Denver Law Review

Volume 43
Issue 1 *Symposium - Oil Shale*

Article 10

January 1966

Vol. 43, no. 1: Full Issue

Denver Law Journal

Vol. 43, no. 1: Full Issue

DENVER LAW JOURNAL

VOLUME 43

1966

DENVER LAW JOURNAL

VOLUME 43 1966 NUMBER 1

Published by

The University of Denver College of Law

Editor's Note

The members of the Journal staff, and everyone connected with the College of Law, wish to thank the readers for their response to our request for subscriptions. We hope to justify your confidence in us by continuing the recent improvements which have been made in both the quality and the size of the Journal (then published as the *Denver Law Center Journal*).

Future issues will feature articles on such subjects as: Oil and Gas Financing under the Uniform Commercial Code, the Colorado Deadman's Statute, and Estate and Gift Taxation. Also scheduled for a later issue are two articles dealing with Trusts and their use in Estate Planning.

As in the past, the Denver Law Journal welcomes the submission of articles from attorneys and law professors. Although we are prevented by the limitations of space from using all the material sent to us, each article will be given our full consideration.

Richard M. Koon
Editor in Chief

Denver Law Journal

VOLUME 43 1966 NUMBER 1

OIL SHALE SYMPOSIUM

ARTICLE

BOOKS RECEIVED

Published quarterly and copyrighted 1966 by the Denver Law Journal and University of Denver College of Law, 200 West 14th Avenue, Denver, Colorado 80204.

Subscription rates: $5.00 per year in the U.S., $6.50 per year in foreign countries. Individual copies: Regular issues $1.50, symposium issues $2.00.

Advertising agent: Business Manager, Denver Law Journal, 200 West 14th Avenue, Denver, Colorado 80204, 292-2916.

Denver Law Journal

VOLUME 43 1966 NUMBER 1

Oil Shale: Introduction and Perspective

There appears to be no question that the potential value of Colorado's untapped oil shale reserves represents a "bonanza" far in excess of the wildest dreams of the old gold rush prospectors, dwarfing the uranium boom of the 1950's.[1] Whether efforts to develop these vast deposits will succeed in opening a treasure chest or a Pandora's box depends substantially upon the manner in which the Federal Government evolves policy for the orderly development of oil shale reserves. The American citizen is the major stockholder; his Government owns an estimated 72 per cent of the oil shale lands of the Green River formation[2] — which contains almost ten times the known oil shale reserves in all the rest of the world.[3] These lands are the richest, too, carrying perhaps 900 billion gallons of oil in deposits rated upward from 15 gallons per ton.[4] Little wonder, then, about the rekindled interest in finding ways and means of converting this vast treasure into productive wealth.

Despite the current swelling of interest in oil shale, oil from shale deposits has been produced commercially for more than a century, principally in oil-short Europe.[5] After a brief period of production in the period immediately preceding the Civil War, the infant United States oil shale industry folded upon discovery of the major petroleum deposits in Pennsylvania.[6] The ease with which new deposits of petroleum were found and put into production caused interest in the relatively high-cost oil shale to diminish.[7] Only in recent years have the oil industry and the Federal Government stepped up research efforts to a significant degree.[8]

---

[1] A national petroleum trade publication computes the value of recoverable oil in the shale deposits of the Green River Formation at $2,577,000,000,000 (OIL AND GAS JOURNAL, March 9, 1964, p. 65) [hereinafter cited as OIL AND GAS JOURNAL].

[2] Childs, *The Status of the Oil Shale Problem,* QUARTERLY OF THE COLORADO SCHOOL OF MINES, July 1965, p. 2.

[3] U.S. BUREAU OF MINES, BULL. No. 611, OIL SHALE MINING, RIFLE, COLO., 1944-56. Table 2, p. 4 (1964).

[4] Childs, *supra* note 2 at 1.

[5] U.S. BUREAU OF MINES, BULL. No. 611, *supra* note 3 at 4.

[6] *Ibid.*

[7] OIL AND GAS JOURNAL, p. 33.

[8] *Ibid.*

I. TECHNOLOGY

A major impediment to production of oil in commercial quantities from shale has been the cost of extracting oil from the tough matrix-like rock in which it is contained.[9] Because of its peculiar chemical properties the solid hydrocarbon — kerogen — must be separated from the marlstone, of which it is a part, by application of heat. At 800 to 900 degrees the kerogen decomposes into a liquid oil similar to petroleum crude, leaving about 25 per cent in a solid state similar to coke.[10]

The liquid itself is a highly viscous oil which is a slushy solid at room temperature, and has a pour point of between 90 and 100 degrees F. Thus it must be partially refined before it can be transported by pipeline.[11]

The ore may be mined by conventional means, crushed and retorted on the surface. A plant having a capacity of 40,000 barrels of oil per day is considered the minimum for economic success;[12] such a plant would represent, including mining development costs and a share of research expenditures, a capital outlay of approximately $100,000,000 — this before realizing a cent from production.[13] And in the absence of a Federal policy directed toward oil shale, only the conventional mining depletion rate of 15 per cent is available, compared with a 27½ per cent depletion rate for crude oil.[14] Further, the status of shale oil with respect to a refiner's import quota has not been determined, and if no credit is given the shale oil must absorb a price penalty proportionate to the reduction of the refiner's import quota.[15]

Despite these factors, industry spokesmen think shale oil can now be produced as cheaply as the average barrel of crude, and one trade publication has indicated a 1970 date as most realistic for "on stream" commercial production.[16]

II. LAND STATUS

The status of oil shale lands adds to the complexity of the picture. The Green River formation comprises some 896,000 acres in Colorado, 2,700,000 acres in Utah, and 460,000 acres in Wyo-

---

[9] *Id.* at 79.

[10] Lekas & Carpenter, *Fracturing Oil Shale With Nuclear Explosives for In-Situ Retorting,* QUARTERLY OF THE COLORADO SCHOOL OF MINES, July 1965, p. 21.

[11] OIL AND GAS JOURNAL, p. 71.

[12] *Id.* at 69.

[13] *Id.* at 80.

[14] *Id.* at 76.

[15] *Id.* at 80.

[16] *Id.* at 65.

ming.[17] In 1914 the lands were open to homesteading with mineral rights reserved,[18] and six years later the lands were made subject to the Mineral Leasing Act of 1920.[19] President Hoover in 1930 withdrew the classified oil shale lands from entry on a "temporary" basis for the purpose of "investigation, examination, and classification."[20] It is of interest to note that during the 10-year period between the effective date of the Mineral Leasing Act and the executive order withdrawing lands from location no leases were issued.[21] Meanwhile, in 1916 and 1924 three large tracts of land in Utah and Colorado were withdrawn from entry as a future source of oil for the Navy;[22] the Colorado tracts comprise 38,700 acres with an estimated content of 5 billion barrels of oil in deposits rating 25 gallons per ton.[23] Further, under terms of the Multiple Mineral Development Act of 1954,[24] certain of the lands in the oil shale area have been opened to location for conventional petroleum exploration.

Thus the picture of land status is mottled. Basically, homestead entries made prior to July 17, 1914, carry with them mineral rights; subsequent to that date mineral rights for homestead lands are retained by the Federal Government. Patents issued prior to November 11, 1920, are generally considered unassailable.[25] Placer mining claims made prior to that date are open to question; some have been patented in subsequent years.[26]

Following the decline of the early oil shale boom in 1926, many of the estimated 30,000 claims were abandoned.[27] A series of contest actions initiated by the Federal Government resulted in declarations that claims were void for failure to perform requisite annual development work.[28] But in 1935 the Supreme Court resolved the question by holding that the requirement for annual work did not apply to oil shale claims.[29] Then, in a significant holding in

---

[17] U.S. BUREAU OF MINES, BULL. No. 611, *supra* note 3 at 14.

[18] 38 Stat. 509 (1915), 30 U.S.C. § 122 (1942).

[19] 41 Stat. 437 (1921), 30 U.S.C. § 22 (1942).

[20] Exec. Order No. 5327, April 15, 1930.

[21] U.S. BUREAU OF MINES, BULL. No. 611, *supra* note 3 at 15.

[22] *Ibid.*

[23] PRIEN, *Oil Shale* in MINERAL RESOURCES OF COLORADO, 452 (1960).

[24] 68 Stat. 711 (1954), 30 U.S.C. § 527 (1942).

[25] United States v. Chandler-Dunbar Water Power Co., 209 U.S. 447 (1907).

[26] Records of the Colorado Land Office, U.S. Bureau of Land Management, indicate 269 oil shale patents covering 1,750 claims have been issued in the last 45 years. See Meek, *Records, Documents, and Service of the Colorado Land Office, Bureau of Land Management,* this edition, *infra,* p. 85.

[27] Meek, *supra* note 26 at 85.

[28] See Lohr, *Conclusiveness of United States Oil Shale Placer Mining Claim Patents,* this edition, *infra,* pp. 35-37.

[29] Ickes v. Virginia-Colorado Dev. Corp., 295 U.S. 639 (1935).

1964, the Solicitor of the Department of the Interior held that the 1935 Supreme Court decision did not apply retroactively to claims voided prior to that date by departmental action.[30] Even though the Department might have been in error, he said, cancellations which were neither appealed from nor attacked over a period of 25 years could not now be reopened to inquiry, being barred by "the principles of res judicata, finality of administrative action, and laches."[31] With millions of dollars potentially at stake, it is undoubted that final determination of the question must await completion of the lengthy process of appeal through the Federal courts. Further, the unsettled circumstances have raised questions as to the conclusiveness of all patents issued since 1920. And of an estimated 30,000 claims recorded in the Colorado office of the Bureau of Land Management, nearly one-fourth are still considered representative of "administrative problems" to the Land Office.[32]

III. ECONOMIC FACTORS

The status of the land itself is but one of the problems encountered in analyzing prospects for oil shale development. The effects of a burgeoning oil shale industry upon the economy of the state, nation, and world must also be considered.

If ore carrying 10 gallons per ton is considered, the Green River formation contains at least 2 trillion barrels of oil, or 25 times the amount of oil produced to date from all sources by the United States.[33] An "open door" policy toward oil shale would cause enormous dislocation of the oil industry as now constituted. The regulation of oil imports by the United States maintains a fine balance predicated upon consideration of domestic production, exploration, and development; maintenance of adequate domestic reserves for national defense purposes; conservation of resources; dollar balances involving oil-producing nations; competition with the Communist bloc for economic and political considerations abroad; policy toward research and development of other fuel sources, *i.e.,* tar sands and atomic energy.

Domestic economic implications are equally complicated. There is enough oil in Green River shales to constitute 189 East Texas oil fields, enough potential wealth to pay off the national debt with $11,000 left over for every man, woman, and child in the United

---

[30] Union Oil Co., 71 Interior Dec. 169 (1964).

[31] *Id.* at 185.

[32] Meek, *supra* note 26 at 85.

[33] Childs, *supra* note 2 at 1.

States.[34] A continued increase in the cost of finding crude could shift substantial attention to shale oil; revision of depletion allowances to favor shale oil could have a similar effect. Yet a major crude oil find discovered subsequent to multi-million dollar commitments by the oil industry to shale operations could burst the bubble overnight.[35]

IV. Water Problems

A thriving oil shale industry will require vast quantities of water, not only for the anticipated metropolitan area of 340,000 persons envisioned by one researcher for western Colorado,[36] but also for the refining process essential prior to pipeline transportation of the oil. Thus provision must be made for the acquisition of water in quantities estimated at up to 455,000 acre feet per year.[37] It is not at all certain that oil shale industry representatives are fully aware of the legal complexities surrounding acquisition, diversion, and retention of water rights. It is disconcerting, for example, to hear an industry expert dismiss the question of water rights as being a simple market place transaction whereby "some of the poorer farms which are now using water will be purchased, and water from them will be stored and used for oil shale processing and the related communities."[38] While water may become available to the extent that it is needed, as need increases so does price. Reliance upon purchase of existing irrigation rights to supply projected oil shale requirements could well price the industry out of existence.

In view of the interest of the Federal Government in the orderly exploitation of oil shale reserves, the problem of water allocation could be solved by the Secretary of the Interior, who serves both as master of the Colorado River Basin by Supreme Court edict,[39] and as custodian of the public lands held in trust for the American people. Coordination of these two aspects of the Department of the Interior's responsibilities through initiation of planning for capture and retention of now-surplus flood waters has been advocated as one means of insuring adequate water for oil shale at a reasonable price.[40]

---

[34] Oil and Gas Journal, p. 65.

[35] *Ibid.*

[36] Prien, *op. cit. supra* note 23 at 458.

[37] Colorado Conference Committee, *Water Requirements of an Oil Shale Industry,* Sept. 24, 1953.

[38] Ertl, *Mining Colorado Oil Shale,* Quarterly of the Colorado School of Mines, July 1965, p. 83, 90.

[39] Arizona v. Colorado, 373 U.S. 546 (1963).

[40] Delaney, *Water for Oil Shale Development,* this edition, *infra,* at p. 75.

V. CONSERVATION

Conservation problems go a lot deeper than just tidying up the landscape after the mining operation. Certain of the deposits may be amenable to strip mining, but others are topped with hundreds of feet of overburden and range up to 1,500 feet in depth. A unique property of the mineral and the retorting process results in an expansion of the shale so that spent shale occupies about two-thirds more volume than does the marlstone ore. A 40,000 barrel per day plant thus would be required to dispose of 62,000 cubic yards of spent shale from the 37,000 yards of raw shale it uses each day.[41] Where to put the mountainous debris and then what to do with it is something more than an inconsequential problem.

Oil shale need not be mined; experiments have been conducted to determine feasibility of extracting the liquid product from the ground by application of heat through steam, by controlled burning (fire flooding), and by use of nuclear explosions to make a vast retort of the ore body itself. Researchers are divided on the effectiveness of the "in situ" process, but the nature of the method indicates built-in problems. It seems agreed that the process is less efficient, thus an ore body decomposed by in situ retorting is likely to produce less oil than an identical body conventionally mined and retorted above ground.[42] Ramifications of a process which will recover only a portion of the kerogen in place raise serious questions related to conservation of resources.

Although theoretical studies have been made under auspices of the Atomic Energy Commission and the U.S. Bureau of Mines aimed at developing a commercially feasible means of using nuclear explosions for oil shale retorting, field experimentation must await results of the current research and experimentation before being given serious consideration, although the subject has some conservation-minded groups worried.

Conservationists, too, are concerned about effects of an oil shale industry takeover of irrigation rights to farmlands, and see as the consequences of such a takeover a return of fertile fields to arid semi-desert land with a concurrent diminution of wildlife. The prospect of a return flow of 165,000 acre feet of water per year from a prospering oil shale industry[43] raises further worries about contamination of downstream domestic water and of fishing waters and waterfowl rookeries.

---

[41] OIL AND GAS JOURNAL, p. 69.

[42] *Ibid.*: yield from one mechanical retorting process is reported as approaching 100 per cent.

[43] Delaney, *supra* note 40 at 74.

VI. A Federal Policy

Formulation of federal policy toward oil shale is replete with pitfalls. Since the rekindling of interest in oil shale following World War II, the Department of the Interior has moved sporadically toward evolving a policy through intradepartmental studies and committees,[44] the efforts of the President's Materials Policy Commission[45] and, most recently, the Oil Shale Advisory Board.[46] And in the absence of affirmative action by the Department, rustlings have been heard from Congress about legislating an answer.[47] It is not without justification that oil shale industry leaders accuse the Department of moving with leaden feet; the Department's Solicitor, speaking at an oil shale symposium April 23, 1965, in Denver, reminded his listeners: "There is enough oil in 10-gallon shale for 368 years. . . . It would be presumptuous for us to attempt to solve the problems people may have 368 years from now. We owe it to future generations to pass along some of the good things on this planet. We owe it to ourselves to pass along some of its problems."[48]

There is much to be said for a "go-slow" attitude on the part of the Federal Government, however. Until the force of an oil shale industry's impact upon the economy can be predicted with some reasonable basis of assurance, a green light for development of shale lands might prove disastrous. There seems to be good basis for expecting a federal policy to evolve on a cautious basis designed to keep oil shale in the position of supplementing conventional petroleum resources, rather than competing directly with them.

In seeking a method of leasing oil shale lands, federal officials are caught on the horns of a dilemma. To permit only a few companies to obtain leases could well bring down charges of favoritism, while opening the doors wide could result in a wild scramble and consequent disorganized development. The great capital cost of developing a mine and retorting facility supports the argument that leases should be restricted to companies which are financially able to proceed immediately into production. Further, an open policy

---

[44] Mock, *The Oil Shale Advisory Board,* this edition, *infra* at 48.

[45] *Ibid.*

[46] *Ibid.*

[47] Most recently, Senator Douglas of Illinois introduced a measure (S. 2708, 89th Cong., 1st Sess. (1965)) providing that upon opening of federal lands to leasing the Federal Government would retain a one-eighth royalty, proceeds of which would be allocated to reducing the national debt. The proposal has been attacked by Sen. Wallace F. Bennett of Utah as "unrealistic and another example of Easterners telling us how to handle our natural resouces in the West." (Rocky Mountain News, Nov. 3, 1965, p. 24, col. 3.)

[48] Barry, *A National Policy for Oil Shale,* QUARTERLY OF THE COLORADO SCHOOL OF MINES, July 1965, p. 97, 105.

of competitive bidding would encourage speculation in what may very well be the nation's most valuable untapped natural resource.

Advocates of an open-door policy on oil shale lands include not only the holders of extensive tracts of oil shale lands, but also state officialdom, particularly in states with extensive deposits, industrial development agencies, such as chambers of commerce, and a cadre of congressional members including some who look to federal oil shale holdings as the key to paying off the national debt.

How many of the problems are resolved today and how many are passed on to future generations will depend to a great extent upon how effectively the Department of the Interior, the Congress, and the oil shale industry itself cooperate in seeking to devise a means of meeting and overcoming the technological, economic, legal, political, esthetic, and international complexities which now stand between the immense wealth in the ground and its unrealized fruition.

* * *

In this Oil Shale Symposium edition of the Denver Law Journal the editors do not propose to provide a comprehensive analysis of the legal problems confronting the oil shale industry. To attempt to so would be far beyond the resources and capacities of the Journal in view of the immense complexities of the current picture. The purpose is, rather, to provide a broad general view, touching in greater detail upon issues related to validity of claims and patents, acquisition and retention of water rights, factors involved in formulation of a federal policy, and upon some of the tools available to the practitioner who might have occasion to inquire into title questions.

Joseph G. Lawler, Symposium Editor

Do Unpatented Oil Shale Mining Claims Exist?

By MAURICE T. REIDY*

The subject of this article is constipation. Webster's dictionary defines "constipation" as a "state of the bowels in which evacuations are infrequent and difficult." Another definition of constipation in Webster is "costiveness," and "costiveness" means "reserved; slow or stiff in expression or action." In applying these definitions to the problem of unpatented oil shale mining claims, one can readily see that evacuations of oil shale are, to say the least, infrequent and difficult, and the attitude of the United States government relative thereto is reserved or slow in expression or action.

This article is limited to the status of unpatented oil shale mining claims. No definite conclusions will or can be drawn and no binding authority can be cited. The conclusions will be reached in numerous cases pending before the Department of the Interior and the courts. In fact, if you walk into the clerk's office of the United States District Court for Colorado to find the cases pending, all you need to do is mention "oil shale cases" and one of the clerks will deliver a group of files to you. Some of the cases have their own little wrinkles, but the principal problem in most of the cases is the one which will be discussed in this article.

The problem may best be phrased in the question, "Does such a thing as a valid unpatented oil shale mining claim exist?" The answer to this question will ultimately determine the ownership of many thousands of acres of potentially valuable lands in Colorado, Utah, and Wyoming. For this reason, the final answer will probably come only from the United States Supreme Court.

I. GENERAL MINING LAW APPLICABLE

We must first, therefore, review generally the background of the mining law relating to the location of mining claims. The first mining law was set forth in the acts of July 4, 1866[1] and July 26, 1866.[2] These laws basically enacted and made legal the customs and self-made rules and regulations of the prospectors in the days

*Member, Colorado Bar; B.S.C., *Magna cum laude,* University of Notre Dame, 1955; LL.B., *cum laude,* University of Denver, 1957; in private practice.

[1] 14 Stat. 86 (1866), 30 U.S.C. § 21 (1965).

[2] 14 Stat. 251 (1866).

of the Gold Rush in 1849. Until these acts all prior mining claims were technically trespasses upon the public domain. The Placer Act of 1870[3] brought non-lode claims under the mining law. A lode claim is one based upon a discovery of "veins or lodes of quartz or other rock in place"[4] bearing valuable deposits. A placer claim is based upon a discovery of deposits excepting veins of quartz or other rock in place.[5] The pending oil shale claims are based upon placer locations. Whether oil shale is more susceptible to lode claims than placer is, therefore, moot unless the government attacks the claims on this basis, which so far has not been alleged. The act of 1872[6] basically re-enacted the acts of 1866 and 1870 and is the last general mining law enacted by Congress. Other particular statutes will be commented on hereafter, but what determines the validity of a mining claim is controlled by these acts.

The most important fact to be proven in establishing a valid mining claim is a discovery. The historic test of what constitutes a discovery is "where minerals have been found and the evidence is of such a character that a person of ordinary prudence would be justified in the further expenditure of his labor and means, with a reasonable prospect of success, in developing a valuable mine."

This was the prudent man test set forth by the Secretary of the Interior in *Castle v. Womble,*[7] and affirmed by the Supreme Court in *Chrisman v. Miller*[8] and *Cameron v. United States.*[9] The interpretation and application of this test to oil shale claims will be discussed hereinafter.

With the discovery there must be a location of the claim in accordance with the federal mining law as supplemented by state law. This includes the staking of the claim's boundaries, the posting of a location notice, recording location certificates, the performance of required discovery development work, and such matters as may be required under the law of the particular state. In this discussion it will be presumed that claims are properly located, although questions may exist respecting proper location of many claims.

Once there is a valid discovery and proper location, a mining claim, in the language of the Supreme Court, is "real property in

---

[3] 16 Stat. 217 (1870), 30 U.S.C. § 35 (1965).
[4] 17 Stat. 91 (1872), 30 U.S.C. § 23 (1965).
[5] 16 Stat. 217 (1870), 30 U.S.C. § 35 (1965).
[6] 17 Stat. 91 (1872), 30 U.S.C. § 22 (1965).
[7] 19 Land Dec. 455 (1894).
[8] 197 U.S. 313 (1905).
[9] 252 U.S. 450 (1920).

the highest sense."[10] Legal title to the land remains in the United States, but a valid, equitable, and possessory title is in the claimant, subject to taxation, capable of being transferred by deed or devise, and otherwise possessing the incidents of ownership of real property. There is no present requirement that a mining claimant ever apply for a patent from the United States. In fact, until an application for a patent is filed, there is no requirement that notice of the claim be recorded other than by posting on the claim and in the county records. Thus, the United States Government may not even know of the existence of the claim. However, until a patent is obtained, the unpatented claim must be maintained in accordance with the mining law.

The principal requirement under the law to maintain a claim is the performance of annual labor on the claim.[11] The federal requirement is supplemented by state laws concerning recording affidavits of annual assessment work, but the controlling question is whether the work is performed. If a claimant fails to perform such annual labor, the land becomes subject to relocation, and if validly relocated, the claim is extinguished, or the real property interest of the prior claimant terminates. Until a relocation is made, however, the prior claim is valid even though the assessment work is not performed, unless the claim is abandoned.

Thus, relocation and abandonment are the only means by which an unpatented claim may be lost under the archaic mining law. The historic test of abandonment is "intent to abandon." All lawyers know the difficulty in proving intent in any situation. The failure of a claimant to perform annual labor may be considered in the factual question of intent to abandon but is not controlling.

The important distinction to be remembered between relocation and abandonment is that a valid relocation after the failure to perform assessment work extinguishes the prior claim as a matter of law, whereas, in the case of abandonment, the failure to perform annual labor is but one of the facts to be considered in proving the requisite "intent to abandon."

This, in a nutshell, was the status of the mining law at the time of the passage of the Mineral Leasing Act of 1920,[12] and as to minerals other than oil shale and other leasing act minerals, is the present status of the law.

---

[10] Forbes v. Gracey, 94 U.S. 762, 767 (1876).

[11] 17 Stat. 92 (1872), 30 U.S.C. § 28 (1965).

[12] 41 Stat. 437 (1920), 30 U.S.C. §§ 181-263 (1958).

II. PARTICULAR STATUTES, ORDERS, AND DECISIONS HAVING APPLICATION TO OIL SHALE CLAIMS BEING SUBJECT TO THE MINING LAW

After the passage of the 1872 act, serious questions existed as to whether the discovery of petroleum could be used as a basis for a mining claim. This problem was resolved by the act of February 11, 1897,[13] which provided, "Any person authorized to enter lands under the mining laws of the United States may enter and obtain patent to lands containing petroleum or other mineral oils, and chiefly valuable therefor, under the provisions of the laws relating to placer mineral claims." Natural uncertainty remained, however, as to oil shale claims since this mineral is not, strictly speaking, an oil. Shale oil is obtained from kerogen in the rock by crushing and distillation. This uncertainty was eliminated on May 10, 1920, in *Instructions* from the First Assistant Secretary of the Department of the Interior, wherein he stated:

> Oil shale having been thus recognized by the Department and by Congress as a mineral deposit and a source of petroleum, and having been demonstrated elsewhere to be a material of economic importance, lands valuable on account thereof must be held to have been subject to valid location and appropriation under the placer mining laws, to the same extent and subject to the same provisions and conditions as if valuable on account of oil or gas . . .[14]

Pursuant to such instructions, the first oil shale patent issued for the La Paz claims Numbers 1 to 14, inclusive.[15]

The claims theretofore located were protected in the passage of the Mineral Leasing Act of February 25, 1920, by Section 37 of such act,[16] which provided:

> That the deposit of . . . oil shale . . . shall be subject to disposition only in the form and manner provided in this act, except as to valid claims existent at the date of the passage of this act and thereafter maintained in compliance with the laws under which initiated, which claims may be perfected under such laws, including discovery.

III. HISTORY OF OIL SHALE CLAIMS PRIOR TO PENDING CASES AND CONTESTS

The oil shale claims were originally located from 1916 to February 25, 1920. On that date the Mineral Leasing Act became effective and oil shale was designated as a leasing act mineral.[17]

---

[13] 29 Stat. 526 (1897).

