate review. As such, to the extent the Court does not otherwise rectify the violations of due process and state law by reinstating Appellants' property rights in ADL 369116, Appellants request that the matter be remanded to the agency for further deliberation.

Of paramount importance in evaluating a plan of development is whether the plan will promote conservation of all natural resources, including all or part of an oil or gas pool and the prevention of economic and physical waste and provide for protection of all parties.[154] Neither the March 31, 2005, decision of the Director of the Oil and Gas Division nor the May 26, 2005, Decision from the Commissioner (affirming that the March 31, 2005, decision) take into account the impact of the plan on the other working interest owners in the NMGSU. Nor do either of these decisions provide anything more than conclusory statements that the factors in 11 AAC 83.303 were considered and that approval of the 2005 POD is in the best interest of the state. This does not provide Appellants with an adequate basis to understand and evaluate the decision reached by the agency. Given the impact that the approval of the 2005 POD might have had on Appellants' ability to develop ADL 369116, Appellants are entitled to more than a cursory recitation of the regulatory standard.

[153] 11 AAC 83.303 (c) (3).
[154] 11 AAC 83.303 (a).

For example, Appellants are entitled to an explanation as to how the 2005 POD prevents economic waste. After all, the oil and gas reserves in the NMGSU benefit the state as a whole. Unocal initially identified a break even point of $57 per barrel when it ceased production in 2002.[155] However, nothing in the record supports the conclusion that $57 per barrel remained the economic threshold at the time the Commissioner approved the 2005 POD. Since 2002, the price of oil has increased exponentially, raising the question overlooked by the Commissioner—whether Unocal's failure to continue operations in the NMGSU represents economic waste to the State.

The Commissioner's May 26, 2005 Decision approving the 2005 POD also fails to take into account the comments of the Oil and Gas Conservation Commissioner. In response to Unocal's 2005 plans to abandon the Baker and Dillon wells, the Chairman of the Commission stated in a letter dated January 7, 2005: "the Commission recognizes that much oil remains in place in the developed reservoirs, deeper exploration opportunities may exist that could only be exploited by the existing platforms, and other beneficial uses of the platforms may exist."[156] This letter was copied to the Director of Oil and Gas. Hence, even the Oil and Gas Commissioner took the position that there was a need to keep the platform in working order and to develop hydrocarbon deposits beneath ADL 17595 and the NMGSU. What DNR fails to appreciate is that if these oil and gas resources are to be developed at all, even with the current price of oil, it will be through the efforts of small oil producers. Removal of the Baker platform and the

[155] Exc. 180-181.
[156] Exc. 227.

cessation of drilling in the NMGSU were not in the best interest of the state at the time the 2005 POD was approved.

Appellants request that to the extent relief is not otherwise granted, restoring Appellants' rights in ADL 369116 and the NMGSU, the matter be remanded to the agency to explain the basis for its decision and specifically address which factors it considered to be determinative of the issue.

2. The Commissioner failed to fully take into account the impact of the 2005 POD on the working interest holders and overriding royalty interest holders of the unit.

The Commissioner erred in approving the 2005 POD because he failed to take into account the potential adverse impact that the plan would have on the other working interest holders of the NMGSU. Specifically, the Commissioner did not take into account the full impact that the dismantling of the Baker platform might have on the continued development of ADL 369116.

Pursuant to 11 AAC 83.303 (b)(6), the Commissioner is required to consider "any relevant factors, including measures to mitigate impacts" caused by the proposed plan of development.[157] One of the key factors in determining whether a plan of development is in the best interest of the state is the impact that the plan may have on the other working interest owners of the unit. Because Appellants were denied the opportunity to present evidence of the potential adverse impact that the

[157] 11 AAC 83.303 (b)(6).

2005 POD would have on plans to develop ADL 369116, the Commissioner did not have they necessary information before him to make an informed decision.

As is evident from the May 26, 2005 Decision, the Commissioner did not fully appreciate the impact that abandonment of the Baker platform would have on the working interest owners of ADL 369116. Because Appellants were never given the opportunity to develop a record before the agency on this issue, they request that the matter be remanded to an impartial forum to conduct an evidentiary hearing.

F. The Commissioner Erred By Terminating ADL 396116 And The North Middle Ground Shoal Unit.

It is not clear whether the superior court intended that the February 15, 2008, Decision on Appeal also dispose of Appellants' appeal of the Commissioner's April 24, 2006, Final Decision and Order affirming the termination of ADL 369116 and the NMGSU (appealed in Case No. 3AN-06-8419 CI). That notwithstanding, Appellants maintain that because of DNR's numerous constitutional and statutory violations (discussed *supra*), the Commissioner erred in terminating ADL 369116 and the NMGSU.

If the Court concludes that DNR violated Appellants' due process rights, Appellants respectfully request that the Commissioner's April 24, 2006, Final Decision and Order be vacated and that that the NMGSU and ADL 369116 be reinstated consistent fairness and substantial justice.

V. CONCLUSION

Fundamentally, this is a case about due process. It began nearly ten years ago with DNR taking the position that Donkel and other ORRI owners of ADL 369116 were not

entitled to notice or an opportunity to be heard before the agency issued a decision which effectively terminated the lease. DNR lost that issue on appeal to the superior court in *Donkel, et al. v. State*, pursuant to a Settlement Agreement, DNR reinstated the lease with a three-year extension to conduct test drilling but did not clear title to the lease until over half the duration of the extension had passed. When Appellants brought their concerns to the agency's attention, the Commissioner was dismissive, even though it was his own error. When Appellants requested a hearing on factual and legal issues regarding the NMGSU and ADL 369116, the Commissioner denied their request. At every stage of the proceeding, the Commissioner denied Appellants due process protections of state and federal law.

DNR may argue that it was justified in breaching the terms of the lease agreement, failing to clear title to the lease in a reasonable time, denying Appellants a hearing on disputed factual issues, and declining to exercise its discretion to extend the lease according to the terms of the Settlement Agreement. Though any one of the agency's actions might not result in reversible error, when viewed in the aggregate, there is little question that Appellants were denied due process of law.

For the foregoing reasons, the Commissioner's May 26, 2005 and April 24, 2006 Decisions, which approved the 2005 POD and denied Appellants' request for a hearing and two-year extension and terminated ADL 369116 and the NMGSU, should be vacated. Consistent with principles of due process and substantial justice and consistent with the express terms of the of the Settlement Agreement, which authorizes DNR to extend the term of the lease, Appellants' property rights in ADL 369116 and the NMGSU

should be reinstated with an uninterrupted extension of two years, from the later of the issuance of the this Court's decision or the time from which appeal may be taken from this Court's decision, to complete the drilling of an initial test well. Appellants also request that this Court order that neither the State nor DNR interfere with Appellants' ability to develop the lease during the term of the extension. In the event that this Court grants Appellants' request, it need not remand the matter to the agency or an impartial forum on the other factual issues presented. Appellants believe that the best interests of the State would be served by reinstating their property rights without further expense to the parties and without further delaying the development of the proven oil and gas in ADL 369116.

To the extent that the record does not support the reinstatement of Appellants' property rights at this time, Appellants request that the matter be remanded to an impartial hearing officer to convene an evidentiary hearing and/or *de novo* trial.

DATED at Anchorage, Alaska this ____ day of August, 2008.

By: _____
Christopher M. Brecht
Alaska Bar No. 0611089

By: _____
William M. Bankston
Alaska Bar No. 7111024

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing (typed in Times New Roman 13) was mailed to the following attorney(s) on the _____ day of August, 2008:

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_____
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