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Robert K. Corbin

May 11, 1987

Mr. M. J. Hassell, Acting Commissioner
Arizona State Land Department
1624 West Adams
Phoenix, Arizona 85007

Re: I87-065 (R87-031)

Dear Mr. Hassell:

We are writing in response to your February 2, 1987 inquiry concerning the nature and ramifications of the state's reservation of a one-sixteenth mineral interest in all state lands sold between July 9, 1954 and March 18, 1968. You asked whether the reservation is of one-sixteenth of the actual minerals or merely of a one-sixteenth royalty interest. In addition, you asked various questions concerning the State Land Department's rights with respect to production of the minerals if the state reserved an interest in the minerals themselves rather than a mere royalty interest.

The ability of the State Land Department ("Department") to reserve minerals in sales of state lands is prescribed by the legislature. Campbell V Flying v. Cattle Co., 25 Ariz. 577, 220 P. 417 (1923). Therefore, the nature and extent of the reservation must be determined through an interpretation of the statute which allowed that reservation, A.R.S. § 37-231(C).^{1/}

^{1/}The pertinent statutory provisions are as follows:

C. All sales, grants, deeds or patents to any state lands sold between July 9, 1954, and the effective date of this section [March 18, 1968] shall be subject to and shall contain a reservation to the state of an undivided

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The operative language for the reservation itself is contained in the introductory portion of subsection (C). That subsection provides that all sales during the relevant period "shall contain a reservation to the state of an undivided one-sixteenth of all oil, gases . . . or any other material which is or may be determined . . . to be peculiarly essential to the production of fissionable materials" There is no language in the clause discussing the statutorily required reservation which suggests that the reservation is to be anything other than a reservation of an interest in the minerals themselves.

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one-sixteenth of all oil, gases and other hydrocarbon substances, coal or stone, metals, minerals, fossils and fertilizer of every name and description, together with all uranium, thorium, or any other material which is or may be determined by the laws of the state, the United States, or decisions of courts to be peculiarly essential to the production of fissionable materials, whether or not of commercial value, subject to the following:

1. For the purpose of promoting the sale of state lands and the more active cooperation of the owner of the soil, and to facilitate the development of its mineral resources, the state constitutes the purchaser of the land, its agent for the purposes specified in this section, and in consideration hereof, relinquishes to and vests in the purchaser of the state land an undivided fifteenth-sixteenths of all oil, gas and the value thereof which may be upon or within any state land purchased after July 9, 1954 and before the effective date of this section.

2. The purchaser of the soil may sell or lease to any person, firm or corporation the oil and gas and other minerals which may be on

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Subsection (C), however, makes the reservation of minerals "subject to" certain conditions. The use of the term "subject to" in a statute means that the provisions following that phrase limit the rights preceding it. Anderson v. Southwest Savings and Loan Association, 117 Ariz. 246, 248, 571 P.2d 1042, 1044 (App. 1977). Therefore, although the reservation appears to constitute the reservation of a mineral interest, the manner in which the state may exercise its rights in the interest and, consequently, the nature of the interest itself, are limited by the provisions in the numbered paragraphs contained in subsection (C).

A.R.S. § 37-231(C)(1) and (2) set forth the manner in which the state will realize its interest. The purchaser of the soil is appointed the state's agent for purposes of the

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or in the land, upon terms and conditions the purchaser and the owner deem best, subject to the provisions and reservations of this section, but the lessee or purchaser shall pay to the state an undivided one-sixteenth of the mineral produced or the value thereof at the well or mine as determined by the state land department.

3. Upon discovery of oil and gas in paying quantities on land adjoining state lands purchased under the authority of this section, the purchaser or his lessee shall drill and produce all wells necessary to protect the land so purchased from drainage by wells on lands in which the state has no royalty interest, or has a lesser royalty interest. If the purchaser or his lessee fails to protect against such drainage, the state, acting through the state land department, may, three months after demand therefor in writing by the state land department to such purchaser and his lessee, enter upon such lands and drill all wells necessary to protect the state against such drainage.

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reservation. The purchaser of the soil is given the right to sell or lease "the oil and gas and other minerals which may be on or in the land." This right to sell or lease includes all the minerals and is not limited to the fifteenth-sixteenths interest which is vested in the purchaser of the soil in consideration of the purchaser's acting as the state's agent.

The purchaser of the soil is given complete control over the terms and conditions under which he may sell or lease the minerals. The statute requires only that the state be paid "an undivided one-sixteenth of the mineral produced or the value thereof at the well or mine." Therefore, the statute provides that the state's only compensation for its interest will be one-sixteenth of the minerals or their value as produced. By appointing the purchaser of the soil the state's agent and thereby relinquishing the right to enter upon the lands to mine the one-sixteenth interest, the statute strips the reserved interest of one of the major incidents of a mineral interest, the right to lease. The owner of a royalty interest has no such right. 1 WILLIAMS AND MEYERS, OIL AND GAS LAW, § 303.3, pages 455, 456.

The fact that the state intended to relinquish its right to mine or lease its interest is further reflected in A.R.S. § 37-231(C)(3). That subsection provides that the purchaser of the soil must drill offset wells if wells on adjoining property are threatening to drain the interest of the state. The subsection goes on to provide that the state, after certain notice requirements, may enter upon the land and drill the necessary offset wells if the purchaser of the soil refuses. A method by which the state can give notice and then enter the property in certain circumstances would be unnecessary if the state possessed that ability merely by its reservation, which would be the case if an unqualified mineral interest had been reserved. That the state did not reserve the right to enter the property for exploration or production purposes supports the interpretation that the interest reserved is in fact a royalty interest.

This conclusion is reinforced by the use of the term "royalty interest" in A.R.S. § 37-231(C)(3). It refers to land adjoining state lands purchased under the authority of the section as "lands in which the state has no royalty interest, or has a lesser royalty interest." Mention there of a lesser "royalty interest" on adjoining land indicates the legislative

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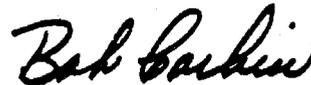
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intent to reserve a royalty interest on the subject property. As the owner of a royalty interest, the state should receive one-sixteenth of the amount of minerals produced or their value, free of costs of production. 1 WILLIAMS AND MEYERS, OIL AND GAS LAW, § 303.1, pages 450-451; see also, Superior Oil Company v. Vanderhoof, 307 F.Supp. 84 (D. Mont. 1969).

You asked whether, assuming the state retains an actual interest in the minerals, that interest can be satisfied by a miner leaving the last one-sixteenth of the minerals in the ground and designating that the state's portion. Because the state retains a royalty interest, it is entitled to receive one-sixteenth of the amount of minerals produced or their value, free of costs of production.

You also asked what authority the state has to issue leases or permits to explore or mine its retained interest in the minerals. Because we conclude that the state retains only a royalty interest in the minerals of the subject land, the state has no authority to explore or mine the minerals and therefore no authority to issue leases or permits to others to do so.

Sincerely,



BOB CORBIN
Attorney General

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