[14] 47 Land Dec. 548 (1920).

[15] Mineral Entry Glenwood Springs-015847 (Denver Land Office, Bureau of Land Management).

[16] 41 Stat. 451 (1920), 30 U.S.C. § 193 (1965).

[17] 41 Stat. 445 (1920), 30 U.S.C. § 241 (1965).

As noted above, Section 37 of the act contained a savings clause protecting claims existing as of that date and perfected and maintained in accordance with the law. The claims protected under the savings clause are those which are involved in the present controversies. No claims were located subsequent to 1920 because the Mineral Leasing Act in effect withdrew the lands from a location based on a discovery of oil shale.

One result of this was to eliminate the penalty of relocation for failure to perform annual assessment work, unless the relocation was based on the discovery of minerals other than leasing act minerals. As a practical matter, the penalty of relocation has been eliminated since no significant discovery of non-leasing act minerals has been made in the area.

After the passage of the Mineral Leasing Act, annual labor was not performed on many of the claims. Whether the reasons were that the penalty of relocation was removed or that the locators did not care to perform the work and maintain the claims, may never be known since most of the original locators are now dead. The Department of the Interior, however, from 1927 to 1933, brought numerous contest proceedings to cancel claims on the basis of failure to perform assessment work. The authority of the United States to contest the validity of a mining claim at any time before patent is clear.[18] Unless an application for patent pursuant to a mineral entry has been filed with the Bureau of Land Management, however, the procedure for contesting the claims is difficult. The United States, as the moving party, must determine the name of the claim, its description, and the names of the owners. The contests were commenced in accordance with *Instructions* of February 26, 1916,[19] and the Rules of Practice then in effect.[20] In most cases, notices of the contest were mailed to the parties by registered mail. In many cases notices were not mailed to all owners and in some cases the notices were not addressed to any of the owners. In such cases, the Department of the Interior has admitted notice was improper.[21]

Almost all of the contests were based on failure to perform assessment work. In most cases, no answers or appearances were made by the mining claimants and decisions declaring the claims null and void were issued.

---

[18] Cameron v. United States, 252 U.S. 450 (1920); Ickes v. Virginia-Colo. Dev. Corp., 295 U.S. 639 (1935).

[19] 44 Land Dec. 572 (1916).

[20] 51 Land Dec. 547 (1926).

[21] Union Oil Co. of Cal. A-29560 (Supp.) GFS, SO-1965-41.

Some claimants did appear and appealed to the Supreme Court. The Supreme Court, in the case of *Wilbur v. Krushnic* in 1930,[22] and, to clarify a point, in *Ickes v. Virginia-Colorado Development Corporation* in 1935,[23] held that the Interior Department could not declare a claim void for failure to do assessment work since the only penalty under the law was relocation.

Shortly thereafter, in a departmental decision in *The Shale Oil Company*,[24] which case had been suspended pending the Supreme Court decision, the following statement appears:

> In view of this opinion of the court, the adverse proceedings and decision of the Commissioner therein, in the instant case, must be held as without authority of law, and void. The above-mentioned decision of the Department in the *Virginia-Colorado Development Corporation* case and the instructions of June 17, 1930 are hereby recalled and vacated. The above-mentioned decisions in the cases of *Francis D. Weaver* and *Federal Oil Shale Company* and other Departmental decisions in conflict with this decision are hereby overruled.

For a number of years after these decisions, no significant departmental or court cases arose concerning the problem. The general opinion among many attorneys was that the original department decisions voiding claims for failure to do assessment work were void also, which opinion was shared by officers within the Department of the Interior. In fact, patents subsequently issued on some claims which had been declared void prior to the 1935 decision of the Supreme Court.[25]

The limbo continued to exist until the passage of Public Law 585, commonly known as the Multiple Use Act, in 1954.[26] Section 7 of this act[27] established a procedure under which a lessee of a United States oil and gas lease could institute an action to verify the title under such lease. This is necessitated since the mining claimant, if the claim is valid, would own the full equitable title, including oil and gas. Although the Multiple Use Act was enacted to clarify problems between unpatented uranium claims and conflicting federal oil and gas leases, its provisions clearly apply to all unpatented claims. Various proceedings under Section 7 of Public Law 585 have been commenced, many of which concerned conflicts with unpatented oil shale claims. However, no significant decisions were issued since most of the proceedings were settled with the mining claimants

---

[22] 280 U.S. 306 (1930).

[23] 295 U.S. 639 (1935).

[24] 55 Interior Dec. 287 (1935).

[25] Schmidt, *Status of Unpatented Claims*, QUARTERLY OF THE COLORADO SCHOOL OF MINES, July 1964, p. 125.

[26] 68 Stat. 708 (1954), 30 U.S.C. § 521 (1958).

[27] 68 Stat. 711 (1954), 30 U.S.C. § 527 (1965).

prior to hearing by means of protective leases from the claimants or options for leases. Assuming the regularity of the proceeding, if a mining claimant failed to file a verified statement within the time allowed during such a proceeding, it is clear that the claimant has lost all rights to leasing act minerals,[28] and consequently, in the case of oil shale, the claimant will have lost his claim.

In connection with the passage of Public Law 585, however, one significant case did arise. In 1954, Union Oil Company applied for patent on numerous oil shale placer claims. The proceedings had progressed to the point where a final certificate had been issued to Union and only the issuance of patent remained. However, no action had been taken by a lessee of a federal oil and gas lease covering the same lands. Another oil company which had control of this lease challenged Union's right to a patent. The Secretary of the Interior decided that Union would be required to bring contest proceedings to cancel the lease before patent could issue.[29] There had been a flurry of general oil and gas activity in the area, but by the time of the Secretary's decision, the oil and gas lessee had lost interest in the area. However, when Union appealed to the district court, the Secretary of the Interior stayed in the fight. The decisions of both the district court[30] and the court of appeals[31] affirmed the Secretary's decision requiring the contest proceedings.

This decision is most significant, not in its holdings, but in the change in attitude of the Department of the Interior which resulted thereby. Prior to this case, patents were being issued on oil shale claims; subsequently, to this author's knowledge, no oil shale patents have been issued and attempts to obtain the same have been strongly resisted by the Department of the Interior. This brings us to the current status of constipation.

IV. Decision of Secretary of the Interior on April 17, 1964

On February 16 and 23, 1962, the Manager of the Denver Land Office of the Bureau of Land Management issued decisions rejecting mineral patent applications on some 257 oil shale placer claims. No hearings were conducted on the merits of the claims, *e.g.,* valid location and discovery. The Manager's decisions were based on the grounds that the claims had been declared null and void in contest proceedings initiated from 1927 to 1931, and that

---

[28] 68 Stat. 711 (1954), 30 U.S.C. § 527(b) (1965).

[29] Union Oil Co. of Cal. v. Calvert, 65 Interior Dec. 245 (1958).

[30] Union Oil Co. of Cal. v. Seaton, Civil No. 3042-58, D.D.C. (1960).

[31] Union Oil Co. of Cal. v. Udall, 289 F.2d 790 (D.C. Cir. 1961).

under the "principles of finality of administrative action, estoppel by adjudication, and res judicata," the prior decisions in the contests could not now be challenged. All of the prior decisions involved were of the type discussed above, wherein the Government in the earlier contest proceedings had alleged failure to perform assessment work. All of the prior decisions had been issued before the Suprme Court decision in *Ickes v. Virginia-Colorado Development Corporation.*[32] Some of the contests had been commenced prior to the *Krushnic* case, but apparently new contest proceedings were commenced after the *Krushnic* case.[33]

Twenty-seven different appeals were taken to the Director, Bureau of Land Management, from the Manager's decisions. Such appeals were considered together by the Secretary of the Interior, who assumed supervisory jurisdiction. In *Union Oil Company of California,*[34] decided on April 17, 1964, the Secretary affirmed the Manager's decisions on the principles of res judicata, finality of administrative action, and laches. The Manager and Secretary both held that the earlier decisions in the contest proceedings could not now be challenged, even though possibly incorrect as a matter of law. The Secretary's decision of April 17, 1964, relied heavily on the fact that the opinion in *The Shale Oil Company*[35] case in 1935, which was issued after the *Virginia-Colorado*[36] decision of the Supreme Court, merely overruled certain cases and specifically vacated and recalled other cases. By overruling cases, the Secretary contends such cases merely lose their precedent and authority for future decisions, but the decisions in such cases are not affected.

The decision of April 17, 1964, also relies heavily on the decision of the Circuit Court for the District of Columbia in *Gabbs Exploration Company v. Udall.*[37] The *Gabbs* case parallels the factual situation of the earlier contest proceedings used as a basis for the April 17 decision with one important exception. The original notice of contest in the *Gabbs* case, in addition to alleging failure to perform assessment work, also alleged abandonment. Thus, the earlier *Gabbs* decision would not be incorrect as a matter of law under the *Virginia-Colorado* case, since the Government may challenge unpatented claims on the basis of abandonment as stated in the *Virginia-Colorado* case.[38]

---

[32] 295 U.S. 639 (1935).
[33] 280 U.S. 306 (1930).
[34] 71 Interior Dec. 169 (1964).
[35] 55 Interior Dec. 287 (1935).
[36] 295 U.S. 639 (1935).
[37] 315 F.2d 37 (D.C. Cir. 1963), *cert. denied,* 375 U.S. 822 (1963).
[38] 295 U.S. 639 (1935).

The decision of the court of appeals in the *Gabbs* case does, however, lend some authority to the doctrines of res judicata and finality of administrative action asserted by the Secretary in his decision of April 17, 1964, but the *Gabbs* case does not cite any court authority in this respect.[39]

The Secretary's decision of April 17, 1964, considered the question of notice in the prior contest proceedings. As to some claims it held the notice proper and the decision was final. As to other claims, the finality of the decision was held in abeyance pending a determination of the sufficiency of notice of contest in the early proceedings. Such determination has now been made and is set forth in the supplemental decision in *Union Oil Company of California,* decided July 30, 1965.[40] The supplemental decision upholds service of notice by registered mail, with the proof thereof being a return receipt signed by the owner of the claims or his authorized agent, if such authorization is in writing. The decision adds to the constipation by declaring fractional interests in some claims cancelled and other fractional interests in the same claims not cancelled. The supplemental decision does not, however, change the basis of the April 17, 1964, decision and considers only the notice question.

V. Appeals of Decisions of April 17, 1964, and July 30, 1965

Several appeals were immediately prosecuted to the United States District Court for the District of Colorado after the April 17, 1964, decision. Additional appeals can now be expected after the supplemental decision of July 30, 1965.

In *The Oil Shale Corporation, et al., v. Udall,*[41] the Government filed a motion to dismiss on the grounds that the complaint failed to state a claim and was premature since the plaintiff had not exhausted its administrative remedies, that the primary authority in the matter was in the Secretary of the Interior, and that the United States was an indispensable party. The motion to dismiss was denied by Judge William E. Doyle on November 27, 1964.[42] Thereafter, the Government filed its answer including the same grounds as were included in the motion to dismiss, and in addition alleged laches, estoppel, res judicata, and finality of administrative action. The government's answer curiously alleges therefore both that the plaintiffs are too early by not exhausting their administrative

[39] 315 F.2d 37, 40-41 (D.C. Cir. 1963).
[40] A-29560 (Supp.) GFS, SO-1965-41.
[41] Civ. Act. No. 8680, U.S.D.C., Colo. (pending).
[42] 235 F. Supp. 606 (D. Colo. 1964).

remedies and too late by reason of laches and estoppel. It is possible that either or both of these grounds will ultimately prove successful.

The typical type of relief sought in the appeals is that prayed for in *Napier v. Udall.*[43] The plaintiffs in this case seek a mandatory order requiring the Secretary of the Interior to process the patent application and take such action as is necessary to issue the patent, as well as orders declaring the early contest decision null and void and the Manager's decision of February 16, 1962, and Secretary's decision of April 17, 1964, invalid.

If the Secretary of the Interior is successful in defending these appeals, and it is a sure thing that such success will only be achieved after action or denial of review by the Supreme Court, the problem as to claims involved in the appeals will be resolved. If, however, the Secretary's decision is reversed, all of these claims will then be remanded to the Manager's office for hearings on the merits of the claims. The position of the Secretary in such hearings, as well as in hearings on claims not declared invalid by reason of improper notice, is indicated by additional directions of the Secretary.

VI. SECRETARY'S MEMORANDUM OF APRIL 17, 1964

On the same date the Secretary issued his decision in *Union Oil Company of California, et al.,*[44] the Secretary also issued a Memonrandum to the Director, Bureau of Land Management concerning the determination of rights to outstanding unpatented oil shale mining claims. The Bureau of Land Management was directed to determine all remaining claims, and as to those which were not the subject of contests or patent applications, to initiate contest proceedings to test the adequacy of discovery, and to assert any ground for contest which might be justified by the facts. The Secretary directed that to qualify as valid, the discovery must have been such, on the date it was made, as would justify a person of ordinary prudence in the further expenditure of labor and means, with reasonable prospect of success, in developing a valuable mine. This is the historic test of a discovery as noted above.[45] However, the application of the test is controlling. In this connection, the following is quoted from the Secretary's Memorandum:

> 4. In applying the test of discovery, the Bureau should observe the following guidelines:
>
> a) The fact that any given deposit of oil shale may be a valuable resource for future use does not render the

---

[43] Civ. Act. No. 8691, U.S.D.C., Colo. (pending).

[44] 41 Interior Dec. 169 (1964).

[45] Cameron v. United States, 252 U.S. 450 (1920); Crisman v. Miller, 197 U.S. 313 (1905); Castle v. Womble, 19 Land Dec. 445 (1894).

> discovery valid under the mining laws unless a person of ordinary prudence would be justified in the further expenditure of labor and means with the reasonable prospect of developing a valuable mine;
>
> b) The finding or exposure of an isolated bit of mineral or quantities of low-grade mineral, not connected with or leading to valuable mineral deposits, will not in itself be considered a sufficient discovery;
>
> c) The mineral deposit actually found or exposed by the locator must itself have been of such character as to meet the test of discovery without regard to other physical evidence or information not obtained from within the boundaries of the claim from which the existence of substantial values beneath the surface may be inferred.
>
> 5. In further contest proceedings, the Bureau will raise the question of the economic or commercial value of oil shale, as of the time the claims were located, as one of the elements in the application of the standard test of discovery discussed above. The lack of any economically or commercially feasible method of extraction and production of shale oil from oil shale is a relevant, although not necessarily decisive, consideration in determining whether a discovery was made. In this regard, the mere showing of an outcrop of the Mahogany Ledge, in circumstances which heretofore have provided the basis for patent, will no longer be accepted as *prima facie* evidence of compliance with the requirements of the mining laws. This does not mean that the claimant is required to demonstrate the immediate marketability of oil shale as in the case of certain non-metallic minerals of widespread or common occurrence.

It is noted that the Secretary cited authority in other parts of his Memorandum, but cited no authority in the above quoted parts of the Memorandum. There is no real objection to this since the "guidelines" are now established for the future, except the increased constipation which will result therefrom.

The guidelines, by their own admission, conflict with the past application of the test of discovery. The general rule of discovery in oil shale claims heretofore followed by the Department of the Interior was set forth in the case of *Freeman v. Summers*.[46] The test to be applied hereafter apparently is set forth in the Secretary's Memorandum quoted above. As noted above, the *Instructions* of May 10, 1920, from the First Assistant Secretary of the Interior[47] recognized the value of oil shale and authorized the issuance of patents. No discoveries have been made since such date because the Mineral Leasing Act of February 25, 1920, prohibited further locations. As early as 1916 the United States Geological Survey issued regulations governing what would be considered valuable oil shale.[48] Such regulations included considerations of the depth of the shale

[46] 52 Land Dec. 201 (1927).

[47] 47 Land Dec. 548 (1920).

[48] Cited in Empire Gas & Fuel Co., 51 Land Dec. 424, 429 (1926).

from the surface, the thickness of the bed, and the ultimate yield in gallons per ton of the shale discovered. The regulations were later revoked as being possibly too strict.[49] However, they did constitute a recognition by the Department of the Interior of the value of oil shale. In effect, the Supreme Court decisions in the *Krushnic*[50] and *Virginia-Colorado Development Corporation*[51] cases acknowledged discoveries prior to 1920 were sufficient under the mining law, and, of course, the numerous patents heretofore granted were based upon similar discoveries.

The Secretary's application of the test of discovery is not necessarily a new rule, but a new application of the rule to oil shale claims. There have been numerous interpretations or constructions of the so-called "prudent man" test.[52]

The so-called "liberal rule" of construction is usually cited as requiring only that a locator be able to establish that there was such a discovery of mineral within the limits of his claim that would justify an ordinarily prudent man, not necessarily a miner, in expending his time and money thereon in the further development of the property. It should be noted that a purely literal interpretation of this rule would not require the locator to submit any evidence as to the potentially commercial and profit-making nature of his discovery deposit.[53] It is this rule which is most commonly applied in those cases, arising in state courts, the purpose of which is to adjudicate rights of possession between conflicting mineral locators.[54]

The so-called "strict rule" of construction requires that a mineral locator be able to establish mineralization within the limits of his claim to an extent which would make the land more valuable for the purpose of removing and marketing minerals than for any other purpose. Such a rule necessarily seems to imply that the locator be able to establish that his claim can be worked at a profit or that the quantity and quality of his mineral discovery be "in paying quantities." This rule has been applied, either expressly or impliedly, in proceedings involving a contest between an agricultural and a mineral entry,[55] a contest between a placer and lode

---

[49] Pitcher v. Jones, 71 Utah 453, 267 Pac. 184 (1928); 36 AM. JUR. *Mines & Minerals* § 87 (1938).

[50] 280 U.S. 306 (1930).

[51] 295 U.S. 639 (1935).

[52] Cameron v. United States, 252 U.S. 450 (1920); Crisman v. Miller, 197 U.S. 313 (1905); Castle v. Womble, 19 Land Dec. 445 (1894).

[53] 3 LINDLEY, MINES § 336 (3d ed. 1914).

[54] Pitcher v. Jones, 71 Utah 453, 267 Pac. 184 (1928); 36 AM. JUR. *Mines & Minerals* § 87.

[55] Davis's Administrator v. Weibold, 139 U.S. 507 (1891).

deposit,[56] applications for patent,[57] and in actions brought by the United States to contest the validity of a location[58] or to set aside a patented claim on the basis of fraud.[59]

The rule generally applied by the Department of the Interior in patent applications until recent years appears to be reflective of a more general rule sufficiently broad to encompass both the liberal and strict constructions. Such rule may be stated as requiring that a locator find mineral in mass so placed that he can follow a vein or other mineral deposit with reasonable hope and assurance that he will ultimately develop a paying mine.[60] For a comprehensive analysis of the problems of discovery, see Title IV of the American Law of Mining (1964).

The sole conclusion to be derived concerning the new guidelines established as to oil shale discoveries is that if the discoveries are not deemed valid, another decision of the United States Supreme Court will be required.

Before leaving a discussion of the Secretary's Memorandum of April 17, 1964, it is noted that although the question of discovery is primarily discussed therein, the Secretary also directed the Bureau of Land Management to assert any other ground for contest which might be justified by the facts. The Secretary's supplemental decision in *Union Oil Company of California, et al.*[61] indicates other grounds which will be asserted. The following is quoted therefrom.

> It should be noted that, as to cases hereinafter remanded for further action and processing by the Bureau of Land Management, this decision is not intended to be the final administrative determination of the possessory rights now claimed by the patent applicants. The patent applications have yet to be examined by the Bureau for the purpose of determining, among other things, whether locations were validly made, whether the claims were validly maintained, and whether the claims were abandoned . . . .
>
> The Bureau must also determine, assuming the claims are otherwise valid, whether the present patent applicants have acquired all of the outstanding uncancelled possessory interests in the claims for which they seek patents. Specifically, there remains open the question whether the Department is bound to accept a State Court's determination regarding the relative rights of possession of alleged co-owners of an association placer claim . . . .
>
> If it is not bound by such decisions, an additional question to be

---

[56] United States v. Iron Silver Mining Co., 128 U.S. 673 (1888).

[57] Royal K. Placer, 13 Land Dec. 86 (1891).

[58] United States v. Dawson, 58 Interior Dec. 670 (1944).

[59] 1 RICKETTS, AMERICAN MINING LAW § 598 (4th ed. 1943).

[60] Cameron v. United States, 252 U.S. 450 (1920); United States v. Minnilee Baker, 60 Interior Dec. 241 (1948); Freeman v. Summers, 52 Land Dec. 201 (1927); Montana Copper Mines Co., 41 Land Dec. 320 (1921); 1 RICKETTS, AMERICAN MINING LAW § 597 (4th ed. 1943).

[61] A-29560 (Supp.) GFS, SO-1965-41.

> determined is whether the Department will recognize an asserted title to an association placer oil shale mining claim where the patent applicant's title is based in part on interests allegedly acquired since 1920 by means of forfeiture notices published in accordance with Rev. Stat. 2324 (30 U.S.C. 28) (1958 ed.).

Thus, slowly but surely, the battle lines are being drawn. It is clear that once hearings on the merits are conducted, the factual presentations in each case will be of great importance, and the probable court review of the denials of patent applications and the ultimate decisions therein will, in themselves, be a comprehensive analysis of the entire mining law.

VII. GENERAL SUMMARY AS TO OIL SHALE DEVELOPMENT

As commented upon earlier herein, no binding authority is cited, the reasons being evident. This article merely brings the problem up to date since an excellent article on the subject in DICTA in 1950.[62] Since that time, a significant change may be noted in the position of the Department of the Interior. The changes may be summarized as follows:

1. The Department now takes a position that the claims were cancelled in the early proceedings if notice was proper. This on the surface would appear to be consistent.
2. However, the Department did not take this position at all times since 1935, as evidenced by the issuance of patents since such date on claims previously declared null and void.
3. The Department's test of discovery to be applied in future patent applications is inconsistent with that previously applied in *Freeman v. Summers*.[63]

Lest a reader think the Government's position seems arbitrary and capricious, a few further comments are necessary. This article was requested to represent both views, *i.e.*, that of the Government and that of the claimant. Since this is more of a factual history than a citation of legal authorities, some more facts should be emphasized.

With few exceptions, most of the claims involved in the present proceedings were acquired after 1935 by the persons or parties now seeking patents. Such acquisitions were made with the record showing the prior decisions declaring the claims null and void, and consequently, with full knowledge of the possible invalidity of the

---

[62] 27 DICTA 195 (1950).

[63] 52 Land Dec. 201 (1927).

claims. No significant development of the properties has yet been made. Consequently, if the mining claimants win, they will have obtained title to thousands of acres of valuable lands for doing nothing from 1920 to the middle 1950's except the nominal work required for patent.[64] After 1955, admittedly the claimants will have expended large sums for attorneys' fees.

As a result, this author has no objection to the Government's contesting the validity of the claims. The objection is to the procedure being followed by the Government in not having hearings on all aspects of the particular cases at one time. The Manager's decisions in February 1962 now have been reversed in part and affirmed in part. Some claimants must now appeal to the courts for the right to have a hearing on the merits, while at the same time, the Government is preparing new attacks which will require additional court appeals if the Manager's decisions of 1962 are ultimately reversed. Maybe logically the Government could respond that since nothing was done from 1920 to 1955, what is the big hurry now. The answer to this is simply that oil shale can not be developed until this problem is resolved, and the Government should encourage the orderly development of our natural resources, and not be in a position of constipating it by its own action.

If the ultimate decisions are reached on the basis of principles of law, the claimants appear to have the better position. If, however, the ultimate decisions are based on principles of equity, such as laches and estoppel, the Government may win if it does not by its new actions create such inequities as would, under the old maxim, prevent it from coming into court "with clean hands."

[64] 221 Stat. 61 (1880), 43 Stat. 144 (1925), 30 U.S.C. § 29 (1965).

Conclusiveness of United States Oil Shale Placer Mining Claim Patents

By GEORGE E. LOHR*

A significant amount of land in western Colorado containing deposits of oil shale is privately owned.[1] Title to much of this land is derived under United States patents based on oil shale placer mining claims. The recent intensification of efforts to develop an oil shale industry has given new importance to the question whether these patents are vulnerable to attack by the United States or by others. Most of the authorities bearing on this question have long been part of the public land law and apply to Federal public land patents of all kinds, but a new facet relating specifically to oil shale patents has been added by the April 17, 1964, decision of the Solicitor of the Department of the Interior in *Union Oil Co. of California.*[2]

This article represents an attempt to distill from the cases some conclusions concerning the present status of the law governing the conclusive effect of oil shale placer mining claim patents. Based upon these conclusions, some suggestions will be made concerning the scope of examinations of title to privately owned property, title to which is derived under such patents.

EFFECT OF A UNITED STATES PATENT, IN GENERAL

The issuance of a United States patent passes to the patentee legal title to the property therein described.[3] It divests the Department of the Interior of further jurisdiction over that property, with the result that a patent cannot be cancelled by administrative action.[4] Any challenge to the validity of a patent must be made in a judicial proceeding, taken in the name of the government for that special purpose.[5]

---

*Member, Colorado and Denver Bar Associations. Partner, Davis, Graham and Stubbs, Denver, Colo. B.S., South Dakota State College of A&M Arts, 1953; J.D., University of Michigan, 1958.

[1] Approximately 335,000 acres, according to HANNA, *Oil Shale* 12 (1964), a reprint of articles appearing in The Denver Post, Aug. 30, 1964, through Sept. 6, 1964. This estimate is stated to be based on a rough estimate by the staff of Lowell M. Puckett, then Director of the Colorado Land Office of the United States Bureau of Land Management.

[2] 71 Interior Dec. 169 (1964).

[3] *E.g.,* Steel v. St. Louis Smelting & Ref. Co., 106 U.S. 447 (1882). Provided, of course, that the Department of the Interior had jurisdiction over the disposition of the lands. See, *e.g., ibid.*

[4] *E.g., ibid;* Germania Iron Co. v. United States, 165 U.S. 379 (1897).

[5] Steel v. St. Louis Smelting & Ref. Co., 106 U.S. 447 (1882); see United States v. Stone, 69 U.S. 525 (1865). An exception exists in the case of void patents. See discussion at footnote 45 *et. seq. infra,* Attacks by the United States, Relief for Lack of Jurisdiction to Issue Patent.

The issuance of a United States patent necessarily involves consideration of the qualifications of the applicant, the acts he has performed to secure title, the nature of the land, and whether it is of a class which is open to sale.[6] The issuance of a patent by the Department of the Interior is a judgment of a special tribunal upon such matters.[7] It also is an adjudication of compliance with relevant state statutes relating to perfection of mining claims.[8] Issuance of a United States patent creates a presumpion that all preceding steps required by law were duly taken.[9]

Attacks by the United States

I. *Grounds for Relief:*

The United States may attack a United States patent on any one of three grounds:[10] (1) fraud by the patentee in inducing issuance of the patent;[11] (2) mistake by the Department of the Interior in issuing the patent;[12] and (3) lack of jurisdiction in the Department of the Interior to issue the patent.[13]

The United States cannot avoid its patent for irregularities or defects of procedure.[14]

The Attorney General of the United States has the authority to bring actions in the name of and on behalf of the United States to cancel United States patents.[15]

A. Relief for Fraud

A patent obtained by fraud is not void, but is voidable upon

---

[6] Steel v. St. Louis Smelting & Ref. Co., 106 U.S. 447 (1882).

[7] *Ibid;* St. Louis Smelting & Ref. Co. v. Kemp, 104 U.S. 636 (1882); see El Paso Brick Co. v. McKnight, 233 U.S. 250 (1914).

[8] Creede & Cripple Creek Mining & Milling Co. v. Uinta Tunnel Mining & Transportation Co., 196 U.S. 337 (1905).

[9] Diamond Coal & Coke Co. v. United States, 233 U.S. 236 (1914) (presumption rebutted); St. Louis Smelting & Ref. Co. v. Kemp, 104 U.S. 636 (1882) (presumption conclusive against collateral attack).

[10] The three categories adopted provide a convenient grouping for the purpose of discussion of remedies available to the United States. Most, if not all, cases of attacks by the United States on its land patents are based on grounds which are described accurately by one of these categories.

[11] Diamond Coal & Coke Co. v. United States, 233 U.S. 236 (1914); United States v. Minor, 114 U.S. 233 (1885).

[12] Germania Iron Co. v. United States, 165 U.S. 379 (1897) (patent approved by clerk in ignorance of pending proceedings based on conflicting claims); see Williams v. United States, 138 U.S. 514 (1891) (inadvertent certification when administrative decision on conflicting claim was pending).

[13] United States v. Stone, 69 U.S. 525 (1865) (land within the limits of a military reservation created by executive order).

[14] See Wight v. Dubois, 21 Fed. 693 (D. Colo. 1884). As examples of procedural defects the court suggested the time of publication of notice, the filing of the plat, and the discovery of mineral in the discovery shaft.

[15] United States v. Beebe, 127 U.S. 338 (1888); United States v. San Jacinto Tin Co., 125 U.S. 273 (1888).

suit by the United States.[16] The United States has the same right to avoid a patent issued on the basis of fraudulent inducements as does an individual grantor to avoid a deed for such cause.[17]

The history of disposition of public lands by the United States is replete with cases in which the United States has sought judicial relief to avoid patents obtained by fraud. In some of these cases lands were alleged to have been acquired by "dummy" entrymen for the benefit of persons not qualified by law to acquire such lands.[18] In others, false representations were allegedly made concerning satisfaction of requirements of the homestead laws, including settlement and construction of improvements,[19] and concerning the amount of other land owned by the applicant.[20] Still other cases involve charges of false representations that land was not known mineral land within the meaning of laws excluding such land from disposition thereunder.[21] This list is by no means exhaustive.

In an action by the United States to cancel a United States patent allegedly issued as a result of fraud, the United States has the burden of proving the fraud.[22] To carry this burden, the evidence must command respect and produce conviction[23] — that is, it must be clear, convincing, and unambiguous.

If property has been transferred to a third person by a patentee who obtained his patent by fraud, the United States can recover from the third person the property so patented,[24] provided that the third person is not a bona fide purchaser.[25]

---

[16] Diamond Coal & Coke Co. v. United States, 233 U.S. 236 (1914).

[17] United States v. Minor, 114 U.S. 233 (1885); see United States v. San Jacinto Tin Co., 125 U.S. 273 (1888). United States v. Minor, *supra,* contains the suggestion that the right of the United States to avoid a patent may be greater than that of the individual grantor, at least where the United States must rely on proofs furnished by the entryman because of the impracticability of independently checking the facts.

[18] Exploration Co. v. United States, 247 U.S. 435 (1918); Diamond Coal & Coke Co. v. United States, 233 U.S. 236 (1914); United States v. Bighorn Sheep Co., 9 F.2d 192 (D. Wyo. 1925); United States v. Booth-Kelly Lumber Co., 246 Fed. 970 (D. Ore. 1917).

[19] Colorado Coal & Iron Co. v. United States, 123 U.S. 307 (1887); United States v. Minor, 114 U.S. 233 (1885); United States v. Jones, 242 Fed. 609 (9th Cir. 1917); United States v. Norris, 222 Fed. 14 (8th Cir. 1915); United States v. Albright, 234 Fed. 202 (D. Mont. 1916); United States v. Cooper, 217 Fed. 846 (D. Mont. 1914) (construction of improvements only).

[20] United States v. Christopher, 71 F.2d 764 (10th Cir. 1934).

[21] Diamond Coal & Coke Co. v. United States, 233 U.S. 236 (1914); United States v. Southern Pac. R.R., 11 F.2d 546 (S.D. Cal. 1926).

[22] Diamond Coal & Coke Co. v. United States, 233 U.S. 236 (1914); Colorado Coal & Iron Co. v. United States, 123 U.S. 307 (1887).

[23] Diamond Coal & Coke Co. v. United States, 233 U.S. 236 (1914); United States v. San Jacinto Tin Co., 125 U.S. 273 (1888); Colorado Coal & Iron Co. v. United States, 123 U.S. 307 (1887); United States v. Maxwell Land-Grant Co., 121 U.S. 325 (1887).

[24] See Colorado Coal & Iron Co. v. United States, 123 U.S. 307 (1887).

[25] *Ibid.*

The United States may elect to affirm a patent obtained by fraud and to recover damages for the fraud from the patentee[26] or from a subsequent owner of the property who is not a bona fide purchaser.[27] It is implicit in these decisions that the administrative officials have the authority to decide to elect the damage remedy, although the effect is to permit disposition of public lands in a manner not authorized specifically by Congress. Transfer of the property by the patentee does not extinguish the right of the United States to recover from him damages resulting from the fraud.[28]

Under some circumstances, an action by the United States to cancel a patent based on fraud may result in an election of remedies by the United States, either confirming the patent or electing to rescind it.[29]

It would seem that the measure of damages for fraud should be the difference between the value of the lands patented, measured as of the time of patent, and the amount paid by the patentee to the United States, and there is authority to this effect.[30] Measure of damages in these fraud cases has not received extensive consideration by the courts, however, and no completely consistent rule is established by the cases. In absence of other evidence of value, a purchaser from the patentee has been held liable for the amount for which such purchaser had agreed to sell the land, plus interest (in lieu of rents and profits), for the time such purchaser had possession.[31] If the patentee has improved the lands subsequent to patent and prior to sale to a third party, the value of the improvements must be deducted from the sale price if that price is to be used as a guide to establish the value of the land for the purpose of measuring damages.[32] In absence of proof of value of the lands, the government has been limited to the minimum government price of the lands.[33]

---

[26] United States v. Whited & Wheless, 246 U.S. 552 (1917); United States v. Jones, 242 Fed. 609 (9th Cir. 1917); Bistline v. United States, 229 Fed. 546 (9th Cir. 1916); United States v. Koleno, 226 Fed. 180 (8th Cir. 1915).

[27] Pitan v. United States, 241 Fed. 364 (8th Cir. 1917).

[28] Bistline v. United States, 229 Fed. 546 (9th Cir. 1916); United States v. Koleno, 226 Fed. 180 (8th Cir. 1915).

[29] United States v. Oregon Lumber Co., 260 U.S. 290 (1922); *cf.* Bistline v. United States, 229 Fed. 546 (9th Cir. 1916); United States v. Bellingham Bay Improvement Co., 6 F.2d 102 (9th Cir. 1925). No full treatment of the election of remedies doctrine as applied to voidable patents is attempted here.

[30] Pitan v. United States, 241 Fed. 364 (8th Cir. 1917) (not considering specifically the time as of which the land should be valued); see United States v. Norris, 222 Fed. 14 (8th Cir. 1915).

[31] United States v. Cooper, 217 Fed. 846 (D. Mont. 1914). No mention was made of deduction of the amount received by the United States for the land. The court created a lien on the patented lands to secure to the United States the payment of the damages.

[32] United States v. Norris, 222 Fed. 14 (8th Cir. 1915).

[33] *Ibid.* But had not the government already received this amount upon entry?

B. Relief for Mistake

A patent issued by mistake is not void but is voidable upon suit by the United States.[34]

Some of the instances of mistake considered in the cases are issuance of an agricultural land patent based upon erroneous diagrams furnished by the surveyor general which failed to show a conflict with a prior mining claim as to which a patent application proceeding had been commenced;[35] issuance of a patent at a time when there was in effect an order of the Land Department suspending action on the entry pending resolution of disputes concerning conflicting claims;[36] and issuance of a patent at a time when a decision of the register and receiver rejecting the claim was on appeal to the Commissioner of the General Land Office.[37]

Issuance of a patent to lands reserved from disposition for public purposes or previously disposed of, based upon a mistake of fact or law, might be considered as a form of mistake,[38] but in view of the difference in applicable rules of law obtaining in such cases, these and similar types of "mistake" are considered separately under the category of lack of jurisdiction.

In an action to cancel a United States patent based on mistake, the United States should have the burden of proving the mistake upon which its claim for relief is based. The patentee cannot defend successfully on the basis that, notwithstanding the mistake, the facts presented to, but not yet passed on by, the Department of Interior entitle him to a patent.[39] These matters must be considered by the Department of the Interior, the tribunal entrusted by the law with jurisdiction over such matters.[40]

The United States can recover lands patented by mistake from a third person to whom they have been conveyed by the patentee, provided that person is not a bona fide purchaser.[41]

---

[34] Germania Iron Co. v. United States, 165 U.S. 379 (1897).

[35] See Empire Star Mines Co. v. Grass Valley Bullion Mines, 99 F.2d 228 (9th Cir. 1938). No proceedings to cancel the agricultural land patent were ever instituted, although the United States had invited the mining claim owner to request institution of such proceedings.

[36] Germania Iron Co. v. United States, 165 U.S. 379 (1897). The "Land Department" is sometimes referred to in this article. Its functions are among those now performed by the Department of the Interior.

[37] United States v. Southern Pac. R.R., 43 F.2d 591 (S.D. Cal. 1930), *aff'd*, 51 F.2d 873 (9th Cir.), *cert. denied*, 284 U.S. 675 (1931).

[38] See, *e.g.*, United States v. Chandler-Dunbar Water Power Co., 209 U.S. 447 (1908).

[39] Germania Iron Co. v. United States, 165 U.S. 379 (1897); see Southern Pac. R.R. v. United States, 51 F.2d 873 (9th Cir.), *cert. denied*, 284 U.S. 675 (1931).

[40] Germania Iron Co. v. United States, 165 U.S. 379 (1897); Southern Pac. R.R. v. United States, 51 F.2d 873 (9th Cir.), *cert. denied*, 284 U.S. 675 (1931).

[41] Germania Iron Co. v. United States, 165 U.S. 379 (1897).

The United States may elect to affirm a patent issued by mistake and to recover from the patentee the value of the land so patented,[42] at least where the land was conveyed to a bona fide purchaser prior to discovery of the mistake.[43] If this election may be made in all cases by the administrative officials in their discretion, the effect of election of the compensation remedy will be to permit disposition of public lands in a manner not authorized specifically by Congress.

The amount which the United States may recover in case of election of the compensation remedy probably is measured by the value of the land patented at the date of patent,[44] perhaps less the amount paid by the patentee on entry, but no cases have been discovered in which the measure of damages has received detailed consideration.

C. Relief for Lack of Jurisdiction to Issue Patent

A patent issued by the Department of the Interior when that Department has no jurisdiction over the lands patented is void.[45]

Lack of jurisdiction cases include situations where the land has been reserved from disposition as a result of Presidential order,[46] or treaty reservation.[47] They also include situations where the land is not public property, no provision has been made by Congress for its sale, or it has been previously disposed of or has been reserved from sale by Congress.[48] These patents pass no title and may be attacked directly[49] or collaterally.[50]

Legal actions to obtain adjudications that patents are void are appropriate[51] and are not uncommon. Often the facts establishing that a patent is void are not apparent from the face of the patent,[52] and even when a patent is void on its face it may be desirable to obtain a judicial decree confirming that fact.

Appropriate cases for collateral attack on void patents would seem to be limited to circumstances where private rights could be obtained in the land. Otherwise a claimant would have no interest on the basis of which to maintain an action. Such appropriate cases

---

[42] Southern Pac. R.R. v. United States, 200 U.S. 341 (1906).

[43] *Ibid.*

[44] See *ibid.*

[45] See United States v. Chandler-Dunbar Water Power Co., 209 U.S. 447 (1908).

[46] Stone v. United States, 69 U.S. 525 (1865); see Louisiana v. Garfield, 211 U.S. 70 (1908) (grant by approved list rather than by patent).

[47] United States v. Minnesota, 270 U.S. 181 (1926); Northern Pac. Ry. v. United States, 227 U.S. 355 (1913).

[48] See St. Louis Smelting & Ref. Co. v. Kemp, 104 U.S. 636 (1882).

[49] Stone v. United States, 69 U.S. 525 (1865).

[50] See St. Louis Smelting & Ref. Co. v. Kemp, 104 U.S. 636 (1882).

[51] See, *e.g.*, United States v. Minnesota, 270 U.S. 181 (1926).

[52] See *ibid.*

might include situations where land has been patented twice or where a withdrawal in effect at the time of inception of rights on the basis of which a patent issued was subsequently cancelled.

It has been held that the United States can elect to leave void patents uncancelled and sue the patentee for the value of the lands sold by it,[53] although this is conceptually inconsistent with the doctrine that void patents pass no title.

If the United States is barred from attacking a void patent by reason of a statute of limitations, as discussed herein, any person claiming through the United States based upon rights initiated subsequent to the patent is barred as well.[54]

II. *Defenses to Attacks by the United States:*

The defenses of bona fide purchase and statute of limitations have been asserted frequently in actions in which the United States has attacked patents.

A. Bona Fide Purchase

Bona fide purchase is a defense to an action by the United States to recover lands from a purchaser from a patentee, where such action is based on fraud in inducing issuance of the patent[55] or on mistake.[56] Presumably it is no defense where the action is based on an assertion that the patent is void because of lack of jurisdiction of the Land Department to issue the patent, the patent in such case being void rather than voidable. No case has been discovered where that defense has been asserted in such a situation.

The elements of bona fide purchase are valuable consideration, absence of notice, and presence of good faith.[57] A transferee who paid no consideration cannot qualify as a bona fide purchaser.[58] A purchaser is not required to inquire behind the patent into the circumstances surrounding its issuance, and is not deemed to have constructive notice of such matters.[59] The good faith of a purchaser from the patentee is not impaired by information contained in the

---

[53] United States v. Minnesota, 270 U.S. 181 (1926). The value was held to be the amount the United States would have received for the lands for the benefit of Chippewa Indians under the act by which the Chippewas ceded the lands to the United States.

[54] Hogan v. United States, 72 F.2d 799 (9th Cir. 1934), *cert. denied,* 295 U.S. 752 (1935).

[55] See Colorado Coal & Iron Co. v. United States, 123 U.S. 307 (1887).

[56] See Germania Iron Co. v. United States, 165 U.S. 379 (1897); United States v. Winona & St. P. R.R., 165 U.S. 463 (1897); United States v. Krause, 92 F. Supp. 756 (W.D. La. 1950).

[57] United States v. Winona & St. P. R.R., 165 U.S. 463 (1897); United States v. California & Ore. Land Co., 148 U.S. 31 (1893).

[58] United States v. Cooper, 217 Fed. 846 (D. Mont. 1914)..

[59] See United States v. California & Ore. Land Co., 148 U.S. 31 (1893).

patent application file, where the purchaser had no actual knowledge of such information.[60] Anyone purchasing land actually occupied by settlers claiming rights under the homestead laws is charged with notice of the settlers' claims.[61] Close association with an entryman under the homestead laws, visible conditions on homesteaded lands, and proximity of purchaser's ranches, business, and residence to the homesteaded lands are sufficient to place a purchaser on notice that the entryman did not meet the requirements of actual residence and construction of improvements, as required by the homestead laws.[62] Under familiar legal principles, a principal is charged with knowledge acquired by his agent who was empowered to purchase property on behalf of the principal.[63]

Knowledge that the opinion of officials of the government has changed concerning a question of law on which turned the validity of previously issued patents is not sufficient to take away the protection of good faith.[64] A transfer of ownership of a majority of stock of a corporation to persons having no knowledge of fraudulent acquisition of a patent by a person who acted for, and transferred the property to, the corporation does not enable the corporation to contend successfully that it is a bona fide purchaser.[65] If a mortgagee of a patentee can establish that it is a bona fide purchaser, its interest will be protected in an action by the United States to cancel a patent based on fraud of the patentee.[66] The burden of proving bona fide purchase is on the one asserting that defense.[67]

B. Statute of Limitations

In 1891 there was enacted the following statute of limitations of general applicability to patents for public lands of the United States, including patents issued for placer mining claims:

> Suits by the United States to vacate and annul any patent shall only be brought within six years after the date of the issuance of such patents.[67a]

When early considered by the courts, this statute was read literally and broadly to bar any action by the United States after the

---

[60] United States v. Krause, 92 F. Supp. 756 (W.D. La. 1950).

[61] United States v. New Orleans Pac. Ry., 248 U.S. 507 (1919).

[62] United States v. Cooper, 217 Fed. 846 (D. Mont. 1914).

[63] United States v. Smith, 181 Fed. 545 (D. Ore. 1910), *aff'd sub nom.* Linn & Lane Timber Co. v. United States, 196 Fed. 593 (9th Cir. 1912), *modified on other grounds,* 203 Fed. 394 (9th Cir. 1913), *aff'd,* 236 U.S. 574 (1915).

[64] United States v. Southern Pac. R.R., 184 U.S. 49 (1902). All past decisions of courts justified the view that the patents were valid; bona fide purchase was expressly provided by statute as a defense.

[65] United States v. Booth-Kelly Lumber Co., 246 Fed. 970 (D. Ore. 1917).

[66] United States v. Grover, 227 Fed. 181 (N.D. Cal. 1915).

[67] United States v. Cooper, 217 Fed. 846 (D. Mont. 1914).

[67a] 26 Stat. 1093 (1891), 43 U.S.C. § 1166 (1964).

statutory period had run, regardless of any mistake or error of the Land Department or any fraud or misrepresentations of the patentee, provided only that the land was public land of the United States and open to sale and conveyance through the Land Department.[68]

The landmark case of *United States v. Chandler-Dunbar Water Power Co.*[69] established that the statute bars an action by the United States even if the patent was void at its inception because it purported to convey land reserved for public purposes. The reasoning would apply equally to validate patents void for any reason where the United States owned the land at the time the patent issued.

At an early date, however, it was held that the statute does not begin to run until discovery of fraud where the fraud is actively concealed or is self-concealing in nature.[70] This is in accord with equitable principles long held applicable in construing other Federal statutes of limitations.[71] The burden is upon the United States to prove that (1) the fraud was concealed or self-concealing so as not to fall within the statute of limitations, and (2) it remained so for the appropriate period.[72] The United States must be specific in pleading the manner in which the fraud was effected and the steps taken to achieve secrecy.[73] Possession of the means of obtaining knowledge of the fraud is tantamount to knowledge itself,[74] and the United States may be precluded by laches from asserting that the statute was tolled for the necessary period.[75]

In a number of cases courts have considered whether fraud was concealed or self-concealing, and whether the United States was guilty of laches in not discovering the fraud. The character of land as mineral land can be considered concealed where the proofs include applicant's affidavit that the land is not mineral land.[76] The most common type of fraud involved in this group of cases is misrepresentation of ownership of the beneficial interest in a claim under homestead laws or under coal land laws so as to conceal the fact that the beneficial owner is not qualified to receive

---

[68] See United States v. Winona & St. P. R.R., 165 U.S. 463 (1897). The statute was not applicable in that case, so the language is dictum.

[69] 209 U.S. 447 (1908).

[70] Exploration Co. v. United States, 247 U.S. 435 (1918).

[71] Bailey v. Glover, 88 U.S. 342 (1875) (construing a statute of limitations section in a bankruptcy act).

[72] United States v. Bighorn Sheep Co., 9 F.2d 192 (D. Wyo. 1925).

[73] United States v. Christopher, 71 F.2d 764 (10th Cir. 1934).

[74] See United States v. Christopher, 71 F.2d 764 (10th Cir. 1934).

[75] United States v. Diamond Coal & Coke Co., 255 U.S. 323 (1921).

[76] United States v. Southern Pac. R.R., 11 F.2d 546 (S.D. Cal. 1926).

lands under those laws.[77] Unrecorded conveyances,[78] and use of nominees or trustees[79] have been found to be devices for actively concealing true ownership. Denial of fraud in response to inquiries also constitutes concealment.[80]

The United States is not placed on inquiry of fraud through knowledge that land was conveyed by the entryman within nine months after patent,[81] or through examination of books containing disguised indications of fraud where the examination was conducted for another purpose,[82] and perhaps not through information appearing in county real estate records of which information the government had no actual knowledge.[83] Knowledge that coal land was occupied by a coal company disqualified to acquire the land at the time the land was patented to an individual entryman probably puts the United States on inquiry notice of fraud.[84]

No cases have been found suggesting that failure to discover mistake or failure to discover lack of jurisdiction can be used as a basis to toll the statute of limitations.

The statute of limitations is part of the public land laws and is applicable only to public lands subject to acquisition under the laws enacted for the disposition of the public domain.[85] It does not apply to lands withdrawn from disposition under a swamp lands act by treaty obligating the United States to apply the land and the proceeds of its sale exclusively to the use, support and civilization of certain Indians.[86] It does not apply to lands as to which possessory rights have been earlier acquired by individual Indians,[87] to reserved

---

[77] See United States v. Diamond Coal & Coke Co., 255 U.S. 323 (1921); cases cited note 18 *supra*.

[78] United States v. Booth-Kelly Lumber Co., 246 Fed. 970 (D. Ore. 1917).

[79] United States v. Diamond Coal & Coke Co., 255 U.S. 323 (1921); Exploration Co. v. United States, 247 U.S. 435 (1918).

[80] United States v. Booth-Kelly Lumber Co., 246 Fed. 970 (D. Ore. 1917).

[81] United States v. Albright, 234 Fed. 202 (D. Mont. 1916). *But see* United States v. Diamond Coal & Coke Co., 255 U.S. 323 (1921), involving a pattern of conveyances from entrymen to the corporation almost immediately following the initiation of the right to purchase.

[82] United States v. Booth-Kelly Lumber Co., 246 Fed. 970 (D. Ore. 1917).

[83] See United States v. Diamond Coal & Coke Co., 255 U.S. 323 (1921); United States v. Christopher, 72 F.2d 375 (10th Cir. 1934). In each of these cases the question was posed by the court, but not decided.

[84] See Diamond Coal & Coke Co. v. United States, 233 U.S. 236 (1914).

[85] United States v. Minnesota, 270 U.S. 181 (1926); LaRoque v. United States, 239 U.S. 62 (1915); Northern Pac. Ry. v. United States, 227 U.S. 355 (1913); see Cramer v. United States, 261 U.S. 219 (1923).

[86] United States v. Minnesota, 270 U.S. 181 (1926).

[87] Cramer v. United States, 261 U.S. 219 (1923).

[88] LaRoque v. United States, 239 U.S. 62 (1915); Northern Pac. Ry. v. United States, 227 U.S. 355 (1913).

Indian lands,[88] or to acquired lands as to which there was no legislation authorizing sale.[89]

The statute of limitations has been found inapplicable in certain other fact situations. It does not bar an action by the United States to impose a constructive trust on property in aid of a prior decree, operating on the equitable owners only, holding the United States to be the rightful owner.[90] It does not apply to actions brought by the United States for the benefit of third parties.[91] The statute does not apply to bar an action by the United States to establish a breach of a condition subsequent in a grant based on legislation which made no provision for confirmatory patents.[92] One case has held the statute inapplicable to an action by the United States to have the title holder declared to be a trustee ex maleficio for the benefit of the United States.[93] This accomplishes indirectly what the United States could not do directly; it has never been followed on this point and probably should be regarded as an anomaly.[94]

Where an individual claims rights in lands derived through the United States and allegedly initiated subsequent to issuance of a patent to another and which could be given effect only by cancellation of that patent, the bar of the statute of limitations can be asserted successfully against the individual.[95]

An important and interesting question which apparently has never been decided, although it has been adverted to many times, is whether the statute of limitations applies to titles derived under certifications of lands to the states, pursuant to statute, rather than under patents.[96]

---

[89] United States v. Stewart, 121 F.2d 705 (9th Cir. 1941). The court found the case "readily distinguishable" from United States v. Chandler-Dunbar Water Power Co., 209 U.S. 447 (1908). It seems questionable whether the distinction between acquired lands not authorized to be sold and reserved public domain should have any relevance for the purpose of determining the applicability of the statute of limitations.

[90] Independent Coal & Coke Co. v. United States, 274 U.S. 640 (1927); United States v. Carbon County Land Co., 46 F.2d 980 (10th Cir. 1931), *aff'd*, 284 U.S. 534 (1932).

[91] Cramer v. United States, 261 U.S. 219 (1923) (an action for the benefit of Indian wards of the United States).

[92] Kern River Co. v. United States, 257 U.S. 147 (1921).

[93] United States v. Amalgamated Sugar Co., 48 F.2d 156 (10th Cir. 1931).

[94] The only case cited by the court to support this creation of a constructive trust is United States v. New Orleans Pac. Ry., 248 U.S. 507 (1919), cited in the concurring opinion. In that case, the beneficiaries of the trust were homestead claimants to whom the United States owed a statutory duty to protect their rights. This case falls within the exception noted at note 91 *supra*.

[95] Hogan v. United States, 72 F.2d 799 (9th Cir. 1934), *cert. denied*, 295 U.S. 752 (1935).

[96] Independent Coal & Coke Co. v. United States, 274 U.S. 640 (1927); Louisiana v. Garfield, 211 U.S. 70 (1908); United States v. Winona & St. P. R.R. Co., 165 U.S. 463 (1897). Dictum in the latter case indicates a view that the statute of limitations is applicable, but subsequent cases indicate that the question is an open one.

In conformity with the principle that the United States, asserting rights vested in it as a sovereign government, is not bound by any statute of limitations unless Congress has clearly manifested its intention that it should be so bound, 43 U.S.C. § 1166 is not applicable to an action for damages for obtaining a patent by fraud,[97] or to an action to recover the value of property patented by mistake.[98]

III. *Attacks by the United States on Oil Shale Patents:*

A. History of Issuance of Patents Covering Oil Shale Placer Mining Claims

Prior to the Mineral Leasing Act,[99] enacted on February 25, 1920, oil shale was a mineral subject to location under the mining laws of the United States. Many placer mining claims based on discovery of oil shale were located prior to that time.[100] The Mineral Leasing Act withdrew oil shale from the operation of the mining laws and made it subject to disposition by leasing only.[101] That Act did not impair the effectiveness of valid oil shale placer mining claims existent on February 25, 1920, and thereafter maintained in compliance with the laws under which initiated.[102]

In *Emil L. Krushnic,*[103] the Land Department held that failure to perform annual assessment work on an oil shale placer mining claim was a failure to maintain the claim in compliance with the laws under which initiated and automatically subjected the claim to cancellation by the government. The United States instituted contests against many of these claims on that basis and obtained a number of administrative rulings declaring specific oil shale placer mining claims void for failure to perform annual assessment work.[104] The question was pursued to the Supreme Court of the United States, where it was held that the United States could not challenge the validity of oil shale placer mining claims on the basis of failure to perform annual assessment work.[105] In that case the claimant had resumed assessment work before the contest was instituted, and the

---

[97] United States v. Whited & Wheless, 246 U.S. 552 (1918).

[98] See *ibid.* Mistake is not considered specifically, but the reasoning applies equally to cases involving mistake.

[99] 41 Stat. 437 (1920), 30 U.S.C. § 181 (1964).

[100] See Emil L. Krushnic (On Rehearing), 52 Interior Dec. 295, 298 (1928); *vacated* 53 Interior Dec. 45 (1930).

[101] 41 Stat. 451 (1920), 30 U.S.C. § 193 (1964).

[102] *Ibid.*

[103] 52 Interior Dec. 282 (1927); *rehearing denied,* 52 Interior Dec. 295 (1928); *vacated,* 53 Interior Dec. 45 (1930).

[104] See Union Oil Co. of California, 71 Interior Dec. 169 (1964); see also Schmidt, *Status of Unpatented Claims,* QUARTERLY OF THE COLORADO SCHOOL OF MINES, July 1964, p. 125.

[105] Wilbur v. Krushnic, 280 U.S. 306 (1930).

decision left some doubt whether this fact was essential to the result. The Land Department took the position that it was[106] and continued to contest and declare void oil shale placer mining claims upon which annual assessment work had not been performed during some period after enactment of the Mineral Leasing Act and had not been resumed prior to initiation of the contest. About five years passed before a challenge to the validity of this position of the Land Department reached the United States Supreme Court. That Court held, in *Ickes v. Virginia-Colorado Development Corp.*,[107] that the Land Department's position was incorrect and that the United States could not challenge oil shale placer mining claims based on failure to perform assessment work whether or not assessment work had been resumed prior to the time of initiation of a contest.

As a result of the Supreme Court decisions in the *Krushnic* and *Virginia-Colorado* cases and the Land Department contests which preceded them, there were many oil shale placer mining claims with respect to which administrative decisions had been entered holding the claims invalid on grounds found in the *Krushnic* and *Virginia-Colorado* cases to reflect an erroneous view of the law.

The Land Department then recalled and vacated the administrative decision involved in the *Virginia-Colorado* case.[108] Subsequently, United States patents have issued covering a number of claims without any action to vacate the decisions of invalidity entered in the earlier contest proceedings.[109] This procedure appears to have reflected a view by the Land Department that *Virginia-Colorado* rendered those contest proceedings of no effect[110] even though only two of the many contests were directly involved in that case.

On February 16 and 23, 1962, a number of mineral patent applications were rejected by decisions of the Manager of the Colorado Land Office.[111] These applications related to oil shale placer mining claims in Garfield and Rio Blanco Counties, Colorado, which had been declared invalid in contests instituted between 1930

---

[106] See Instructions, 53 Interior Dec. 131 (1930), *recalled and vacated sub nom.* The Shale Oil Company, 55 Interior Dec. 287 (1935).

[107] 295 U.S. 639 (1935).

[108] The Shale Oil Company, 55 Interior Dec. 287 (1935), *recalling and vacating* Virginia-Colorado Development Corp., 53 Interior Dec. 666 (1932). The Shale Oil Company, *supra,* held that all other department decisions in conflict with the decision of the Supreme Court of the United States in the Virginia-Colorado case were "overruled."

[109] See Schmidt, *Status of Unpatented Claims, supra* note 104 at p. 126.

[110] See Union Oil Co. of California, 71 Interior Dec. 169 (1964), at Appendices C-1 to C-6, inclusive; see also The Shale Oil Company, 55 Interior Dec. 287, 290 (1935).

[111] *E.g.,* Union Oil Co. of California, C-07667, Decision of Manager of Colorado Land Office, Bureau of Land Management.

and 1933 based on failure to perform annual assessment work.[112] The Manager of the Colorado Land Office held the claims invalid, not on the basis that the decisions in the earlier contest proceedings were correct, but that, under principles of finality of administrative action, estoppel by adjudication, and res judicata, they cannot now be challenged.[113] This position was sustained by the Solicitor on April 17, 1964, in *Union Oil Co. of California,*[114] subject to resolution of a question with respect to some of the claims as to whether the claimants had been afforded proper notice in the original contest proceedings.[115]

The following discussion of the validity of oil shale placer mining claim patents considers the general principles relating to attacks on patents and the special implications which the foregoing historical background has for the conclusive effect of oil shale placer mining claim patents.

B. Conclusiveness of Oil Shale Patents

In the absence of special circumstances which might exist in particular cases, there seems to be no basis upon which it could be maintained seriously that oil shale placer mining claim patents were issued as a result of fraudulent inducements by the patentees. The fact that a particular claim had been declared void in a pre-*Virginia-Colorado* contest would appear on the government's own records. Absent an affirmative representation by the applicant that no such contest existed, there would be no basis to charge the patentee with fraudulent concealment of such a contest. Prior to the 1962 decisions of the Colorado Land Office, the Department of the Interior was issuing patents in which a history of such contests appeared,[116] so there is no reason to believe that an applicant for patent would have attempted to conceal the existence and results of such a contest. The evidence of discovery of oil shale would be fully set forth in the patent application in the usual case, so an allegation of fraudulent concealment of absence of discovery should not be supportable.

---

[112] See Union Oil Co. of California, 71 Interior Dec. 169, 170 (1964).

[113] *E.g.,* Union Oil Co. of California, C-07667, Decision of Manager of Colorado Land Office, Bureau of Land Management.

[114] 71 Interior Dec. 169 (1964).

[115] The Solicitor explained that the effect of the statement in The Shale Oil Company, 55 Interior Dec. 287 (1935) that departmental decisions inconsistent with the decision of the Supreme Court of the United States were "overruled" was to destroy the value of these cases as precedent but not to vacate the decisions. It noted that The Shale Oil Company decision specifically "recalled and vacated" the decisions in the two cases directly involved in that proceeding. The Shale Oil Company decision also states that the adverse proceedings and decision of the Commissioner in that case "must be held as without authority of law and void."

[116] See Schmidt, *Status of Unpatented Claims, supra* note 104 at p. 126.

The Department of the Interior might assert that issuance of an oil shale placer mining claim patent resulted from mistake, in a situation where the claim's history includes a pre-*Virginia-Colorado* contest resolved unfavorably to the claimant. The argument would be that by mistake of law the Department of the Interior officials considered themselves compelled by law to issue patents notwithstanding such contests, and that this mistake became apparent only upon decision of *Union Oil Company of California.* There is only technical merit in this argument. A counter-argument could be made that until legal title passes from the United States, the Department of Interior is free to reconsider and reopen any proceeding at any time,[117] and that the issuance of a patent in these circumstances operated as a withdrawal of the determination in the earlier contest. If an attack is based on mistake, bona fide purchase would be a good defense.[118] If other elements of bona fide purchase are present, the existence of the possibility that the legal arguments which prevailed in *Union Oil Co. of California* might be made would not impair the bona fide purchaser status of one who purchased prior to that decision.[119] This is true even if the purchaser knew at the time of purchase that the Department of the Interior contemplated attacks on patents on such basis.[120] Furthermore, some of the arguments used by the Department of the Interior to support its decision in *Union Oil Co. of California* could be used in defending against an attack based on mistake.[121]

Lack of jurisdiction would seem to provide a stronger basis for attacks by the Department of Interior on these oil shale placer mining claim patents. The government's contention would be that when a contest is decided adversely to a claimant, and the claimant fails to appeal, the decision becomes final. The result is that the claim at that point is no longer valid, the land becomes part of the public domain and is subject to the congressional withdrawal of oil shale as a locatable mineral as effected by the Mineral Leasing

---

[117] See West v. Standard Oil Co., 278 U.S. 200 (1929); Gabbs Exploration Co. v. Udall, 315 F.2d 37 (D.C. Cir. 1962), *cert. denied,* 375 U.S. 822 (1963); see also Union Oil Co. of California, 71 Interior Dec. 169, 181 (1964).

[118] See cases cited at note 56 *supra.*

[119] See United States v. Southern Pac. R.R., 184 U.S. 49 (1902).

[120] See *ibid.*

[121] Thus, it could be argued that the change in interpretation of the requirements of the law since the patent should not be given retroactive effect. Union Oil Company of California, 71 Interior Dec. 169, 175 (1964). Also, the issuance of a patent being an adjudication of a special tribunal as to the validity of the claim, it could be argued that it is res judicata on this issue, at least where the Department of the Interior has acquiesced through failure to complain for a number of years. *Id.* at p. 176.

Act.[122] Therefore, the argument would proceed, the Department of the Interior was without jurisdiction to issue the patent, and it is void. The ability of the Department of the Interior to reconsider past decisions is limited to situations where the Department retains jurisdiction of the land.[123] It has no such jurisdiction as to withdrawn land, at least for the purpose of disposing of the land under the mining laws as land valuable for oil shale. Were this argument to prevail, bona fide purchase should provide no defense.[124]

Absent a successful frontal attack on *United States v. Chandler-Dunbar Water Power Company,*[125] section 1166 of 43 U.S.C. bars the United States from recovery of lands patented more than six years prior to attack where the attack is founded on mistake or lack of jurisdiction. No authority has been discovered holding that the statute can be tolled where these are the bases of attack. The United States would have a compensation remedy in these cases, but compensation should be based on the value of the land at the date of the patent less the amount paid by the patentee.[126] Bona fide purchase would insulate an owner from such remedy if the claim is founded on mistake.[127] Although no authority has been found, there is no reason to believe that bona fide purchase would provide a defense where the claim is based on lack of jurisdiction.

Serious concern is justified that an oil shale placer mining claim patent less than six years old, covering a claim held to be void in a pre-*Virginia-Colorado* contest, can be successfully attacked by the United States. Patents older than six years should be successfully insulated from attack by *United States v. Chandler-Dunbar Water Power Co.* Present owners of properties covered by those patents may be subject to a compensation claim by the United States without

---

[122] A similar argument, based on Executive Order No. 5327, which withdrew for purposes of investigation, examination, and classification all oil shale deposits owned by the United States, from lease or other disposal, subject to valid existing rights, was made but not pursued to its logical conclusion in Union Oil Company of California, 71 Interior Dec. 169, 183 (1964).

[123] See West v. Standard Oil Co., 278 U.S. 200 (1929).

[124] See text following note 56 *supra.*

[125] The possibility of such an attack cannot be discounted entirely. Cases which could be regarded as making inroads in the philosophy, although not the holding, of the case, include Exploration Co. v. United States, 247 U.S. 435 (1918) (holding that concealed fraud tolls the statute of limitations); and United States v. Whited & Wheless, 246 U.S. 552 (1918) (holding that the statute of limitations does not apply to an action to recover damages for fraud).

[126] As discussed above, the measure of damages has not received extensive consideration in the reported cases.

[127] The defense of bona fide purchase should apply in actions for compensation under the same reasoning applicable in actions to recover lands. See cases cited at note 56 *supra.*

regard to their status as bona fide purchasers.[128] In view of the aggressive attitude which the Department of the Interior has exhibited toward oil shale placer mining claims in the past, there is no reason to expect that attacks on oil shale patents will not be initiated and vigorously prosecuted.

Final evaluation of the effect which *Union Oil Co. of California* will have upon the conclusiveness of oil shale placer mining claim patents must be reserved until it is seen how the rules of law stated in that decision fare in the courts.[129]

ATTACKS BY INDIVIDUALS CLAIMING NO RIGHTS IN THE PATENTED CLAIM

The United States mining laws prescribe a procedure which must be followed by a claimant seeking to obtain a patent to a mining claim.[130] This procedure includes the following steps: (1) a copy of the notice of application for patent, and a copy of the survey plat, if applicable,[131] must be posted in a conspicuous place on the claim or claims covered by the application, (2) a copy of the notice of application for patent must be filed in the Land Office by the applicant and must be posted in the Land Office by the register and (3) a notice that application for patent has been made must be published by the register in a newspaper designated by the register as being published nearest the claim. The statute and the rules of the Department of the Interior[132] prescribe the length of time during which such posting and publication shall continue.

Notice given pursuant to statute is essential to vest in the Department of the Interior jurisdiction to issue the patent.[133] The notice affords all persons having an adverse claim the opportunity

---

[128] See Schmidt, *Status of Unpatented Claims, supra* note 104 at 127, where it is said:

> It is our view as title examiners in the State of Colorado that we will be forced to note on all title opinions concerning oil shale patents that, if the Department of Interior's present decisions as outlined on February 16, 1962, and April 17, 1964, are allowed to stand, all the patents heretofore issued with a history of such contests could be subject to suit by the Government to recover the land or the value thereof.

[129] Discussion of the merits of the Union Oil Co. of California decision and the present status of judicial actions which have been initiated to test the validity of the rules of law stated therein are not within the scope of this article. The only reported result to date is the denial of a motion by the United States to dismiss a complaint raising these issues. Oil Shale Corporation v. Udall, 235 F. Supp. 606 (D. Colo. 1964).

[130] 21 Stat. 61 (1880), 30 U.S.C. § 29 (1964).

[131] See 26 Stat. 1097 (1880), 30 U.S.C. § 35 (1964).

[132] See 43 C.F.R. § 3453.1 (1965).

[133] Silver King Coalition Mines Co. v. Conkling Mining Co., 255 U.S. 151 (1921); El Paso Brick Co. v. McKnight, 233 U.S. 250 (1914).

to be heard in opposition to the issuance of the patent.[134] This opportunity is not limited to claimants under the mining laws.[135]

It has been held that personal notice is not required to be given to conflicting claimants even if the applicant knew or could have determined from Land Office records the names and addresses of the conflicting claimants.[136] Notice given by publication brings all adverse claimants into the patent application proceedings.[137] It has been stated that notice so given is due process of law.[138] Failure of any claimant to file an adverse claim in the patent proceedings precludes the adverse claimant from contesting the patent, regardless of the substantive merit of his claim.[139]

No one can successfully attack a patent collaterally,[140] unless that patent is void.[141] Thus, it would seem that the only time a third party can attack a patent when the Department of the Interior had no jurisdiction to issue the patent, as where the lands never were the property of the United States, no legislation authorized their sale, or they had been previously disposed of or reserved from sale.[142]

In a limited area, however, a third party can maintain an action to have the patentee declared to be a constructive trustee for the benefit of the third party. This requires that the aggrieved party possess such an equitable right to the premises as would give him the title if the patent were out of the way,[143] or that through the fraud of the patentee the aggrieved pary who had a superior claim was kept in ignorance of the patent proceedings[144] or was fraudulently induced not to file an adverse claim,[145] in a situation

---

[134] El Paso Brick Co. v. McKnight, 233 U.S. 250 (1914).

[135] Northern Pac. R.R. v. Cannon, 54 Fed. 252 (9th Cir. 1893), *appeal dismissed on appellant's motion,* 166 U.S. 17 Sup.Ct. 997 (1896) (memorandum decision).

[136] *Ibid.*

[137] Wight v. Dubois, 21 Fed. 693 (C.C.D. Colo. 1884); Kannaugh v. Quartette Mining Co., 16 Colo. 341, 27 Pac. 245 (1891).

[138] Golden Reward Min. Co. v. Buxton Min. Co., 79 Fed. 868 (C.C.D.S.D. 1897).

[139] Golden Reward Min. Co. v. Buxton Min. Co., 79 Fed. 868 (C.C.D.S.D. 1897); Wight v. Dubois, 21 Fed. 693 (C.C.D. Colo. 1884); Seymour v. Fisher, 16 Colo. 188, 27 Pac. 240 (1891); see Gwillim v. Donnellan, 115 U.S. 45 (1885).

[140] Steel v. St. Louis Smelting & Ref. Co., 106 U.S. 447 (1882); Putnam v. Ickes, 78 F.2d 233 (D.C. Cir.), *cert. denied,* 296 U.S. 612 (1935).

[141] See St. Louis Smelting & Ref. Co. v. Kemp, 104 U.S. 636 (1882).

[142] See *ibid.*

[143] St. Louis Smelting & Ref. Co. v. Kemp, 104 U.S. 636 (1882); see Leonard v. Lennox, 181 Fed. 760 (8th Cir. 1910). This does not require that the claimant establish that at the moment patent issued it should have been awarded to him. It is enough if he has brought himself so far within the laws as to entitle him, if not obstructed or prevented, to complete his claim. Duluth & Iron Range R.R. v. Roy, 173 U.S. 587 (1899).

[144] Seymour v. Fisher, 16 Colo. 188, 27 Pac. 240 (1891).

[145] See Golden Reward Min. Co. v. Buxton Min. Co., 79 Fed. 868 (D. S.D. 1897).

where such party had a prior right.[146] Laches is a defense to claims of this nature.[147] State statutes of limitations may also provide defenses in appropriate cases.[148]

Placer mining patents must yield to extralateral rights of lode claims, and any question concerning such rights is not concluded by a patent but must be resolved by the courts.[149]

ATTACKS BY INDIVIDUALS CLAIMING A PRE-PATENT INTEREST IN THE PATENTED CLAIM

If a patent issues to fewer than all the owners of a mining claim, the patentee will be considered to hold title as trustee for the owners not named in the patent to the extent of their respective interests.[150] These latter persons can maintain an equitable action to enforce the trust.[151]

The same reasoning should result in a conclusion that easements, liens, and other interests in an unpatented mining claim, in appropriate proceedings, should be assertable as interests in legal title to the claim on issuance of patent. No cases considering this situation have been discovered.

Statutes of limitations requiring adverse possession or exclusive possession for creation of limitation title are of little value in defending against an alleged co-owner in Colorado, for the possession of one co-tenant is, under usual conditions, considered not to be adverse to other co-tenants.[152] Until actual ouster of a co-tenant has been established by conduct apart from mere use and occupation of the land, the statute based upon a claim of adverse possession does not run.[153]

In proceedings involving Colorado lands, Colorado Revised

---

[146] See United States v. Throckmorton, 98 U.S. 61 (1878) for a discussion of the types of fraud which will permit re-examination of a decree of court; see also Vance v. Burbank, 101 U.S. 519 (1880).

[147] United States v. Marshall Silver Mining Co., 129 U.S. 579 (1888).

[148] See *e.g.* (in the case of Colorado lands) COLO. REV. STAT., §§ 87-1-15; 118-7-8, -9, -11 (1963).

[149] Round Mountain Mining Co. v. Round Mountain Sphinx Mining Co., 36 Nev. 543, 138 Pac. 71 (1914); see Empire State-Idaho Mining & Dev. Co. v. Bunker Hill & Sullivan Mining & Concentrating Co., 114 Fed. 420 (9th Cir. 1902), *cert. denied*, 186 U.S. 482 (1902).

[150] Turner v. Sawyer, 150 U.S. 578 (1893); Ballard v. Golob, 34 Colo. 417, 83 Pac. 376 (1905).

[151] *Ibid.* These constructive trust proceedings are not technically attacks on validity of the patent; the effect of the patent to pass title from the United States is not challenged in these cases.

[152] Fallon v. Davidson, 137 Colo. 48, 320 P.2d 976 (1958); Rose v. Roso, 119 Colo. 473, 204 P.2d 1075 (1949).

[153] Fallon v. Davidson, 137 Colo. 48, 320 P.2d 976 (1958).

Statutes 87-1-15 (1963)[154] offers the best promise for a defense based upon a statute of limitations. To start this statute running, it is necessary that the trust be repudiated and the fact of that repudiation be made known to the beneficiary.[155] A conveyance by the trustee probably would effect repudiation of the trust.[156]

Recordation of the conveyance probably would not assure constructive notice to the beneficiary, for the constructive notice effect probably would be limited to persons acquiring interests after recordation of the conveyance.[157] The burden of proving that the cause of action accrued within less than five years before the suit was begun is upon the person denying the applicability of the statute.[158]

Special Considerations in Examining Title to Properties Title to Which Is Derived Under Oil Shale Placer Mining Claim Patents

In any transaction for the sale or encumbrance of patented oil shale placer mining claims where the values involved justify maximum care and caution, the scope of the customary examination of title to patented lands can be expanded to obtain additional information which will be helpful in evaluating the possibility that the patents could be challenged successfully.

Of course, no examination of official records could be expected to disclose actual fraud. The authorities with respect to bona fide purchase provide the only effective insulation from this infirmity.

I. *Abstracts of Title:*

A complette abstract of title should be examined rather than an abstract limited to that period of time beginning with the issuance of the patent. (This is not to suggest that such a limitation is ever advisable.) This will disclose any recorded claims of co-owners or of holders of other interests in the patented claim which were not recognized in issuance of the patent. Under the Colorado recording act[159] subsequent purchasers undoubtedly are on constructive notice of such recorded interests.

It is suggested that photographic abstracts be obtained, or that

---

[154] Colo. Rev. Stat. § 87-1-15 (1963) provides:
> In certain trusts, five years limitation. — Bills of relief, in case of the existence of a trust not cognizable by the courts of common law, and in all other cases not provided for in this article, shall be filed within five years after the cause thereof shall accrue, and not thereafter.

[155] Ballard v. Golob, 34 Colo. 417, 83 Pac. 376 (1905).

[156] Vanderwiele v. Vanderwiele, 110 Colo. 556, 136 P.2d 523 (1943); see Ballard v. Golob, note 155 *supra.*

[157] The Colorado recording act is found at Colo. Rev. Stat. § 118-6-9 (1963).

[158] Cliff v. Cliff, 23 Colo. App. 183, 128 Pac. 860 (1912).

[159] Colo. Rev. Stat. 118-6-9 (1963).

the examination of non-photographic abstracts be supplemented by a comparison with the original county records, to minimize the possibilities for error.

II. *Status Reports:*

Status reports based upon the Bureau of Land Management records in the applicable state office of the Bureau of Land Management and upon the Bureau of Land Management records in Washington, D. C., can be obtained. These reports can be prepared on the basis of personal examination of the records, but, in the case of the Washington, D. C., records, it is usually more convenient to cause them to be prepared by attorneys in that city.

Such reports would reveal whether the lands were subject to disposition by the United States at the relevant times and whether any adverse claims under the mining laws or other laws had been perfected in the Bureau of Land Management prior to issuance of the mining claim patent. They would also help reveal whether any contests had been conducted against the claim being examined prior to issuance of the patent, as discussed in more detail below.

Perhaps this step could be omitted without significant practical risk, in reliance on the usual check made by the Bureau of Land Management prior to patent.

III. *Patent Application Files:*

The files covering the patent applications can be examined to assure that no jurisdictional step was omitted. This is particularly important if the abstract discloses conflicting mining claims located prior to patent or if there are indications, in the status reports or elsewhere, of other conflicting claims of any kind. The notice and publication procedures prescribed by statute are jurisdictional and must have been followed to assure that such conflicting interests have been effectively extinguished. In many cases the patent application file will be in the National Archives in Washington, D. C., or in the Bureau of Land Management records in or near that city. In such cases the only feasible approach may be to cause the files to be examined by Washington, D. C., attorneys. Specific instructions concerning the matters to be checked should be provided to them.

Perhaps no significant practical risk would be involved in omitting this examination, for Bureau of Land Management officers would not knowingly have issued a patent if the essential preliminary steps had not been taken.

IV. *Contests:*

It is essential to determine to the extent possible whether the

claim on which the patent is based was previously held invalid in a contest based on failure to perform annual assessment work. This will determine whether there is danger that the patent can be attacked by the United States and whether the present owner may be subject to a claim by the United States for compensation. There is no easy way to ferret out these contests. Reference to contests found in the tract books and plat books in Denver and tract books in Washington, D. C., cannot be relied upon as complete. An unofficial tract book is maintained in Washington, D. C., relating solely to oil shale placer mining claims and sets forth references to contests and to patents issued in connection with oil shale placer mining claims. A large contest docket and a card file are maintained by the Bureau of Land Management in Denver. The latter probably is not complete. The former should be reliable and should disclose any such contest, but the contests are listed serially by contest numbers, with no index by claim name or legal description. Thus, examination of these books is an extensive and time-consuming task. If there is an easy way to determine whether a claim has ever been contested the author has not discovered it.

Once a contest is discovered, the file relating to the contest should be examined, if possible, to ascertain the outcome and, if adverse to the claimant, whether proper notice was given to interested parties.

V. *State Records:*

As an extra precaution, the records in the office of the State Board of Land Commissioners of the State of Colorado can be checked to assure that no claim to the lands is asserted by or under the State. Any such claim should be revealed by the federal records, but this additional check can be made quickly and provides further assurance that no such claim exists.

VI. *Miscellaneous:*

In addition to checking the above matters, which have particular relevance to the question of the conclusiveness of patents, other usual steps in title examination should be followed, such as surface inspection; geological inspection for known lodes; examination of the patent to ascertain the nature of reservations contained therein; examination of a certificate of taxes due; examination of a plat of a boundary survey; and examination of plats and field notes of the government surveys, to the extent this latter step is necessary to solve any special problems which may exist.

CONCLUSION

Although the title problems of owners of patented oil shale mining claims are not great in comparison with the problems of the owners of unpatented oil shale claims and in comparison with the problems involved in evolving a policy for development of federally-owned oil shale lands, they are nonetheless real. The fate of *Union Oil Co. of California* in the courts, and clarification of the policy which the Department of the Interior will adopt toward patented oil shale claims must be awaited before the questions concerning the conclusiveness of patented oil shale placer mining claims can be answered with confidence.

The Oil Shale Advisory Board

By H. Byron Mock*

When the editors of this publication asked me to comment on the Oil Shale Advisory Board the opportunity and challenge required acceptance. The board had been appointed by Secretary of the Interior Stewart L. Udall and first convened on July 7, 1964. Followers of oil shale problems know the report of the board was submitted in February of 1965 and consisted of twelve pages of report and six separate statements, one by each board member, covering an additional twenty-nine pages.[1] Some have labeled it a report with six dissents. To readers, but particularly to the six board members, such a result was frustrating. There were strong differences among the six, but in my opinion a broader area of agreement existed than we had time to hammer out. For this reason I am challenged to show that the report was not six dissents, but actually was six majority opinions.

I. Scope

The scope of this article is limited to the deliberations of the Oil Shale Advisory Board. Initially, I had a typical lawyer's irresistible impulse to try to cover the oil shale problems exhaustively, both policy deliberations and legal issues. In view of the able authors who are discussing many of those facets in this publication, the irresistible has been resisted; not entirely perhaps, but I have tried.

These comments propose to discuss the three problems suggested by the editors, namely:

1. Provide underlying background of the oil shale controversy;
2. Analyze the various arguments developed within the Oil Shale Advisory Board; and
3. Suggest necessary conclusions for guidelines which might be followed in development of both legislative and administrative policies.

*Partner in the Salt Lake City, Utah, firm of Nelson & Mock; A.B., University of Arizona (1933); LL.B., Georgetown University (1938); Member of Salt Lake City and American Bar Associations, Utah State Bar; member, Oil Shale Advisory Commission.

[1] Interim Report of The Oil Shale Advisory Board to The Secretary of The Interior, February 1965, transmitted by letter of Chairman, Joseph L. Fisher, February 15, 1965, 43 pp.

II. BACKGROUND

My interest in oil shale problems dates back to January 1, 1947, the date I assumed duties as the first Bureau of Land Management Regional Administrator for Colorado and Utah. Almost from the first day staff members working on mineral problems called my attention to active oil shale interests frustrated in their efforts to patent oil shale placer claims. In mid or late 1948 then Secretary of the Interior Julius A. Krug traveled to Glenwood Springs, Colorado, on a Denver and Rio Grande train fueled by shale oil. There he met with a large gathering of industry leaders and land or claim owners and gave his blessing to efforts to remove Interior obstacles to oil shale development. Before we left the concluding dinner meeting several delegations had demanded of me some affirmative action to implement the Secretary's stated goals. We tried. Numerous meetings were held with oil shale interests. With particular clarity are the several oil shale sessions at the annual Colorado Mining Congresses in Denver remembered. They were challenging and stimulating meetings. The President's Materials Policy Commission (commonly called the Paley Commission) had published predictions as to oil that the United States would "find it economical to turn increasingly to foreign supplies, and eventually to liquid fuel from shale and coal."[2] The Commission also stated ". . . synthetic oil, probably first from shale and later from coal will come into commercial production within a decade or so — perhaps sooner."[3] From all these meetings and reports a very basic fact emerged: the problem of unpatented mining claims and other factors contributing to a scattered land ownership pattern made it economically doubtful that either federal or privately owned lands could be developed independently. The Colorado problems were most heavily emphasized, but owners or claimants to oil shale lands in Utah were active too. My jurisdiction did not include Wyoming, so there is no first-hand knowledge of that area.

On September 2, 1952, we had reached the stage where the problems and remedies seemed reasonably clear to us in the field. On that date, over my signature as Regional Administrator, we sent by telegram a "statement submitted for oil shale justification." It is best summarized by quoting the first portion:

> Inadequate ownership information and failure to investigate validity of unpatented claims are obstructing development of an oil shale industry. The ownership pattern is so confused that neither government leasing of shale lands nor development of private holdings is

[2] PRESIDENT'S MATERIALS POLICY COMMITTEE, RESOURCES FOR FREEDOM, Vol. I, *Foundations for Growth and Security*, p. 107 (June 1952).

[3] *Ibid*, Vol. III, *The Outlook for Energy Sources*, pp. 8-9 (June 1952).

feasible. The U. S. Geological Survey has outlined the bodies of oil shale deposits; the Bureau of Mines has proved the feasibility of extracting oil from shale; oil companies are attempting to block shale holdings, as well as doing experimental work. The President's Materials Policy Commission has indicated that oil shale development is not only inevitable but imminent; but, if the ownership problem is not cleared up in advance, confusion as to ownership can block oil shale development in a period when time may be of the essence.

The principal oil shale deposits are located in Colorado, Utah, and Wyoming. The area of highest potential industrial development and of highest present interest is in Colorado. The deposits are principally on public lands. Except for those areas subject to mining claims, the government has withdrawn all oil shale lands from access and development. The problem is to determine which lands are subject to valid mining claims and to block private and public holdings.

The BLM is the agency responsible for solving the problem. Specifically the steps which would be taken are: first, collect data to allow determination of Federal and non-Federal ownership claims. This would involve: (1) obtaining from BLM land office records information to identify mineral ownership retained by U.S. on lands; (2) obtaining from other Federal agencies and county records the record of lands re-acquired by the U.S.; (3) obtaining from BLM Archives, and other files complete record of all withdrawals and restoration orders which affected availability of public land for mineral entry; (4) obtaining from BLM offices records of any other action which segregated lands from mineral entry; and (5) obtaining from county recorder's office record of all unpatented mining claims in the area.

Second: Clarify land descriptions by (1) as necessary, completing cadastral surveys, either original or re-survey; (2) processing mineral surveys; and (3) verifying location of mining claims by field check of monuments.

Third: Accelerate processing of claims to patent by (1) comparing claim with withdrawal and other segregation records to determine validity of claim at time of filing; (2) making field check of discovery and of necessary development work; and (3) issuance of patents.

Fourth: Cancelling invalid claims, as required.

Fifth: Blocking public and private oil shale holdings by (1) analyzing and mapping land ownership pattern in shale area; (2) initiating and processing exchanges of mineral lands to achieve solid blocks of holdings under private or public ownership; and

Sixth: Issuance of leases for shale lands as requested.

Even earlier, by August 22, 1952, Howard J. VanderVeer, then Regional Chief for Minerals, and others of my staff had already prepared, and without undue difficulty persuaded me to sign and submit, a "Proposed Project to Remove Public Land Obstacles to Oil Shale Development." On that date such a proposal, consisting of some seventeen pages and fourteen separate exhibits, was forwarded to the Director of the Bureau of Land Management in Washington, D.C. For various reasons the project was never approved, nor even,

so far as my knowledge goes, presented to the Budget Bureau or Congress.

In early 1954, my area of jurisdiction as a Bureau of Land Management field administrator was changed to exclude Colorado, but to add to Utah the States of Idaho, Nevada, and Arizona. Nevertheless, my interest in oil shale continued to be one of active participation as to all states because of membership on the Interior Department Colorado River-Great Basin Field Committee. Service as BLM (Bureau of Land Management) representative on that Committee ran from January, 1947, until my government service ended in February, 1955. The frequent meetings and annual study reports of that Committee placed steadily increasing emphasis on oil shale. There were coordinated presentations by representatives of the Bureau of Mines, U.S. Geological Survey, Bureau of Reclamation, the Bureau of Land Management, and to some extent by other agencies of Interior.[4] The inevitability of an oil shale industry was not doubted. Identification of the responsibility of each agency to further such development was our goal. In the analyses extensive consideration was given to the place of oil shale in relation to water power, to oil and gas, to fissionable source materials, and to other energy sources.

Very early I forcibly learned that long before my exposure to oil shale problems in 1947, extensive studies and action programs had been developed in that field.

Passage of the Mineral Leasing Act of 1920[5] recognized extensive prior mining claim activity, and included language allowing prior located oil shale claims to be perfected thereafter "including discovery." There were the regulations for oil shale leasing issued in the 1920's.[6] There were the records of relinquishments, also in the early 1920's, made by some mining claimants in return for the promise of preference leases as provided by law.[7] Some relinquishments had been accepted and at least in some cases recorded; the preference leases to this day have not been issued and conceivably may still be pending. There were the *New York World* articles of about 1928 by a General Land Office Regional Field Examiner crying out against the acquisition of oil shale claims by large oil

[4] *E.g.*, PACIFIC SOUTHWEST FIELD COMMITTEE, PROGRAM FOR THE PACIFIC SOUTHWEST REGION, 1956-1961, March 1954, p. 3.

[5] 41 Stat. 437, 451 (1920) as amended, 30 U.S.C. § 193 (1965).

[6] Circ. 1220, June 9, 1920 (53 Interior Dec. 127; 43 C.F.R., part 197 (1965).)

[7] 41 Stat. 445 (1920), 30 U.S.C. § 241 (1965).

companies as being improperly monopolistic.[8] The 1930 Executive Order withdrew and reserved designated shale lands, subject to valid existing rights, for investigations, examinations, and classification.[9] Then came the Interior Department's abortive efforts to cancel hundreds of oil shale claims on the theory that assessment work had to be kept current on such claims or the claims would become invalid.[10] Next came the two Supreme Court cases repudiating the departmental attempt.[11] Later there was the Shale Oil Company ruling wherein the Department "reversed" previous rulings that were contrary to the later Supreme Court ruling.[12] I also recall seeing departmental correspondence indicating no reinstatement need be made of claims previously declared null and void for lack of assessment work. Even more directly indicating the significance of the "reversed" ruling was the subsequent issuance of patents to thousands of acres of claims. Many of these claims were of the class which the Department's Solicitor of 1964 was to rule,[13] contrary to the actions of contemporary officials and, despite the Supreme Court rulings,[14] were null and void at the time of various administrative decisions of the late 1920's and early 1930's. Probably most impressive to me was the large number of dedicated mining men who had sunk every available dollar into developing and retaining and patenting oil shale claims. Even then sons of those original pioneers were succeeding to the struggle as the original pioneers began to die off. Today only a few of those original dedicated working dreamers still survive. Neither they nor we public officials of those days knew nor suspected that their claims were then null and void for procedural reasons and that the revelation[15] would be forthcoming in 1964, notwithstanding the even then "long established administrative practices."

There is no need here to elaborate further on these matters. They are mentioned as background and because it is always a source

[8] "Statement of Under Secretary of the Interior, John A. Carver, Jr. Before the Senate Committee on Interior and Insular Affairs concerning Oil Shale, May 12, 1965," mimeographed copy, page 4, referring to 1931 hearings of the Senate Committee on Public Lands and Surveys to Senate Resolutions 379, 71st Congress, and to other historical events regarding oil shale.

[9] Exec. Order No. 5327, April 15, 1930.

[10] The BLM Land Offices of Colorado, Utah, and presumably Wyoming, may still have the land files and references to the land and file designations of the numerous actions initiated.

[11] Ickes v. Virginia Colo. Dev. Corp., 295 U.S. 639 (1935); Wilbur v. Krushnic, 280 U.S. 306 (1930).

[12] The Federal Shale Oil Co., 55 Interior Dec. 287 (1935).

[13] Union Oil Co. of Cal., A-29560 (April 17, 1964), 71 Interior Dec. 169 (1964); later supplemented as to "adequacy of service" elements by the Solicitor's Opinion, A-29560-A (July 3, 1965).

[14] Cases cited note 11 *supra.*

[15] Union Oil Co. of Cal., 71 Interior Dec. 169 (1964).

of amazement to learn one's efforts are not an initiation of new ideas and actions, but only a continuation and only a relatively small part of many extensive contributions by others. Here, as many times before and since, it was impressed upon me how essential is a full factual background for sound decisions.

By April of 1963 it was reported that new oil shale regulations would be issued soon. Newspaper articles attributing such statements to responsible Interior officials appeared in August 1963.[16] Some deterring problems seem to have arisen and on November 5, 1963, Secretary of the Interior Stewart Udall invited "suggestions from the public at large looking toward formulation of a program to foster the orderly conservation and development of the vast federally owned oil shale deposits in Colorado, Utah and Wyoming."[17] A February 1, 1964, deadline for comments was fixed. Some oil men construed this to mean Interior feared to act without Congressional direction because of possible implications of "Another Teapot Dome Scandal" if lease terms were too generous or a "Scrooge" appellation if conditions imposed restricted development.[18]

III. CREATION OF THE OIL SHALE ADVISORY BOARD

The above explains my pleasure at receiving and being able to accept with high hopes the invitation of Secretary of the Interior Stewart L. Udall again to study oil shale problems. The invitation came in his letter of June 4, 1964, asking me "to serve as a member of a special Oil Shale Advisory Board . . . to analyze this whole problem." The problem was stated as being: "If the national interest is to be served, and this resource is to make an optimum long-term contribution to the economic well-being of the nation, the major public policy questions need to be identified and evaluated at the outset."

The Secretary proposed "a study in depth of this whole problem."

IV. FIRST MEETING, JULY 7, 1964

The initial meeting was held in Washington, D.C., on July 7, 1964; members present were:

Orlo E. Childs, President, Colorado School of Mines, Golden, Colorado

---

[16] See *e.g.*, Bernick, *Up and Down the Street: Interior Eyes New Rules for Oil Shale*, Salt Lake City Tribune, Aug. 25, 1963.

[17] U.S. DEP'T OF THE INTERIOR PRESS RELEASE (P.M. 37328-63), "Oil Shale Development Suggestions Invited by Interior," for release November 5, 1963; Also, 28 Fed. Reg. 11796, (1963).

[18] Bernick, *Up and Down the Street: Oil Shale Potential Starts Brush Fire*, Salt Lake City Tribune, Nov. 10, 1963.

Benjamin V. Cohen, Attorney, Washington, D.C.
Joseph L. Fisher, President, Resources for the Future, Inc., Washington, D.C.
John Kenneth Galbraith, Professor, Harvard University, Cambridge, Mass.
Lt. Gen. (Ret.) James M. Gavin, Chairman of Board, Arthur D. Little, Inc., Cambridge, Mass.
Milo Perkins, Economic Consultant, Tucson, Arizona
H. Byron Mock, Attorney, Salt Lake City, Utah.[19]

General Gavin attended our first meeting, but press of other assignments unfortunately prevented his attending later sessions and he subsequently resigned before the report was prepared. Secretary Udall presided. Also present were then Assistant Secretary for Minerals John M. Kelly, who was the alternate co-chairman from the Department, then Assistant Secretary for Public Lands (now Undersecretary) John A. Carver, Solicitor Frank M. Barry, and a tremendous array of experienced and able men from all parts of the Department. Members of the press were also present. Of major importance in this and all subsequent Board meetings was the presence of Captain Kenneth C. Lovell (USN), head of the Defense Department oil shale program.

Secretary Udall stated that he placed no narrow limits on the areas to be considered by the Board.[20] He then outlined "broad areas of policy that have come to the surface in our exploration of this problem."[21] In abstracted statements they were:

> . . . First, we must choose those policies which will assure that oil shale development makes its optimum contribution to the Nation's economy over the long term . . .
>
> Second, careful consideration must be given to the implications of oil shale development on our national and collective security . . .
>
> Finally, our actions with respect to oil shale must emphasize its conservation, not in the sense of hoarding, but in the creative sense of efficient recovery and wide use . . .[22]

The Secretary emphasized then and throughout our subsequent meetings that he wanted our independent unguided analysis. In later meetings he broadened his remarks to say he did not expect unanim-

[19] *U.S. Dep't of the Interior, Press Release* (P.N. 48827-64), "First Meeting of Oil Shale Advisory Board Set for July 7," for release July 3, 1964.

[20] *U.S. Dep't of the Interior Press Release* (*P.N.* 49030-64), "Opening Statement by Secretary of the Interior Stwart L. Udall at the first meeting of the Oil Shale Advisory Board, Washington, D.C., July 7, 1964," for release July 7, 1964.

[21] *Ibid.*

[22] *Ibid.*

ity and welcomed divergent views as a guide to exercising his special responsibility.

Key departmental technical personnel were then presented by Assistant Secretary Kelly and spoke on:

"Future Place of Oil Shale in the Energy Mix"..... V. E. McKelvey of the U.S. Geological Survey

"Legal Problems"..... T. J. Cavanaugh of the Solicitor's Office

"Technology of Hydrocarbon Fuels"..... J. S. Rosenbaum of the Bureau of Mines

We also were provided prepared statements for background purposes.[23]

Subsequently, in our executive session, Secretary Udall asked us to select our own Chairman, and Joseph L. Fisher, one of those headquartered in Washington, was chosen. We then agreed that each would submit to the Chairman an outline of issues which he felt required resolution.[24] Responsibility for the numerous details

---

[23] Material supplied before or at the initial meeting included:

1. *Background Data for Oil Shale Policy, March 1964,* prepared for Secretary Udall by the Bureau of Mines, Geological Survey and Office of Solicitor, 56 pp.
2. *The Oil Shale Policy Problem,* "a synopsis prepared for the opening meeting of the Department of the Interior Oil Shale Advisory Board, July 7, 1964," 46 pp.
3. "Summary of Suggestions from the Public for Oil Shale Program," Office of Assistant Secretary — Mineral Resources, April 12, 1964, 38 pp.
4. Map: "Oil Shale Deposits of the Piceance Creek Basin in Nothwestern Colorado:, D. of Int., B. of Mines," revised June 25, 1964.
5. Cowan, *A Bibliography of Bureau of Mines Publications on Oil Shale and Shale Oil, 1917-1963,* Revised December 1963, Laramie Petroleum Research Center, H. M. Thorne, Research Director.

[24] Data received included:

1. Papers presented to the *Western Resources Conference,* Oil Shale Section, Boulder County, Colorado, July 17, 1964, including:
   a. Steele, "Basic Research in Appraising the Future of Shale Oil."
   b. Landsburg, "Factors in the Long-Range Competitive Setting of Shale Oil."
   c. Kelly, "Remarks of John M. Kelly, Assistant Secretary of the Interior — Mineral Resources, Before the Western Resources Conference."
   d. Jackson, "Legal, Political, and Administrative Problems in Oil Shale."
2. Gooding, "Interdepartmental Energy Study, Research and Development in the Petroleum Industry," September 27, 1963, 7 pp.
3. Calhoun, "Leasing for Oil Shale Development on Public Lands," memorandum, July 9, 1964, 9 pp.
4. Donnell, *Tertiary Geology and Oil Shale Resources of The Piceance Creek Basin Between the Colorado and White Rivers Northwestern Colorado,* GEOLOGICAL SURVEY BULL., 1082-L, GPO 1961.
5. Quarterly of the Colorado School of Mines, "First Symposium on Oil Shale," Vol. 59, No. 3, July 1964.
6. THORNE, STANFIELD, DINNEEN, AND MURPHY, OIL SHALE TECHNOLOGY: A REVIEW, U.S. Dep't of Interior, B. of Mines, Info. Circ. 8216, 1964, 24 pp.

of our work was placed in Eugene W. Standley, Staff Engineer to Assistant Secretary Kelly. He ably absorbed those headaches for us.

Before discussing the development of issues, let us look at our total schedule through filing of our "Interim Report" in February 1965. As noted, material was sent us by Chairmen Fisher and Kelly as well as by Secretary Udall. Before adjourning on July 7 we agreed to meet in September for a visit to the principal oil shale area of Colorado, Utah, and Wyoming.

We gathered via Denver and Grand Junction at Rifle, Colorado, about noon on Sunday, September 13, 1964, and participated briefly in the Open House being held that day by Socony Mobil and Humble and others operating the Anvil Point Oil Shale Research Center at Rifle, Colorado, with the Colorado School of Mines on facilities acquired through the school from the Department of the Interior. We then went to Bureau of Mines facilities and held an afternoon executive session with Secretaries Udall and Kelly and other Interior personnel present. In the evening we returned to Grand Junction. On Monday in a Navy plane the Board viewed the tremendous hydrocarbon energy area of the vicinity. We flew over the Union Oil Company's experimental site; the Anvil Points experiment station in the Naval Oil Shale Reserves No. 1 and No. 3; the sodium prospecting area; Sinclair Oil Company's *in situ* shale oil operation; and another area that is considered favorable for oil shale stripping operations. Proceeding on the extensive tour we flew over the Rangely Oil Field, the Hell's Hole Canyon area where exposures of oil shale in the Green River Formation can be seen, the Bonanza Gilsonite area with its veins of solid hydrocarbon, and the Red Wash Oil Field with production mostly from the Green River Formation. Beyond Vernal, Utah, we flew in the vicinity of the Asphalt Ridge, the White Rocks area with its exposure of oil-impregnated Navajo sandstone, the Sunnyside asphalt deposits with the oil-impregnated sandstone beds in the Green River and Wasatch Formations, and back over Naval Oil Shale Reserve No. 2. En route we passed over several areas of interest, but in general we got a comprehensive view of the vastness of the area and the interrelation not only of oil shale but other sources of energy that are present in the vicinity. A business session was held all afternoon at Rifle and then continued at dinner and afterwards in Glenwood Springs. The following morning, the 15th, we met for two hours and then broke up to follow our respective courses for home. The informa-

tion provided us was beginning to ferment. The discussions were active and beneficial. Issues began to be drawn.[25]

The Board had generally agreed that we could not proceed to any final conclusions without an opportunity to hear the non-governmental advocates of oil shale activity. Accordingly, our next meeting was scheduled to hear those who had information of value for us.[26] It was held in Washington, D.C., beginning November 29. We listened to presentations by numerous capable and interested companies and individual spokesmen;[27] the pointed comments on

---

[25] At Rifle, Colorado, talks were given by:

1. Governor John A. Love, Colorado.
2. Professor James Gary, Colorado School of Mines, "Technology of In Situ Recovery of Oil from Shale."

At or subsequent to the Rifle meeting, the following data was provided to the Board:

1. "Summary of Oil Shale Resources of the Green River Formation in Colorado, Utah, and Wyoming," U.S.G.S., (undated, but presented Sept. 14, 1964), 14 pp.
2. "Earlier Oil Shale Proposals" (received by the Department), list of eight proposals (undated, but mailed September 25, 1964), 2 pp.
3. "Memorandum from the President Addressed to the Heads of the Executive Departments and Agencies on Government Patent Policy with Statement Attached," copy of pp. 18320 and 18321, CONG. REC., October 10, 1963.
4. McKelvey, "Economic Problems Attending Oil Shale Development," September 13, 1964, 25 pp.
5. Cavanaugh, "Disposition of money received under the Mineral Leasing Act," September 8, 1964, 3 pp.
6. Love, "Remarks by Governor John A. Love before National Oil Shale Advisory Committee," Sept. 13, 1964, 4 pp.

[26] U.S. DEP'T OF THE INTERIOR PRESS RELEASE, P.N. 54892-64, Office of the Secretary, "Oil Shale Advisory Board to meet with Industry," Nov. 13, 1964.

[27] Parties represented and documents presented included:

1. Governor John A. Love of Colorado, and associates, Ted Stockmar, Russell Cameron, Richard Eccles, Jack Tweedy, Frank Cooley and Richard Schmidt; "Statement of John A. Love, Governor of Colorado, to the National Oil Shale Advisory Board, Dec. 1, 1964, 6 pp.; and "Supplementary Written Statement of Governor John A. Love to the Oil Shale Advisory Board," December 1, 1964, 60 pp.
2. Messrs. O'Brian and Bradley, National Coal Association: "Statement to the Oil Shale Advisory Committee of the Department of the Interior, by Robert E. Lee Hall, Vice-President," (undated), 4 pp.
3. Curtis Morris, American Gas Association: "Statement Prepared for Oil Shale Advisory Board," December 1, 1964, 6 pp.
4. Dr. Charles F. Jones and Ray Sloan: a letter from Dr. Charles F. Jones, President, Humble Oil and Refining Company, Dec. 9, 1964, on "Research," with enclosures, 20 pp.
5. F. W. McWilliam, Rocky Mountain Oil and Gas Association: letter to Oil Shale Advisory Board, by F. W. McWilliams, Nov. 25, 1964, 2 pp.
6. Messrs. Hayes, Stones, Brown, and Black, Shell Oil Company: "Statement of Shell Oil Company Representatives before Oil Shale Advisory Board," Nov. 30, 1964, 4 pp.
7. N. B. Carson and Bruce Grant, Sinclair Oil and Gas Co.: letter to Oil Shale Advisory Board by J. B. Kennedy, President, Nov. 24, 1964, 3 pp.
8. T. W. Nelson, Dr. Dayton H. Clewell, and Jack E. Earnest, Socony Mobil Oil Co., Inc.: "Opening Statement to Oil Shale Advisory Board by T. W. Nelson," Dec. 1, 1964, 10 pp.

many of the issues began to make clear the developing line of the report. The three-day meeting ended on a note that we needed at least one more session to bring our thoughts into final form and again try to resolve differences that were appearing.[28]

The final meeting of the Oil Shale Board was held in Washington, D.C., beginning on Sunday, January 17, 1965, and continuing through the 18th. It was agreed that we had to get the report in by the 1st of February and this was the target we all set out to reach. Chairman Joseph Fisher was having a rough time getting a consensus, but he never ceased to strive toward it.

V. Issues

Against the chronological background we now can begin to develop the issues considered by the Board. At the initial meeting and carrying over into the issues proposed later in writing, three principal questions emerged. They were: First, would present opening of federal oil shale lands to development threaten our existing economy; second, is it in the public interest to proceed with developing an oil shale industry; third, can a method be provided for opening federal oil shale lands to development that affords full protection to all interests. The above was my conception of the basic issues, based on preliminary materials supplied to us and on my own personal experience. Each of the Board Members had agreed to send in a statement of his tentative proposals for the subject matter that the Board would consider. Of the five presented and distributed to the Board, mine was far from the most profound.

---

9. H. I. Koolsbergen, M. M. Winston, and A. F. Lenhart, The Oil Shale Corporation (TOSCO): "Oil Shale Development on Federal Lands, Supplemental Written Statement of the Oil Shale Corporation to the Oil Shale Advisory Board," Nov. 30, 1964, 37 pp.
10. John R. Pownall and John Allen, Union Oil Company of California: "Statement on Oil Shale Policy Matters to the Oil Shale Advisory Board of the U.S. Dept. of the Interior by John R. Pownall," Dec. 1, 1964, 6 pp.
11. J. H. Smith, Jr., and John Savage, Valley Landowners Association: exhibits of letters, 12 pp.

[28] Additional data received at or after the November-December meeting included:

1. "Developments at Rifle Oil Shale Plant under Lease Agreement with Colorado School of Mines Research Foundation," (undated, but mailed Dec. 4, 1964), 2 pp.
2. East, and Gardner, Oil Shale Mining, Rifle, Colorado 1944-56, U.S. Dep't of the Interior, B. of Mines Bull. 611, 1964, 163 pp.
3. Prien, Denver Research Institute, University of Denver, *"Oil Shale-Current Status of U.S. Oil Shale Technology."*
4. "Shale Oil: Colorado, Utah and Wyoming." Charts and schedules, U.S.G.S., Nov. 30, 1964, 13 pp.
5. Stoddard, "Surface Resource Protection-Oil Shale Exploration and Development," prepared by BLM for Oil Shale Advisory Board, (undated, but presented Nov. 29, 1964), 5 pp.

However, since it was mine, I feel free to use it. As submitted on July 16, 1964, it read:

> Questions and subquestions proposed for resolution by the Advisory Group on Oil Shale are:
>
> I. Does the "public interest" require control of the development of oil shale production?
>
> A. What "public interest"?
>
> 1. Defense needs?
> 2. International commitments?
> 3. National energy requirements?
> 4. National economy:
>
> a) Industrial development
> b) Area development
> c) Protection of current capital investment
>
> (1) Investments in the petroleum industry or the energy supplying industries
> (2) Investment in oil shale investments
>
> (a) Realty and deposits
> (b) Research investment
> (c) Improvements
>
> d) Prevention of waste of oil shale resources
> e) Prevention of waste of other resources (i.e., mineral, vegetative, space, recreational, etc.)
>
> B. Should control be restrictive or incentive or flexible?
>
> II. What is the procedural method desirable and possible for federal control of the oil shale resource?
>
> A. Availability of federally owned resources for leasing?
>
> [NOTE: Factual data required with some detail to determine feasibility includes:
>
> 1. What is the true pattern of ownership of the oil shale resources?
>
> a) Federal
>
> (1) Unencumbered
> (2) Subject to doubtful mining claims
> (3) Subject to probably valid mining claims
>
> b) State
> c) Privately owned
>
> (1) Unquestioned fee title
> (2) Questioned patents
> (3) Mining claims]
>
> B. Clearing of non-federal titles for initiation of development
>
> 1. Final decision as to patentability of claims or as to right to develop unpatented claims.
> 2. Exchange program to block federal and non-federal holdings into economically feasible units.
>
> C. Other controls of production as to either federal or non-federal holdings, or both
>
> 1. Restrictive regulatory agencies, pro-ration, allowables, etc.
> 2. Incentive
>
> a) Title security
> b) Exchanges
> c) Opening to leasing
> d) Tax adjustments
>
> III. Other questions arising from above as to timing, responsibility, etc.

After Co-chairmen Fisher and Kelly and others in Washington had had an opportunity to review all the recommendations a statement of "Issues to be Considered by the Oil Shale Advisory Board" was sent out. (My recollection is that mine reached me about September 3.) Since it shows the developing thought at that stage, it is quoted here as follows:

ISSUES TO BE CONSIDERED BY THE OIL SHALE ADVISORY BOARD

I. Should the Federal Government take any action at this time to permit development of oil shale on Federal lands?
Oil shale was withdrawn from disposition under the Mineral Leasing Act by Executive Order in 1930.

* * *

The first task of the Board is to advise whether underlying conditions have so changed since 1930 as to make it advisable to withdraw the Executive Order and permit some form of development of oil shale on Federal lands to proceed.

II. On the assumption that the Board recommends that development should not proceed now, what is its advice as to the circumstances under which development should proceed later? It is possible, for example, that the Board might make development contingent upon an energy supply shortage not now imminent, or on resolution of the problem (and hence extent) of privately owned shale lands, or on private development of a suitable technology and a dynamic competitive industry based on lands now in private ownership.

III. Experimental or commercial scale development?
   A. The Board might recommend that the Government proceed toward development immediately, beginning with an experimental or developmental phase to be undertaken at either Federal or private expense.
   B. Commercial development poses two broad alternatives:
      1. Uncontrolled development
      2. Development in which the Federal Government influences to a greater or lesser extent the timing, mode, and rate of development.

   In the event that 1. is adopted, no further basic policy questions would remain.
   In the event that 2. is recommended as the course of action, the Board should give advice as to the extent to which the following should influence Federal oil shale policy:
      a) Impact on other fuels
      b) Contribution to national economic growth
      c) Contribution to national security
      d) Impact on regional economic development
      e) Impact on international relations

IV. Having provided advice on the foregoing, four problems will remain to be resolved by the Secretary of the Interior, and the Board may wish to offer its advice on one or more. These problems — essentially residual of the broader policy considerations that the Board will deal with in I through III above, are:
   A. What specific programs should be followed to stimulate advances in oil shale technology?

1. Intramural research
2. Contract research
3. Privately financed research
   a) incentives

B. What should be the mechanics of private access to the public lands?
   1. Competitive leasing
   2. Noncompetitive leasing
   3. Concession arrangements
      a) Based on area?
      b) Based on volume of oil?

C. What means should the Government use to influence rate and mode of development?
   1. Taxation
   2. Subsidies
   3. Production limitations
   4. Federal participation in earnings

D. For what purpose should Federal revenues arising from oil shale development be used?
   1. States
   2. Reclamation or other special funds
   3. General receipts

(Mineral Leasing Act of 1920 stipulates 37.5% to States, 52.5% to Reclamation Fund, 10% to general receipts. Some states earmark their shares for special purposes.)

In the beginning two premises had been casually accepted and they operated as an impediment to the initial approach. Those premises were: First, that opening of the federal oil shale reserves could ruin the petroleum industry of the United States, and second, that the oil shale reserves within the United States were so completely controlled by the federal government that there could be no oil shale industry until the federal reserves were opened. By the time of the Rifle meeting in September of 1964, the second of these had been largely repudiated. Discussions of the reserves in Utah and Wyoming showed that there were substantial areas where the Federal Government did not control. This was clear in Utah and implied as to Wyoming. The presence of patented claims in an interspersed fashion was revealed in Utah as well as the presence of state owned school sections in the oil shale area.

Despite this, the presentations by the Department of the Interior personnel continued to be largely focused on the Piceance Basin with particular reference to the heartland of the vast oil shale reserves lying at depth. This heartland as I recall was not fully identified in the early 1950s when the Bureau of Land Management was considering an active program for opening the oil shale lands. Surrounding this heartland is an area of controverted oil shale claims which the federal government has, over the years by one means or another, attempted to invalidate. They are still in contro-

versy. The next ring away from the heartland consists of patented properties lying at lesser depth and with less thickness. Running through the heartland and both of the rings are areas of patented oil shale lands where the outcroppings have been revealed and where the parties had proceeded to patent in years past. Even the emphasis on the Piceance Basin heartland did not fail to reveal that the interspersed private holdings could still proceed without waiting for the lifting of the federal withdrawal order which prevented issuances of leases on federally owned resources.

Interestingly enough the result of the revelation that the federal government did not dominate the oil shale industry by withholding its reserves and, therefore, could not dictate the nature of the development completely was to cause an attack on private owners of oil shale lands for not having gone forward with development. The implication was that it made no difference whether the federal government opened the public lands and, therefore, we had no urgency in proceeding. This line of argument increased in force up to the final draft of the report. At least in my opinion, the presentation that was made in late November and early December when representatives of the private economy appeared before us, completely answered this argument.[29] The fear that a government-operated oil shale industry might come into being after private industry had gotten started in the less rich lands was a ghost that kept appearing. The other element was that private capital having been spent in the development and showing the way might give latecomers a chance to pick up federal leases and compete without having the vast initial investments that appear to be necessary. The other factor which was apparent as we saw the pattern of land ownership was that control of segments of federal land is essential to creating an economic block of state and fee lands in practically all areas.

The first premise as to the threat to a domestic petroleum industry was rebutted not only by the testimony of the representatives of the private segment of our economy but also by the facts that were continually presented to us by the Department of the Interior. Those facts revealed that the cost of extracting kerogen from shale was far greater than the cost of extracting petroleum from a well. The initial investments are greater and for a unforeseeable period the margins of profit would be quite low, if they existed at all. The ability to compete against petroleum, domestic or foreign, is of substantial doubt. The need to make vast expenditures in the development of techniques as well as in the acquisition

[29] See note 27 *supra.*

of the reserves and the construction of the plant facilities indicated that only by some sort of consortium could small operators hope to become active in an oil shale industry. This caused some concern. The interesting result of all the discussions was that on one hand we were being told that the resource was of such tremendous value that no one should be allowed to reap the rich harvest of profits from proceding; while on the other hand we were told that there was no market for the product and that no one could presently or foreseeably treat the oil shale as a valuable mineral deposit for purposes of discovery under the mining laws. One of the men appearing before us, representing what is probably the major producer of petroleum in the United States, stated emphatically that he felt the oil shale would eventually find its place in the energy complex, that it would be phased in and take its position but that it would not be destructive of the petroleum industry. In reply to a question as to why he felt his company should be "subsidized" by having all or part of the vast oil shale reserves "alienated" to it, he replied, "You may call that a subsidy; I certainly do not." One of the Board members later commented that it was the first time he had heard competitive bidding proposed for subsidies.

The developing of the issues ran into one major problem. The members of the Board, with certain minor exceptions, were men of such tremendous intellectual power that they were able to tackle and resolve problems rapidly. There was no false modesty about ability, but to me, as a bystander, that tremendous intellectual ability tended to carry us past certain common facts that might have justified further exploration. There is always a tendency for intelligence to abhor a vacuum. If no immediate explanation of a phenomenon is present, one is found. The need for broad factual information is particularly important in such an atmosphere. The stress of time, the urgency to complete, the desire to serve, all mitigated against the exhaustive treatment that each would have preferred.

At the Rifle discussion two additional issues were emphasized; they had been present before. The first was the problem of the legal interpretations in determining whether unpatented oil shale claims were valid. The Board was not unaware of comments throughout the country that the United States had repudiated the word of its employees over the years by issuing a 1964 opinion which placed a new interpretation on certain past actions of the Department. The Board was asked whether they agreed with the Departmental procedure in these matters. The problem was thoroughly discussed and the conclusion was that the Board was not in a position to pass on

the legal arguments and should not involve itself therein. The Board felt it was desirable to make an affirmative statement that the legal aspects of the mining claim problem were not investigated and that we felt it would be presumptuous for us to do so when the matter was one for the normal administrative tribunals and courts to consider. On that basis there was no further discussion of the mining claim legal problems and none of us felt that the Department should be condemned or praised for its position on those matters, but that the due procedures should continue.

The second matter emphasized at Rifle was the conservation problem. There was extensive discussion on the need to recognize other values in the areas where oil shale was found. This was of deep concern to all and it appeared in our final report. "Conservation" was a goal with which none disagreed. The exact meaning of the word, however, may not have been the same to all. Because it might offer the greatest possibility of conserving the values other than oil shale, the Board gave a great deal of attention to the extractive process known as *in situ*. This involves retorting the shale in the ground and extracting the liquid at the surface. The problems of disposal of waste, the destruction of the landscape, the filling in of the valleys and all of the related aspects might be avoided by such a process. Two questions would require resolution, however. The first is the economics of the *in situ* process if it is found to be feasible. The second is whether the process would waste any substantial amount of the oil shale by leaving in the ground unrecovered shale oil. If the definition of the word "conservation" includes the avoidance of waste of oil shale itself, then the effort to conserve other values in the area might be overweighed by the need to conserve the oil shale from waste. We never did completely resolve this matter. The details of extraction were far beyond our capacity on the basis of the time and information and training available.

The efforts of every Board member to come to grips with the problem before us was interesting. Continually we by-passed the basic problems and tried to tackle details; continually we had to back up. The question of the method of extraction is one example; the details of leases that might be issued is another; the nature of the research and development that should take place was still another. Incidentally, the term "R & D," meaning research and development, is another example of the need for clear definition. Did the term apply to basic research alone or to applied research as well? Did it cover adopting a tested technique in one area to a new area with varying physical problems? The questions are infinite,

even definition may not have resolved them. Some felt "R & D" was a detail; others indicated it might be a goal. Elements of that crept over into our final report.

Another problem continually discussed was concern over whether the federal government should get the maximum return to which it was entitled from the oil shale reserves it owned. This led to one interesting concept of collecting all information that could possibly be obtained before any lease was issued. On this basis the Government could then proceed to issue a lease based upon a fixed number of barrels of oil to be recovered. It took quite a little discussion to get to the heart of this question. It was resolved by pointing out that since no known method of recovery provided 100 per cent efficiency, to issue a lease on the number of barrels would lead to high-grading of the deposit, to the leaving of large amounts of the resource in the ground, to the inability to recover the marginal deposits, and to the destruction of the incentive to the lessee to increase his efficiency and productivity with a resulting increase to the federal government of gross receipts from royalties due to a greater recovery of the resource. Perhaps this problem was adequately resolved. Some of us were never sure it had been settled.

The question of who should do research and development continued to flare as an issue throughout all the discussion up to and including the final draft. Some felt that the Government should conduct all the research with its own personnel. Others appeared to feel that it should be done under a Government contract with the results becoming part of the national property to be used by any group that obtained a lease. Others appeared to feel that the Government should concentrate on basic research and leave the applied research to the private segment of our economy. The confusion of terms is obvious. There were heated discussions about the overfocusing of research by having it controlled from one place as contrasted to the greater possibility of a breakthrough by letting everyone have a try by his own method. A tendency to overgeneralize appeared in some of the proposals. The overgeneralization consisted of assuming that all companies were equally advanced or retarded in their development of the art of extracting the oil shale product. Some wondered if those that are behind were not trying to get the resources retained in federal ownership until they could catch up. We never knew. Certainly an overgeneralization was not called for. The companies are not going to reveal their research secrets; those secrets are part of their assets. Companies may be reluctant to go into a research program where the results go out into the public domain and everyone can start at the same time.

They may be willing to cooperate on research but they would not like to be held back in its application until everyone else is equally ready.

The other overgeneralizations that crept in are illustrated by the continued emphasis of the Piceance Basin as though it were typical of all the oil shale reserves. This was not intended but the impression, nevertheless, prevailed. There was no true distinction between deposits that were shallow and deep; between those that are thick or thin; the beautiful areas and waste areas; the solidly blocked ownership patterns and the scattered patterns; the federally dominated areas and the fee or state dominated areas; the presence of water and numerous other matters infinite in their variety.

At this point it should be pointed out that the first preliminary draft of our report was dated November 11 and was received by the Board members prior to their holding the hearing in Washington for the presentation by non-federal parties. Some of us treated this as the format with which we would try to live; others thought that it was subject to a complete revision. At least two of us took the draft and interlineated our comments as a complete rewrite without changing the format. Others wrote complete revisions of portions as a suggestion. This was done after we had held our November-December meeting in Washington. At the January meeting it had become clear that we were not going to get a consensus. In order to complete the report our chairman, Joseph Fisher, had come up with the agreement that we would have a consensus and each would have a chance to make his pointed comments or exceptions to that in a footnote if he wished and also each would present his own personal views in a separate statement that would be attached *in toto.*

By the time the report came out it seemed to me that we had resolved two questions. First, there was no public interest that justified holding up an oil shale industry. As a consequence thereof there was no public interest that necessitated indefinite delay of lifting the withdrawal on the federal oil shale lands. The second conclusion was that there were definite public benefits to be achieved from opening the oil shale reserves. Specificially, a letter from the Assistant Secretary of the Navy presented to us by Captain Lovell stated that the Navy felt it was of extreme urgency to know whether oil shale could be developed for use as a reserve by the Navy in time of need. It was obvious that pure research was not enough and that applied research had to be perfected before that question could be answered. We had to have an active oil shale industry before we could know the answers. Apparently we had reached a pretty full agreement on those two points.

The question of method, however, was another problem. We clearly did not approve an uncontrolled release of the federal oil shale reserves; nor did the group approve a government-operated oil shale industry. Some commented that no one had ever proposed a government operation, but in the discussions the point was brought out that just before the 1920 period the Department of Navy had specifically proposed to work and operate the oil reserves at Elk Hills and Buena Vista, California, and Teapot Dome in Wyoming as a government operation. Some felt that there had been recent suggestions in Washington, based on the false premise that the federal government owned all the oil shale reserves, that there be a government corporation patterned after the Satellite Corporation to handle the oil shale reserves. These points are incidental but had to be faced in the process of our consideration.

The method to be used resolved on what was the optimum return to the public interest. Rather naturally this came down to dollars. How could the federal government get the maximum dollar return? The other side of that question is, how could private individuals be presented from unjust enrichment? We all had the same objective — get the optimum return to the nation — as the Government and as the landlord, both from rental and royalty revenue and from taxes. We shared a common belief that no special favorites should be benefited in the Government's administration of the oil shale reserves. This may have led some to the belief that the oil shale reserves could not be opened up because some might get special benefits. It led others to believe that only by opening them up on a competitive system could special benefits be denied. This deep concern for the propriety of the operation probably was the greatest problem we had to resolve. Our goals were identical, our proposals of method different.

A complete treatment of our problems which we discussed requires discussion of the ghost of Teapot Dome. This phantom appeared before, during, and after our deliberations. It probably will never entirely go away. It was used to justify government research and to justify "research and development" leases. It was used to justify issuing competitive leases and it was used to justify no leases. A few basic facts about the Teapot Dome controversy may help to bring the problem into perspective.[30]

---

[30] Recommended reading on Teapot Dome is:

1. BATES, THE ORIGIN OF TEAPOT DOME (PROGRESSIVES, PARTIES, AND PETROLEUM, 1909-1921), University of Illinois Press (1963).
2. NOGGLE, OIL AND POLITICS IN THE 1920'S: TEAPOT DOME, Louisiana State University Press (1962).

The original controversy over the Naval oil shale reserves was not one of scandal but one over what legal rights, if any, the Honolulu Oil Company and others had in the oil reserves set aside for the Navy. The controversy turned on whether the Government could invalidate the rights these parties asserted under prior issued permits or whether those parties would be able to continue their operations. It is interesting to note that Honolulu Oil Company won that fight. The similarity with the present fight of oil shale mining claimants seeking patents and the position of the Government try to deny them is fascinating. As noted above the Advisory Board did not see fit to pass on the legal problems and yet the parallel with the early oil reserve problem of California is intriguing. It was not until a later period when the Secretary of Interior was accused of granting special favors to his friends on the Naval reserves that had been transferred to his administration that the term "Teapot Dome" became one of complete opprobrium. As time has passed the events of the two periods have become merged into one. Any discussion of opening up Naval reserves or of lifting the withdrawal on other oil shale lands brings back memories of a scandal and all phases of the controversy are blanketed thereunder. It is interesting to note that the scandals of the Teapot Dome period turn on the granting of favoritism for a few in the development of federally owned resources. The proposal of a method by which a few would be allowed to do research and then get a special grant based upon someone's approval of the results may come closer to the problems of Teapot Dome than would the opening of the lands to competitive leasing. Providence would have to protect the federal administrator who decided between two equally belligerent contestants for an oil shale lease on the basis of which the administrator preferred, rather than on some other more objective and less controversial test. At least to me, the taint of Teapot Dome and its application to the oil shale reserves of the Federal Government will best be laid to rest by opening all or part of the Federal oil shale lands to competitive leasing with performance requirements written in that eliminate those who cannot or will not develop the reserve. This does not mean that all should be opened at once but in my opinion some should be. To some the withholding of the federal oil shale reserves from development may be construed to be as great a granting of favors to those who wish to restrict competition in that field as would be the direct issuance of preference to such people. This dilemma is one common to public administrators. To my mind affirmative action is the only solution.

The avenues and by-ways that were explored by the board were

infinite. In the final comments, it is obvious that many were not explored by all together, but that some of the board brothers participating in the drafting were drawing on other sources of information. Certainly that was true in my case. Had the time been available to hammer out clean decisions on various factual questions, much of the apparent disagreement might have been eliminated. At our final meeting this was becoming quite apparent. It was not until that period that the board finally adopted and agreed upon a statement of goals and incorporated it in the draft which became the January 21st draft. Perhaps we should have fixed those goals in the beginning but that was not possible. In an effort to fix the points on which we had agreed, I undertook to prepare a statement of facts and to have them adopted by the board. On some we agreed; on some we did not. Consequently, we eliminated the entire list that I proposed. They are, however, of sufficient interest, at least to me, to set them forth as a footnote for consideration by any others who may in the future be delving into the oil shale problem.[31]

---

[31] The proposals were:

1. Oil shale development is not presently a matter of major concern in the over-all national needs for energy.
2. Efforts to develop a viable oil shale industry as an alternate source of national energy supplies is in the national interest.
3. Immediate efforts to develop an oil shale industry do not pose a serious threat to that portion of our national economy represented by the oil industry and other industries supplying our energy requirements.
4. Parties interested in oil shale development are in various stages of progress toward commencement of a commercial oil shale industry.
5. The federal government controls some 75% of the total acreage and some 85% of the known reserves of oil shale. An additional 5% of both acreage and reserves may be controlled by the federal government depending on the outcome of pending controversy over the ownership of unpatented mining claims. The remaining ownership of acreage and reserves is in private ownership with some in the states of Wyoming and Utah in state ownership.
6. At least one company and perhaps others are proceeding to develop known oil shale reserves not in private ownership.
7. Withdrawing or maintaining the withdrawal of federal reserves from development will not necessarily prevent development of an oil shale industry by those able to acquire private and state lands.
8. Withholding the federal reserves from access creates a favored position for oil shale development in the hands of the relatively few holders of non-federal lands.
9. Numerous companies or groups of investors are demonstrating substantial interest and making major investments in efforts to develop an oil shale industry.
10. Withholding federal lands will not prevent such development, but will restrict competition and may reduce the probabilities of a breakthrough into successful and economically feasible development.
11. The federal oil shale reserves could be attractive for speculative investment, as contrasted to development investment.
12. The lands involved have values other than those for oil shale. Conservation standards for protection against waste of the oil shale resource itself, for the protection of surface, other mineral values, scenic values, and other values, and protection against pollution and other damages have not been established.
13. The federal government can act contractually to achieve such conservation standards as to federal lands but must cooperate with state and

VI. Conclusions

Having participated with my fellow board members physically, orally, and composition-wise, and having shared their deep interest in oil shale, their unflagging concern for the public interest, and the pressures and frustrations, I must state basic truth to you who may read these comments:

1. Secretary Udall refused to guide us to pre-determined conclusions. He invited and incited diverse opinions. He deliberately forced us to open any new problems we found necessary.

2. It is remarkable that as much was accomplished as was. The delineations of basic conflicting philosophies was an accomplishment. Reconciliation of them might have been possible with more time.

3. Had members of this Board been willing to lend their names to a staff study prepared for them, a less controversial report might have resulted. Not one would have done so, and Secretary Udall

---

local governments and private owners to achieve them as to the remaining area.

14. If federal government wholly or in part withholds access to the federally owner reserves for development, the federal government will not be participating in the development of conservation standards and inducements to orderly development that is in the best national, regional, and local interests.
15. The present stage of oil shale development indicates that continuing adjustment and improvement in the techniques of extraction and processing for the oil shale industry is neeeded to achieve and maintain an economically feasible place in the national energy picture for oil shale.
16. Development of standards for protection of values other than oil shale requires substantial cooperative effort by all segments of our society — federal, states, and private. The establishment of such standards that can be observed within economically feasible limits will have major effect on the development of an oil shale industry.
17. Other considerations, such as depletion and quotas and other factors will also affect the development of an oil shale industry. Such factors are believed to be beyond the scope of this board's mission.
18. The proceeds received by the federal government from its owned oil shale reserves are distributed under the terms of the Mineral Leasing Act of 1920 on the basis of 37½% to the state of origin, 52½% to the reclamation fund, and 10% to the General Fund in the U.S. Treasury. The large sums which may be received in the future, costs of administration and possible costs of protecting other public interests in the area without unduly burdening the oil shale industry with such public benefit expenses may require review of the propriety of the above distribution of receipts. Again, this is a problem noted for consideration, but one considered to be beyond the scope of this board's mission.
19. The current controversy over the ownership of unpatented mining claims creates a situation that allows neither federal nor private — and in some cases state — control of the controverted lands for purposes of development. Until such controversies are resolved the lack of necessary certainty of title in federal or non-federal ownership retards development.
20. The federal government is receiving no present income either in royalties, rentals, or as tax base from its oil shale reserves and has increasing continuing expenses in their management.
21. Withholding oil shale reserves from access or granting of access without making such access open to competition can be expected to evoke accusations of "favoritism" against responsible federal officials.

and Assistant Secretary Kelly were not parties to any pressures in that direction.

4. Joseph Fisher, in the unenviable job of chairman, did a tremendous job in gaining as much consensus as was obtained. Without his firm conference guidance and unflagging efforts to reduce our discussions to written form acceptable to us, there might have been no consensus report at all.

5. All of us, and probably the chairman most of all, would have welcomed several "head-knocking" sessions, beginning where we ended, to factor out facts and issues.

6. Such sessions could have hammered out "findings-of-fact" and "definitions." Such "definitions" clearly stated would have minimized differences arising from words apparently common but actually pregnant with different meaning to each of us. Such "findings-of-fact" would have restricted the reliance and emphasis by each of us on the beliefs and half-truths not agreed upon but drawn upon from the widely divergent backgrounds of the six board members. Without these common grounds of understanding and the limits fixed by them, no agreement could be reached.

7. No group could have been more unalterably dedicated to our national public interest, nor more concerned with an effort to be fair toward all segments of our society. We differed on methods, on some factual conclusions, on timetables of urgency — they were honest differences. No one could be more privileged than was I in testing my principles and beliefs against such fine minds, splendid gentlemen, and principled Americans. My appreciation of the need for and the importance of the democratic process is reaffirmed; my respect for those with whom I differ is enhanced; my desire to continue exploring those differences in search of fundamental truths is burning even more brightly.

8. But even had we been able to "head-knock" into a common recommendation, we still were only "Advisory." The burden of decision and the full responsibility rest directly on the Secretary of the Interior. His concerns are multitude, the pressures of a many-faceted public interest unending. As one of us six majority opinion writers said to Stewart Udall after the report had been made public: "Each of us had definite views on what you should do, but not one of us was certain that he would follow that advice were he sitting in your place."

Consistent with all those conclusions and specifically without necessarily dissenting from the last, my mind turns to an old and wise sailor's remark: "Even the best pilot and navigator can not

steer a drifting ship." My views in the separate "majority" opinion remain the same:

> No proven public interest precludes development. There is a national urgency requiring that we commence. To wait too long may waste all or part of the vast oil shale reserve as its place in energy history is passed by and we go on to other energy sources. Ample precedents for protecting all aspects of public interest are available and workable. Failing to give private capital a chance to try is wasting three great resources: The ingenuity of private enterprise, revenue from rentals and from the tax base of new capital assets, and possibly the shale resource itself.

Development of a viable oil shale industry faces many problems. Until we face them, those problems will not be solved. Objections to every proposed solution will continue to proliferate. Positive losses from delay are far more damaging to our national interests than possible losses from mistakes in proceeding.

The Oil Shale Advisory Board had to stop before it finished. At least it found that opening federal oil shale reserves need not be detrimental to the national interests and that keeping them locked up may be.

Water for Oil Shale Development

By Robert Delaney*

Before a shale oil industry can become a reality, a firm and dependable supply of water must be developed. No process yet devised can function without the use of considerable quantities of water. If not in the mining, then certainly water is required in the necessary refining and processing required for the movement of shale oil through pipelines or by other means. The quantity of water required for industrial use varies according to the process being considered. Some processes involving mining and a minimum of refining after extraction require relatively small quantities of water. If the products are refined to the point of use at or near the site of mining, then a much greater supply of water will be required. If the in situ process of retorting, utilizing steam, should be employed, then obviously an enormous amount of water would be necessary.†

Apart from water required for removal, refining and processing of shale oil, the industry will require many people. A common estimate is that for each individual directly engaged in the shale oil industry, there will be five persons resident in the area. Using another common estimate of one-fourth of an acre foot of water per year per person, a large amount of potable water with low mineral content must be developed suitable for domestic use.[1]

Assuming the area of water use to be in proximity with the oil shale deposits along the northerly side of the Colorado River from Rifle, westerly and extending northerly into the Piceance Basin, the source of water must necessarily be the Colorado River and the White River, with their tributaries, together with a limited ground water possibility of uncertain potential.

The water demand may be expected to increase proportionately as the shale oil industry develops; likewise, since shale oil technology is developing from experimental processes to prototype plants, and may be expected to proceed into full scale commercial production,

---

*Partner, Delaney & Balcomb, Glenwood Springs, Colo.; member, Colorado and American Bar Associations; LL.B., Westminster Law School, 1946.

†Editor's Note: Space does not permit detailed attribution of technical data related to mining and refining processes involved in the production of kerogen. For a brief and lucid technical reference work, see East, *Oil-Shale Mining, Rifle, Colo., 1944-56* (U. S. Bureau of Mines Bull. 611, 1964).

[1] The Mineral Resources Board of the State of Colorado in 1961 estimated that a shale oil production of 1,000,000 barrels per day in western Colorado would require development of a new metropolitan area of 340,000 people, with some 59,130 residents directly employed in the shale oil industry. Mineral Resources of Colorado, First Sequel (1960), 458.

water requirements should have a corresponding gradual increase. Many indulge in the fallacious assumption that the development of firm water supplies to meet the potential demand may be deferred until technology and other conditions launch the industry.

To date, there has been little cooperative planning or unified action by the oil shale interests toward developing water supplies required for a major industry. It is surprising that several of the major oil companies, while expending millions of dollars for the acquisition of oil shale deposits, have failed to take even a second look at water requirements obviously necessary for the development of those deposits. It is more surprising that the United States, with the Naval Oil Shale reserves, the vast amounts of oil shale under control of the Bureau of Land Management, the money spent through the Bureau of Mines on the oil shale demonstration plant with a declared interest in being a major participant in the oil shale program has not taken an active role in studies and planning for water supplies to meet the requirements of the industry.[2]

If this water supply euphoria continues, the day will almost certainly come when oil shale developers will find themselves seriously handicapped or curtailed by lack of water and at a serious disadvantage with their more farsighted competitors who are now actively engaged in developing supplies of water to keep pace with the development of the industry. The water that could be developed to support a major oil shale industry is subject to the intense competition for water from the Colorado River, and oil shale is in danger of losing by default.

The water supply problem has been recognized from the beginning of major planning on oil shale development. In 1953 a state financed study was made under direction of the Colorado Water Conservation Board to determine present and potential water requirements in Western Colorado in an attempt to secure agreement about transmountain diversions.[3] In the course of these studies, an excellent committeee comprised of the best engineers, hydrologists, and other persons obtainable, including representatives of most of the major oil companies, then interested in the area, conducted intensive studies concerning oil shale industry water requirements, and concluded that for a two million barrel per day operation a diversion or stream withdrawal of 625 cubic feet of water per second of time, or 455,000 acre feet of water per year, would be required.[4]

---

[2] While some 31,000 acres of Piceance Creek lands in shale-bearing areas are in Naval Reserves 1 and 3, over 200,000 acres are privately held. *Id.* at 451.

[3] Colorado Conference Committee & Colorado Water Conservation Board, Water Requirements of an Oil Shale Industry, Sept. 24, 1953.

[4] *Id.* at 4.

This would involve a net consumptive use of 400 cubic feet of water per second, or 290,000 acre feet per year with a return flow to the stream of 225 cubic feet of water per second, or 165,000 acre feet per year. It was further stated in their report that:

> A large scale oil shale operation will require water at essentially a constant rate throughout the year . . . .[5]
>
> From available hydrographic data, it seems evident that the only practical and economic source of water to a shale oil industry is the Colorado River, and its tributaries, in and upstream from the oil shale area. It also seems apparent that storage reservoirs will be required to assure a continuous water supply to an oil shale industry of 625 cubic feet per second.
>
> The industry hopes that the report of the Conference Committee to the Colorado Water Conservation Board, and, in turn, the Board's report to the General Assembly of the State of Colorado will show:
>
> (1) that a potential oil shale development in Western Colorado will require an estimated 625 cubic feet per second of Colorado River Water,
>
> (2) whether 625 cubic feet per second of Colorado River Water will be available to a shale oil industry,
>
> (3) what storage will be required to assure the availability of this amount of water,
>
> (4) how the financing, construction and operation of such storage facilities can most appropriately be handled and,
>
> (5) the availability of reservoir site or sites, which will be required for storage purposes, to assure a continuous water supply to an oil shale industry of 625 cubic feet per second.[6]

In the course of the same studies, a report was written and published entitled: "Report on Depletion of Surface Water Supplies of Colorado West of Continental Divide." Mr. Raymond Hill, an eminent engineer and hydrologist of the firm of Leeds, Hill and Jewett of Los Angeles was the author of the report, which was compiled after months of study and investigation at a cost of nearly fifty thousand dollars. The report is recommended reading to anyone interested in water supplies from the Colorado River or its tributaries. It is stated in the report that:

> Development of the oil shale reserves in Western Colorado should be anticipated and the consumption of water for industrial, municipal, and other purposes resulting therefrom may reach 300,000 acre feet per year.[7]

Importantly, it should be pointed out that this is a depletion, or consumed-use figure, and not a stream diversion figure with return flow.

---

[5] *Ibid.*

[6] *Ibid.*

[7] Leeds, Hill and Jewett, *Report on Depletion of Surface Water Supplies of Colorado West of Continental Divide* 59 (Bull. No. 1, Surface Water Series, Colorado Water Conservation Board, 1953).

The answer to the oil shale water supply problem rests with surmounting both natural and legal obstacles. There is a tremendous fluctuation in the flow of both the Colorado and White Rivers from day to day, from month to month, and from year to year. Most annual runoff occurs within a month or six weeks when the snow melts in the high mountains. In this short interval, water supplies exceed the present adjudicated demands. During the remainder of the irrigation season, in most years, the adjudicated demands exceed th supply, so that, on the Colorado River at least, releases from storage are necessary to satisfy the present irrigation and other adjudicated rights, without taking into account new uses for oil shale.

The answer to the problem, of course, rests in the construction of large storage reservoirs, at or above the points of diversion. These reservoirs must have capacity available not only for seasonal fluctuations, but also for cyclic variations to equalize flows between years of high runoff and those of drought. This situation was aptly described by Mr. Raymond Hill in the above mentioned report as follows:

> Under present conditions, very little water would be available during the irrigation season to satisfy the diversion requirements of industry. The natural flow of the rivers is already being used to its utmost to serve lands under irrigation, except during the winter months when the demand for water is insignificant and except during the period of snow melt when the rivers are in flood. Hence, conservation of flood flows by storage in reservoirs will be necessary to satisfy even a small industrial demand.
>
> The only existing reservoir which might be used for this purpose is Green Mountain Reservoir on Blue River constructed by the United States as part of the Colorado-Big Thompson Project. The diversion requirements of the oil shale industry itself might be satisfied by releases from this reservoir but the far greater requirements of the other industries could not so be met. The additional storage reservoirs which will be needed do not have to be located upstream from Rifle; on the contrary, there would be considerable advantage in having a large reservoir in the immediate vicinity of the potential industrial area.
>
> Opportunity exists for the creation of a suitable reservoir by construction of a dam in De Beque Canyon at the lower end of the valley within which the industrial development would presumably be centered. Diversion requirements of such industries could be satisfied by the withdrawal of water from the reservoir without regard to the inflow at the time. Return waters, except the very small proportion which might be unduly contaminated by chemical processes, could be returned to the same reservoir without waste downstream. All irrigation requirements in the Grand Junction area could be satisfied, without conflict with any other use, by the release of water from the reservoir, and the average quality of the irrigation water would be somewhat improved over that now available in the summer months.

> It is recognized that the cost of construction of such a storage project would be large, primarily because of the necessity of relocating the trunk highway and railroad which now follow Colorado River. This cost, however, would be insignificant in comparison to the tremendous capital investment which must be made to industrialize the region and which will not be made until there is assurance of ample water.[8]

As to the availability of stored water, it should be recognized that there is very little water available from the Green Mountain Reservoir for industry or shale oil. This reservoir on the Blue River, with a capacity of about 152,000 acre feet, has 52,000 acre feet allocated to replacement purposes in order that other Colorado-Big Thompson facilities may divert their full allocated amounts for use in Eastern Colorado and 100,000 acre feet allocated for use in Western Colorado. Most of this 100,000 acre feet is already being used during dry years for agricultural and other existing uses that have priority over oil shale development under the provisions contained in Senate Document 80,[9] allocating this water. Interim contracts have been entered or negotiated in recent years for industrial water from Green Mountain Reservoir, but the limitations imposed by the Secretary of Interior under the requirements of Senate Document No. 80 are such that the water contracted for can only be counted on for interim use until it is needed for other preferred purposes. Thus, Green Mountain Reservoir will not be of substantial assistance in supplying stored water for shale oil development.

The other reservoirs on the headwaters of the Colorado River, including Shadow Mountain, Granby Reservoir, Grand Lake, Williams Fork Reservoir, and Dillon Reservoir, are all committed to uses in Eastern Colorado, and therefore will not be of assistance to a shale oil industry in Western Colorado.

The Ruedi Reservoir on the Fryingpan River, with an active capacity of 100,000 acre feet of water, is now under construction by the Bureau of Reclamation. Part of this water should be available for sale, for industrial or municipal use in the oil shale area, through purchase from the Secretary of Interior, acting through Region 7, Bureau of Reclamation, Denver, Colorado.

Water acquired from either the Green Mountain Reservoir, or the Ruedi Reservoir would be released to flow down the channel of the Colorado River, where an equivalent amount, less evaporation and seepage losses, could be pumped out, at or adjacent to, the points of use below Rifle, Colorado.

Probably the best source of oil shale industry water in the

---

[8] *Id.* at 49-50.

[9] S. Doc. No. 80, 75th Cong., 1st Sess. 3 (1937).

Colorado River drainage would be from the Crystal River. For several years the Bureau of Reclamation has had under study the West Divide project, contemplating one or more dams on the Crystal River with diversion by tunnels and canals for use along the southerly side of the Colorado River to a point approximately opposite DeBeque, Colorado. This water could be used to good advantage for municipal use and also for industrial use. The water thus developed would be of excellent quality, much better than that from the Colorado River. The weighted average concentration of dissolved solids in the Colorado River near DeBeque or Cameo is estimated at 387 parts per million, with 2,300 parts per million of suspended sediment, whereas, Crystal River water would be below 225 parts per million of dissolved solids, and below 220 parts per million of suspended sediment, according to the United States Geological Survey.[10]

As one of the projects entitled to participate in power revenues from the Basin Fund of the Upper Colorado Storage Project Act, the West Divide Project should have substantial financial assistance from the United States. What is needed primarily to get this project moving is a demonstration of interest and commitments for municipal and industrial water by oil shale owners and developers. Such interest should be manifested to the Bureau of Reclamation, Grand Junction, Colorado, or Salt Lake City, Utah. It appears probable that with an adequate municipal and industrial commitment, this project could be built so as to deliver water coincident with the needs of the shale oil industry.

The Colorado River Water Conservation District, Glenwood Springs, Colorado, has plans and conditional adjudication decrees for reservoirs that would provide water for part of the oil shale needs. Contractual commitments have been made, and additional commitments are obtainable for water to be delivered from these facilities when built. These reservoirs include the Iron Mountain Reservoir on the Eagle River, with storage capacity of approximately 50,000 acre feet, the Una Reservoir on the Colorado River between Rifle and DeBeque, with active projected capacity of about 170,000 acre feet and the White River Reservoir on the South Fork of the White River, with projected capacity of about 125,000 acre feet.

Some of the more realistic companies having shale oil interests have combined storage adjudications with direct flow adjudications from both the White River and the Colorado River. From the White River, these include both gravity diversion into the Piceance Basin,

[10] U. S. GEOLOGICAL SURVEY REPORT, MINERAL AND WATER RESOURCES OF COLORADO (1964).

and also pumping installations. From the Colorado River, plans are projected, according to adjudication claims, to pump water from the Colorado River over the Book Cliffs to the Piceance Creek Drainage area, which would appear to be an enormously expensive lift system. The direct flow claims, for which conditional adjudication decrees have been obtained from the Colorado River between Rifle and DeBeque exceed the entire flow of the River during some seasons. Many of these decrees optimistically obtained are probably abandoned for failure to show due diligence in putting the water adjudicated to a beneficial use. In several instances, the claimants have not offered proof of diligence in alternate years in the district court as required by statute.[11]

Direct flow adjudication decrees of this nature are of value to oil shale developers if properly obtained, entered, and maintained by reasonable diligence, with proof thereof offered in alternate years, because they reduce the quantity of water required to be obtained from storage. During periods of high seasonal runoff, water is available under such rights. Also, some winter flows are available for such rights during the non-irrigating season. These direct flow rights would also reduce the quantity of water required to be released from storage in order to guarantee a firm and dependable supply.

Steps taken by some oil shale owners toward obtaining water supplies seem to indicate a lack of definite or clear purpose, and a lack of basic understanding of what is involved in obtaining a firm water right available for industrial or municipal purposes. In several instances, ranches have been purchased with the intent at a subsequent date of converting their irrigation rights to the use of oil shale development. Such irrigation rights afford the owner the privilege of taking, according to his order of priority, a quantity of water for irrigation purposes. The irrigation season is from April to October. Irrigation rights, regardless of how early the priority, do not give the appropriator the right to divert winter flows for industrial or domestic use. Winter flows must be separately adjudicated and will be junior or inferior to all decrees previously entered in the same water district.[12]

In order to change the point of diversion from the headgate of the irrigation ditch to the place where it is to be diverted for oil shale purposes, it is necessary to obtain a decree from the district

---

[11] COLO. REV. STAT. § 148-10-8 (1963).

[12] See Greeley & Loveland Irr. Co. v. Farmers Pawnee Ditch Co., 58 Colo. 462, 146 Pac. 247 (1915); Colorado Milling & Elevator Co. v. Larimer & Weld Irr. Co., 26 Colo. 47, 56 Pac. 185 (1899); and COLO. REV. STAT. § 148-9-13(3) (1963).

court changing the point of diversion.[13] Such a decree will not be entered if the rights of other appropriators, including those junior or inferior to the applicants are adversely affected.[14] In some instances, the courts will decree a reduction in the amount that can be diverted in order that other appropriators will not be adversely affected and on that basis will authorize a change in point of diversion as to a portion of such right.[15] Conversely, a right once changed to a new point of diversion, cannot thereafter be taken from the old point of diversion without a similar statutory proceeding. Thus the lands previously purchased become largely valueless because of lack of water, and the water right moved to the new location may be of small value because of reduction in quantity to meet adverse claimants' objections and because of the limitation on the period when diversions can be permitted under an irrigation right.

Another serious problem in the purchase of rights with intent to transfer their points of use, arises in the case of an incorporated or mutual ditch company. It would appear doubtful whether the owner of water rights reflected by shares in a mutual ditch company could, without consent of the other owners having shares in such company, remove the water adjudicated to the company ditch to another point of diversion, regardless of whether the other shareholders were adversely affected.[16]

Yet another example arises from the fact that such claimants often fail to recognize that the direct flow adjudication right, whether for irrigation, domestic, or agricultural purposes does not give the owner the right to store the water so diverted.[17] By the same token, the right to store, properly adjudicated, affords the claimant the right in order of priority of filling the reservoir once in a season,[18] and cannot be used as a direct flow right.[19] A direct flow right does

---

[13] COLO. REV. STAT. §§ 148-9-22 to -25 (1963).

[14] COLO. REV. STAT. § 148-9-25(2) (1963). See DeHerrera v. Manassa Land & Irr. Co., 151 Colo. 528, 379 P.2d 405 (1963).

[15] COLO. REV. STAT. § 148-9-25(2) (1963). See Colorado Springs v. Yust, 126 Colo. 289, 249 P.2d 151 (1952).

[16] The question appears to depend on whether or not the by-laws of the ditch company restrict the right to transfer the water right. If there is such restriction, the shareholder may not transfer. Model Land and Irr. Co. v. Madsen, 87 Colo. 166, 285 Pac. 1100 (1930). However, in the absence of such restriction, the shareholder can change point of diversion subject to rights of other stockholders. Wadsworth Ditch Co. v. Brown, 39 Colo. 57, 88 Pac. 1060 (1907).

[17] Greeley & Loveland Irr. Co. v. Farmers Pawnee Ditch Co., 58 Colo. 462, 146 Pac. 247 (1915). *But see* Seven Lakes Res. Co. v. New Loveland & Greeley Irr. & Land Co., 40 Colo. 382, 93 Pac. 485 (1907), however, this latter decision has not been followed and was rejected in City & County of Denver v. Northern Colo. Water Conservancy Dist., 130 Colo. 375, 276 P.2d 992 (1954).

[18] Holbrook Irr. Dist. v. Ft. Lyon Canal Co., 84 Colo. 174, 269 Pac. 574 (1928).

[19] *Cf.* Cache La Poudre Res. Co. v. Water Supply & Storage Co., 25 Colo. 161, 53 Pac. 331 (1898).

not take precedence over a storage right, but the two are governed by the order of priority decreed by the court; that is, if the decree for the reservoir is senior in time and by administrative number, to the direct flow right, then the reservoir is entitled to one fill ahead of the direct flow right.[20]

In evaluating adjudicated water rights, prospective purchasers sometimes fail to distinguish between conditional and absolute decrees, and fail to recognize that where a decree is conditional, it can only be made absolute by proof in the district court that the conditional requirements have been met with due diligence. This is particularly important where a ditch may have been originally constructed to carry a full adjudicated capacity, but subsequently was allowed partially to deteriorate causing a reduced carrying capacity so that the amount that can be proven to be used is less than that conditionally decreed.

Also, where the duty of water is defined to require irrigation of a specified number of acres, proof of irrigation of that number of acres must be offered before the decree can be made absolute,[21] whereas, in the case of an absolute decree, the decreed water can be used on a greater or lesser or different acreage so long as the original point of diversion is maintained and the demands placed on the decree are not enlarged over those existing when the decree was rendered.[22]

Of course, if the decreed amount of water or a portion thereof has not been used for a long period of time, it may raise an inference of abandonment, and abandonment can be invoked on a proceeding to change the point of diversion.[23] In the same vein, a water right, after diversion from a public stream, being in the nature of real estate, can be lost by adverse possession.[24]

One very misleading impression can be gained by simply observing or measuring the quantity of water flowing at a given time, or on an annual basis, in either the Colorado or the White Rivers. The legal and administrative complexities, particularly on the Colorado River, are numerous, and are becoming even more so each year. Persons contemplating a direct flow diversion from the White River or the Colorado River, or contemplating storage on one or more of

---

[20] COLO. REV. STAT. § 148-5-1 (1963). See People *ex rel* Park Res. Co. v. Hinderlider, 98 Colo. 505, 57 P.2d 894 (1936).

[21] Arnold v. Roup, 61 Colo. 316, 157 Pac. 206 (1916); Drach v. Isola, 48 Colo. 134, 109 Pac. 749 (1910).

[22] Arnold v. Roup, 61 Colo. 316, 157 Pac. 206 (1916).

[23] Means v. Pratt, 138 Colo. 214, 331 P.2d 805 (1958); Arnold v. Roup, 61 Colo. 316, 157 Pac. 206 (1916).

[24] Mountain Meadow Ditch & Irr. Co. v. Park Ditch & Res. Co., 130 Colo. 537, 277 P.2d 527 (1954).

the tributaries to these rivers, would be well advised to first consult with the Division Engineer of the State Engineer's Office at Glenwood Springs, who supervises water administration on the Colorado River, and the Division Engineer at Steamboat Springs, who has supervision over the White River, pertaining to the method of administration and adjudicated demands against the streams.

Over sixty percent of the Colorado River water must be allowed to leave the state to satisfy compact commitments to other states.[25] Of the remaining water, senior decrees require that amounts adjudicated be allowed to reach their respective headgates. Thus, it is not the quantity of water used under a decree, but rather the amount permitted to be diverted that governs the administration of the stream. On the Colorado River, there is a substantial power adjudication below the oil shale area that must be met on a year-round basis, as well as other decrees calling for water in the winter months. A diversion in the oil shale area would not be permitted, except during high runoff, even where there was a substantial part of the water returned to the stream after use, unless enough stored water were added to make up the net depletion.

During the summer months, part of the water flowing in the Colorado River, particularly during dry years, is stored water released from the Green Mountain Reservoir to meet decreed rights below Rifle, particularly for the Grand Junction area.

Under the provisions of Senate Document No. 80, these releases, in addition to generating power at the Green Mountain Reservoir, are made to supplement the flows of the Colorado River so that irrigation and domestic needs within the Colorado River drainage can be met. Thus, a junior or inferior right on a side stream will be permitted to continue diverting for irrigation purposes, even when the natural flow of the river is insufficient to meet senior demands in the Grand Valley area, because these demands are made up or replaced from storage releases out of Green Mountain Reservoir. As mentioned above, oil shale requirements, while recognized as

[25] By Art. III(d) of the Colorado River Compact [COLO. REV. STAT. § 149-2-1 (1963)], the Upper Division states (Colorado, Wyoming, Utah, and New Mexico) cannot deplete flows at Lee Ferry below 75,000,000 acre feet in each ten year period. The average virgin flow at Lee Ferry for the period of 1896 to 1964 has been approximately 14,878,000 annually, of which Western Colorado provides about 71%, or approximately 10,500,000 acre feet annually. By the Upper Colorado River Basin Compact of 1948 [COLO. REV. STAT. § 149-8-1 (1963)], Colorado was apportioned 51.75% of the water allocated to the Upper Division, after an allowance from the Upper Division share of 50,000 acre feet annually to Arizona. If virgin flows permit the Upper Basin to deplete the stream by 7,500,000 acre feet annually, then Colorado would have approximately 3,855,375 acre feet annually. More recent and more realistic water supply estimates place the Upper Basin water supply at not more than 6,200,000 acre feet annually, of which Colorado would be allotted 3,182,625 acre feet annually.

permitted uses from Green Mountain, are not free uses, and are subordinated to the agriculture and municipal requirements within the Colorado River drainage.

Another variable arises from the fact that there are numerous conditional decrees committing water to future use, but not yet diverted, which when developed will take precedence over currently adjudicated appropriations. This is particularly significant in relation to conditional decrees for transmountain diversions where there will be no return flow to the river and the depletion is therefore equal to the diversion.

For the above and other reasons, the water supply and the net depletions above the oil shale area cannot be measured or determined with precision. When an oil shale water demand is defined with certainty, the supply must take into account the uncertainty and fluctuation of the river and the diversions therefrom for natural as well as legal and administrative reasons, and the supply available for diversion must be computed on an estimate with adequate storage to compensate for a considerable margin of error.

There are various storage possibilities on tributaries of the Colorado and the White Rivers, some of which are available for development. A private company undertaking to construct and utilize such storage should recognize that an on-channel reservoir is a major undertaking. It should be commenced only with the most careful investigation as to available water supply, as well as geological and other relevant conditions at the dam site and in the storage area. Other problems arise in providing the means of delivery to the place of use, land acquisition, and right-of-way, particularly if some portion of the reservoir will occupy federal lands. Plans for such a reservoir must be approved by the State Engineer[26] and for obvious reasons the standards of construction will be rigid, with a large measure of safety both in dam construction and in spillway capacity. It should, above all, be borne in mind that a builder of a reservoir is held to a higher standard of legal responsibility than in most other pursuits.[27] His duty is not limited to ordinary care or lack of simple negligence, but he is in fact practically an insuror. A corporation vulnerable to suit should probably consult Lloyds of London before beginning construction.

The moral of the story is that at this time it would behoove all the major oil shale interests and the United States to join forces to cooperate and initiate a program for major storage to keep pace with the rapidly developing technology of oil shale.

---

[26] COLO. REV. STAT. § 148-5-5 (1963).

[27] See, *e.g.*, COLO. REV. STAT. § 148-5-4 (1963).

Records, Documents and Services of the Colorado Land Office, Bureau of Land Management

By W. F. Meek*

I. Introduction

Preliminary to any action taken regarding public lands, or minerals on lands which are owned by the United States, the attorney should have a thorough working knowledge of their status. This paper is designed to explain the material which is available in the Colorado Land Office, a part of the Bureau of Land Management, and to acquaint the researcher with the records systems used in determining land status. In order to understand this system, it is necessary to give a short background of the responsibilities of the Land Office and its resulting activities.

The State of Colorado contains approximately 66 million acres.[1] Of this amount 8⅓ million acres[2] are public domain over which the Bureau exercises its duties on both the surface and subsurface. Added to this are the oil and gas, withdrawal, restoration, exchange, right-of-way, mineral claims, mineral occupancy, Public Law 84-167,[3] and other Land Office responsibilities over approximately 18 million acres of lands reserved for other agencies, primarily the Forest Service.[4] Also included is accountability for certain mineral ramifications of approximately 5½ million acres of lands[5] patented under 1909,[6] 1910,[7] and 1914 Acts.[8] In addition, the Land Office handles all mineral responsibilities on lands patented under the Stockraising Homestead Act of December 29, 1916,[9] which totals 8½ million acres. And last, but not least in importance, are approximately two million acres[10] of lands acquired under the Bankhead-Jones Act,[11] from the Farmers Home Administration, Federal Land Bank, and

---

*Land Office Manager, Bureau of Land Management, U. S. Department of Interior, Denver, Colorado.

[1] Government Printing Office, *Public Land Statistics, 1963,* p. 3, table 1.

[2] *Id.* at p. 18, table 9.

[3] 69 Stat. 367 (1955), 30 U.S.C. § 601 (1965).

[4] Government Printing Office, *Public Land Statistics,* 1963, p. 30, table 10.

[5] Land Office records.

[6] 35 Stat. 844 (1909), 30 U.S.C. § 81 (1965).

[7] 36 Stat. 583 (1910), 30 U.S.C. § 83 (1965).

[8] 38 Stat. 509 (1914), 30 U.S.C. § 122 (1965).

[9] 39 Stat. 862 (1916), 43 U.S.C. § 291 (1965).

[10] Land Office records.

[11] 49 Stat. 436 (1935), 7 U.S.C. § 343 (1965).

others. All told, the Land Office responsibilities extend over 42 million acres, which is approximately two-thirds of the state.

It has been 190 years since the first land office was opened in Virginia.[12] At that time our national population was about 2¾ million.[13] It has been 102 years since the first land office was opened in Colorado and 101 years since our present land office was opened in Denver.[14] By 1864 the nation's population had grown to nearly 39 million.[15] As the westward movement increased, so did demands for land. Consequently, over the next twenty-seven years fifteen more offices were opened in Colorado to help with the lease and disposal of the public domain.[16] These land offices were extensively used for varying periods and, as the lands became settled, the offices were gradually consolidated until today we are back to one land office which houses the records accumulated in all sixteen. And the accumulation is substantial. During the past hundred years of operations approximately 150 tract books containing nearly 50,000 pages and about 600 serial books containing 400,000 pages have been filled. There are nearly 6,000 township, townsite, and state boundary plats, about 2,000 segregation, connection, and protraction sheets, and over 33,000 mineral and homestead surveys. The patents for all lands in this state which have been transferred to private ownership have been microfilmed and affixed individually by page to aperture cards. They number well over 400,000 and are segregated by section, township, and range. That patent record has been augmented by about 500 rolls of microfilm which contain all of the patents issued throughout the United States from July 1, 1914, to March 25, 1954. These are in numerical sequence and cover 724,631 title transfers. Their value lies largely in ready identification of mineral reservations which commenced with the Act of July 17, 1914.[17]

II. LAND OFFICE RECORDS

The Land Office records are, of course, basic to effective operations by the Bureau of Land Management as well as the public. Unfortunately, time and hard usage have taken their toll as many of the records are badly deteriorated. Some are so tattered, torn, faded, and patched that parts are practically illegible. As to their documentary condition, there has been considerable variation with the Land Offices in the use of symbols, color codes, and abbrevia-

[12] GOVERNMENT PRINTING OFFICE, *Historical Highlights of Public Land Management*, p. 6.
[13] *Id.* at p. 7.
[14] *Id.* at p. 31.
[15] *Id.* at p. 33.
[16] Land Office records.
[17] 38 Stat. 509 (1914), 30 U.S.C. § 122 (1965).

tions. Uniformity in this respect has been largely lacking. Likewise, certain classes of entries are missing. In some of the earlier offices references to basic documents were sometimes incomplete. This was particularly true of withdrawals. Cross referencing, a helpful tool to abstractors, was likewise seldom employed. Consequently, the accuracy of some of these early records has been questioned. Such questions can, of course, only be resolved by recovery and analysis of the basic documents, a lengthy process at best.

Looking back over the Land Office records, it becomes apparent that oil shale, an energy resource commanding today's spotlight, was a prominent topic over two generations ago. It has been estimated that 30,000 oil shale placer claims have been placed of record in Colorado. While most are "paper" locations which have been abandoned or forgotten, it is believed that nearly 25 per cent are still sufficiently alive to present administrative problems. The contest docket indicates that over 2,000 contests were initiated against a vast number of these claims during the years past. These contests originated from private sources as well as the Government. The usual charges, when appropriate, included fraud, failure to do assessment work, lack of discovery, lack of monumentation, failure to post notices, and abandonment. As for those patent applicants who were successful, serial page entries indicate that 269 oil shale patents covering approximately 1,750 claims have been issued in the last 45 years. These patents cover 259,265 acres, roughly one-fifth of the oil shale lands. Other patents in the area, mostly agricultural, present a variety of reservations such as oil and gas, coal, uranium, nitrates, and, of course, oil shale.

With the increased interest in oil shale more and more individuals are coming to the Land Office for record information. Those who regularly research information, of course, have a minimum of difficulty in wending their way through the maze of records. Those who come infrequently, however, find the paths to their answers somewhat mysterious. It is to those in the second category that the following discourse is directed.

The Land Office records are based on the rectangular system of survey, and Colorado is represented by three meridians, the Sixth Principal, the New Mexico, and the Ute Meridian, in their order of size of area. The Sixth covers approximately three-fourths of the state, being the north and east portions. The New Mexico includes the remaining southwest part of the state, and the Ute, being quite small, includes but 14 townships along the Colorado River near Grand Junction.

The various plats of survey are identified as the original, supplemental, dependent, independent, mineral, homestead entry, town-

site, and segregation plats. The original includes the various sections and subdivisions of the township and shows courses and distances of the survey and monumentation on the ground. Certain topographic features such as water courses and terrain are generally shown. Supplemental plats are of larger scale. They generally include about a section and reflect changes from the original. Dependent resurvey plats are the result of dependent resurveys on the ground. All original monuments possible are recovered and remonumented. Courses and distances reflect the more recent measurements, and missing corners are replaced proportionately. An independent resurvey plat, the result of a completely new survey on the ground, does not necessarily follow the original monumentation. Prior authorized settlement and entry is monumented and identified by tract numbers.

The need for dependent and independent resurvey stems largely from inaccuracies of the early contract surveyors. Plats from these surveys seldom resemble the originals.

A mineral plat reflects the course of the vein or lode on which discovery was made, and generally does not lie in cardinal directions. Plats from homestead entry surveys are similarly oblique in that they generally follow a valley adjacent to or across a water course. Such are usually within National Forests and precede the subdivisional grid. Townsite plats indicate the lots, blocks, streets, and alleys of communities laid out under the townsite laws and regulations.

Specific mention should be made of the segregation sheets. As noted previously, 33,000 mineral plats have been prepared and are of record. Most of these plats fall within the earlier rectangular surveys. As the mineral plats describe lode claims which usually lie oblique to points of the compass, odd-shaped parcels of land are left which do not fit into the rectangular grid. In order properly to identify these parcels, plats showing a segregation of lots were drafted. In fact, 1,790 segregation sheets were prepared and placed in the records. Patents were issued using descriptions noted on these plats. Unfortunately, however, a substantial number of these segregation plats were neither officially approved nor accepted before appearing with the other plat records. Consequently, titles stemming from these plats are occasionally subject to question. This situation can only be cured by updating and securing official approval of the plat which was the source of the land description.

Oil and gas plats are also included in the plat books. These are only diagrammatic and are intended to show the identity and location by aliquot parts of sections of the oil and gas leases currently in effect. Plats identifying known geologic oil and gas structures are also included.

In summary, one can find in the plat books a system of identifying lands. This includes the location of meridians, the numbered townships, and range lines. The identification of patents by serial number and outboundary has generally been added by Land Office notation. In addition, certain plats contain marginal notations, either handwritten or typed on small sheets and posted to the plat. These notations, also added by Land Office personnel, are generally confined to classifications of either surface or subsurface, withdrawals, reservations, and restorations. Due to the differences of management in the various land offices, however, the added bits of information were not consistently noted.

As with the plat books, the tract books are first identified by the township north or south of the baseline. Range identification then follows in the book index which is always found on the counter in the public record room. Each tract book includes several townships with usually three sections to a double page. Subdivisional or lot description follows under each general section heading, along with the number of acres involved and the name of the applicant. This is followed by the date and type of entry, with closing information such as date of final certificate, date and number of the patent, or other final action.

The tract books also reflect the classification, withdrawal, reservation, and restoration actions, both as to surface and subsurface. When the entire township is affected, the notation precedes the information under Section 1. When the areas are more limited, the notations appear with the respective sections affected.

Briefly, the tract books summarize the various actions which have taken place on specific lands over the many years past. While most have been rebound, these books are quite old and reflect long, hard usage.

Each action initiated in a land office is given a serial numbered identification. This is noted to a serial page, along with the date, the description of the land affected, the number of acres involved, the name and address of the initiating party, the type of action, whether the case is an application, a classification or a withdrawal, and any other initial information if pertinent. As the action receives consideration and is processed toward conclusion, each subsequent step is noted to the serial page according to date. While the notations are brief and in summary form, they do give a chronological account of the entire procedure, whether it be adverse or favorable.

At this point it should be noted that each of the sixteen land offices in Colorado started out with entry No. 1 in the serial book system and followed in numerical sequence until consolidation with another office. The index books previously referred to as being on

the counter in the public room of the Land Office list the various offices with the years the office was open and the name of the office into which it was consolidated. Likewise, on the counter is an official map of Colorado showing the original land districts in addition to township identifications, county lines, cities, towns, and other pertinent information. By referring to both map and index, one can determine which serial book is required.

Frequently in the serial books one will find notice of contest action. Rules of practice under administrative procedures allow both private and Government contests. When this action is initiated, a contest number is assigned, and the same practice is followed as with serial pages. Each action taken in the contest is noted to the contest page in a summary manner, giving a chronological account of the entire procedure.

Also of value to the practitioner are an alphabetical index of all entries and the case files. These files, however, are not accessible to the public. If one has a name only, and desires a serial number, an attendant on duty will readily search for the information. If one wishes to review a file, and has proper authority to do so, the file, if available, will be produced at the inspection table. If the file is in the Federal Records Center or the National Archives, an order will be placed immediately, and the requesting party advised on its arrival.

These, then, are the eight main sources of record information: the state map showing the land districts and township identifications, the index books, the plat books, the tract books, the serial registers, the contest books, the alphabetical index, and the case files. In addition to these, it should be mentioned that the Land Office is staffed with personnel who are familiar with the records and are ready and willing to assist in search and interpretation. It is recognized that the knowledge and experience which make it possible for a person readily to determine reliable land status can be gained only in time.

III. PROCEDURE

In the light of the previous discussion, let us assume that a client wishes to patent an oil shale claim and comes to you with the problem. After you have obtained the legal description, the following is a step-by-step procedure:

The importance of title being paramount, you will first determine from the county records whether the claim has been properly recorded and that the chain of title is in order. Proof of possessory title is required with the patent application and is supplied through a certificate of title or abstract of title.

If title appears satisfactory, the first check in the Land Office will be with the counter index to determine, by description, the proper plat and tract books. From both of these books you will determine whether or not other claims, entries, classifications, or reservations might in any way conflict with the subject land. If a claim or an entry does appear on all or part of the land, it will be identified by serial number.

As our hypothetical claim is oil shale in character, it would be located somewhere in the Piceance Creek Basin. The counter index will show that the Glenwood Springs Land Office covered this area from 1884 to July 1, 1927. If the date on a conflicting entry in the tract book falls within these years, reference would then be directed to the Glenwood Springs series. If the date were after July 1, 1927, and prior to June 20, 1949, the counter index will show the entry in the Denver series. On the last-named date final consolidation was accomplished, and all subsequent serial numbers were then given our state prefix.

If the conflicting entry were a withdrawal or classification, such could be verified by the *Federal Register,* available through Land Office personnel assisting in the public room.

If the serial notations indicated a contest had been initiated against the conflicting entry, the contest number would be the key to further information in the contest books.

In this manner one can research the required status and advise his client accordingly.

IV. Additional Service

In closing, one additional service deserves particular mention. This is the Land Office library. Included in this library are a set of the U. S. Statutes at Large, the United States Code, the Gower Service, Bureau of Land Management decisions by date and category, bound Departmental decisions, Departmental Index-Digest of decisions and opinions, Colorado Revised Statutes, and the following publications of the Rocky Mountain Mineral Law Foundation: *Proceedings of the Institutes, Law of Federal Oil and Gas Leases,* and the *American Law of Mining.* The library also has available a wealth of other relevant reference material. This library is available for use of the public during regular office hours.

In brief, the Colorado Land Office is a repository of a vast quantity of lands and minerals records and documents which have been accumulating over the past 102 years. It is hoped that the foregoing will help to make this wealth of material more useful to those who become involved in the complexities of public land law.

Denver Law Journal

VOLUME 43 1966 NUMBER 1

Member, National Conference of Law Reviews

Casualty Losses

BY LAWRENCE J. LEE*

I. INTRODUCTION

In view of Colorado's recent flood experiences, it seeems appropriate to explore in some detail the taxpayer's burden of establishing a casualty loss for income tax purposes. Section 165 of the Internal Revenue Code of 1954 provides: "There shall be allowed as a deduction any loss sustained during the taxable year and not compensated for by insurance or otherwise." As a general proposition it would appear that the sole criterion in section 165 for a loss deduction is simply that the taxpayer suffer a loss. As to individuals, however, section 165(c) in addition requires that the loss must either (1) be incurred in a trade or business or in a transaction entered into for profit; or (2) arise from fire, storm, shipwreck, or other casualty or theft. In short, any loss arising from fire, storm or other casualty is allowable as a deduction under section 165(c) for the taxable year in which the loss is sustained,[1] and the loss is allowable whether or not it was incurred in connection with property used in a trade or business or held in a transaction entered into for profit.[2] This general rule, deceptively simple in statement, presents numerous problems in application.

II. CASUALTY DEFINED

A. *Introduction*

Although section 165(c)(3) of the Internal Revenue Code of 1954 suggests the definition of a casualty by including the illustrative events, "fire, storm, shipwreck, or other casualty," the regulations fail to expand on the code language and in the discussion

*Partner, Ireland, Stapleton, Pryor & Holmes, Denver, Colorado; member of Colorado, New York, and District of Columbia Bars; B.A., University of Illinois, 1955; LL.B., Cornell Law School, 1958; LL.M., Georgetown Law Center, 1960.

[1] It should be noted that an estate is required to deduct from the value of the gross estate losses incurred during the settlement of the estate arising from fires, storms, shipwrecks, or other casualties if the loss is not compensated for by insurance or otherwise. INT. REV. CODE of 1954 § 2054; Treas. Reg. § 20.2054.1 (1958). However, if the estate so elects and satisfies the requirements set forth in Treas. Reg. § 1.642(g)-1 (1956), the loss may be claimed under section 165(a) in computing the taxable income of the estate. Treas. Reg. § 1.165-7(c) (1960) as amended, T.D. 6786, 1965-1, CUM. BULL. 107.

[2] INT. REV. CODE of 1954 § 165(c)(3); Treas. Reg. § 1.165-7(a) (1960), as amended, T.D. 6786, 1965-1 CUM. BULL. 107.

actually presume an understanding of the term. However, the Internal Revenue Service in its pamphlet entitled *Disasters, Casualties and Thefts,*[3] gives the following definition of a casualty: "A casualty is the complete or partial destruction of property resulting from an identifiable event of a sudden unexpected, or unusual nature."

The pamphlet proceeds to list the following items as casualties: Damage from hurricane, tornado, flood, snow, storm, shipwreck, fire, or accident. With additional explanation, it also lists auto accident, mine cave-in, and sonic boom. By way of contrast the pamphlet states:

> Progressive deterioration through a steadily operating cause and damage from a normal process are not casualty losses. Thus, the steady weakening of a building caused by normal or usual wind and weather conditions is not a casualty loss.
>
> Since termite damage normally occurs over a fairly long period of time, a loss from such damage is not a casualty loss.
>
> Moth damage to property is not a casualty, and such loss is not deductible.

A similar definition was given in Rev. Rul. 59-102[4] which discussed the relationship between section 165 and section 1033:

> The term "casualty" denotes an accident, a mishap, some sudden invasion by a hostile agency; it excludes the progressive deterioration of property through a steadily operating cause. *Charles J. Fay v. Helvering,* 120 Fed. (2d) 253. Also, an accident or casualty proceeds from an unknown cause, or is an unusual effect of a known cause. Either may be said to occur by chance and unexpectedly. *Chicago, St. Louis & New Orleans Railroad Co. v. Pullman Southern Car Co.,* 139 U.S. 79.
>
> To be of the same nature or kind as fires, storms and shipwreck for purposes of section 165 (c) (3) of the code, an event must first be unexpected and, second, be identifiable as the cause of a provable loss. There must be a provable event which not only has a casual [*sic*] relation to the diminution in value of the damaged property but can be isolated from other events or sequences leading to changes in value in the damaged property. The primary significance of the latter requirement is that generally the amount of a casualty loss deduction is in part determined with reference to the value of the property before the casualty and its value immediately after the casualty so that it is necessary to fix a time at which the casualty took place.

A casualty may be the result of natural causes, *i.e.,* through the action of fire, wind, storm or the like, or may be the result of

---

[3] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES, AND THEFTS, p. 2 (March 1964).

[4] 1959-1 CUM. BULL. 200.

human intervention so long as the human action is one which would or should not be expected to produce the resultant loss.[5] The element of human intervention as giving rise to a casualty loss is illustrated by *Ray Durden*,[6] which involved damage to a residence from blasting in a nearby quarry. The residence was constructed in 1938 and occupied by December 7, 1938. During the period of construction and after occupancy, a series of quarry blastings took place and, though these blasts shook the house, they gave rise to no apparent damage. On January 20, 1939, a severe blast took place and thereafter the damage to petitioner's house became apparent. One issue confronting the court was whether the taxpayers sustained a loss arising from a casualty. The court held that the damage did result from a casualty, stating:

> Under the doctrine of *ejusdem generis*, it is necessary to define the word "casualty" in connection with the words "fires, storms, shipwreck" immediately preceding it. "Casualty" has been variously defined, including "an undesigned, sudden and unexpected event" — Webster's New International Dictionary; also as "an event due to some sudden unexpected or unusual cause" — *Matheson v. Commissioner*, 54 Fed. (2d) 537. The term "casualty" "excludes the progressive deterioration of property through a steady operating cause." *Fay v. Helvering*, 120 Fed. (2) 253; also, "an accident or casualty proceeds from an unknown cause or is an unusual effect of a known cause. Either may be said to occur by chance and unexpectedly." *Chicago, St. Louis & New Orleans Railroad Co. v. Pullman Southern Car Co.*, 139 U.S. 79. The blast causing the damage to the houses of petitioners was unusual, heavier than those occuring during the day by day blasting operations which had theretofore been carried on. The damage was not caused by any progressive deterioration of property. We conclude that it was caused by a casualty in the ordinary sense of the word. Whether under the application of the doctrine of *ejusdem generis* it was a casualty of the same general nature or kind, as "fires, storms, shipwreck," offers a somewhat more difficult question. However, it has been held, under section 23(e)(3), that an automobile wreck may be a casualty in closest analogy to shipwreck. *Shearer v. Anderson*, 16 Fed. (2) 995, and Regulations 103, section 19,23(e)-1, approves as a deductible item loss occasioned by damage to an automobile and resulting from the faulty driving of the taxpayer or another operating the automobile, or from the faulty driving of another automobile colliding with it. In *Anderson v. Commissioner*, 81 Fed. (2d) 457, it is held, under section 23 (e)(3), that losses arising from ordinary highway mishaps may be deducted even though caused by the negligence of the taxpayer. Conversely, losses sustained through the action of termites have

[5] Kipp v. Bingler, 64-2 USCT ¶ 9711 (W. D. Pa. 1964).

[6] 3 T.C. 1 (1944), *acq.* 1944 CUM. BULL. 8.

been held not to be deductible under the heading of casualty. *United States v. Rogers,* 120 Fed. (2d) 244; *Charles J. Fay,* 42 B.T.A. 206; *aff'd* 120 Fed. (2d) 753. It thus appears that a proper definition of the term casualty does not exclude the intervention of human agency, such as involved in setting off the blast involved in this case, and the prime element is that of suddenness as opposed to some gradually increasing result. The blast being considered here, though set off by human agency, was sudden and unusual in violence. The fact that ordinary blasts had been occurring, without complaint from the petitioners, from day to day, the fact that such ordinary blasts caused no damage and that much damage was caused by this particular blast, resulting in complaint by the petitioners, all indicate that the occurrance was unusual in its results.

B. *Events Constituting a Casualty*

The Tax Court and Federal courts treat various types of casualties in different ways; their disposition of the cases differ (1) in recognizing the losses and (2) in determining the amounts thereof. The following events (involving both natural causes and human intervention) have been held to constitute "casualties" within the meaning of section 165(c)(3): accident,[7] blasting,[8] bomb explo-

[7] See, *e.g.,* Samual Abrams, 23 CCH Tax Ct. Mem. 1546 (1964) (piece of furniture dropped 16 floors by movers while being moved from one apartmeent to another); I.T. 2231, IV-2 CUM. BULL. 53 (1925), *modified on other grounds,* G.C.M. 16255, XV-1 CUM. BULL. 115 (1936) (bursting of hot water boiler in residence caused by an air obstruction in the pipes which prevented the water from properly coming in contact with the boiler and flowing through the system); The Wellston Co., 24 CCH Tax Ct. Mem. 306 (1965) (collapse of roof due to faulty construction). An automobile owned by the taxpayer, whether used for business purposes or maintained for recreation or pleasure, may be the subject of a casualty loss, including losses caused by nature or the intervention of man. Treas. Reg. § 1.165-7(a)(3) (1960); Helvering v. Owens, 305 U.S. 468 (1939); Francis L. Davis, 9 CCH Tax Ct. Mem. 306 (1950); Nat Lewis, 13 CCH Tax Ct. Mem. 1167 (1954); G.C.M. 16255, XV-1 CUM. BULL. 115 (1936). Thus, a casualty loss occurs when an automobile owned by the taxpayer is damaged and when (1) the damage results from the faulty driving of the taxpayer or other person operating the automobile but is not due to the willful act or willful negligence of the taxpayer or one acting in his behalf; or (2) the damage results from the faulty driving of the operator of the vehicle with which the automobile of the taxpayer collides. Treas. Reg. § 1.165-7(a)(3) (1960). It makes no difference that the automobile was operated by an unauthorized person. Shearer v. Anderson, 16 F.2d 995 (2nd Cir. 1927). However, the taxpayer is not entitled to deduct as a casualty loss, damages (personal injury or property) including costs incident thereto paid to another for injury to the other party's property or person if the injury was not in connection with the taxpayer's trade or business. See cases cited, *infra* notes 49 and 52. However, the damages and costs are deductible if the vehicle was being operated in the ordinary course of a trade or business. Anderson v. Commissioner, 81 F.2d 457 (10th Cir. 1935); M. L. Rose Co., 13 CCH Tax Ct. Mem. 213 (1954), *but cf.* Freedman v. Commissioner, 301 F.2d 359 (5th Cir. 1962), *affirming* 35 T.C. 1179 (1961) (accident occurred while taxpayer was en route from his place of employment to a place of business in which he was a partner).

[8] Ray Durden, 3 T.C. 1 (1944, *acq.* 1944 CUM. BULL. 8 (damage to residence).

sions and bombardment,[9] damage in storage and transit,[10] damage to automobile mechanism, caused by child,[11] damage to septic tank and water line when lot was plowed,[12] drought,[13] earthquake,[14] fire,[15]

---

[9] I.T. 2037, III-1 CUM. BULL. 146 (1924), *modified* by I.T. 35119, 1941-2 CUM. BULL. 96 (home of the taxpayer damaged as the result of the explosion of a bomb placed on his front porch); I.T. 3519, *supra* (taxpayer lost certain personal property located in a residence which was destroyed in 1940 as a result of bombardment of a city in France).

[10] See, Latimore v. United States, 63-1 USCT ¶ 9845 (N.D. Calif. 1963) (art objects in storage either smashed, missing, soiled or crushed beyond restoration); Harry M. Leet, 14 CCH Tax Ct. Mem. 39 (1955), *aff'd* 230 F.2d 845 (6th Cir. 1956) (goods stolen and damaged in transit, loss denied because claimed in incorrect year); Leland D. Webb, 1 B.T.A. 759 (1925), *acq.* IV-1 CUM. BULL. 3 (1925) (personal property in transit aboard naval transport). *But cf.* Guy I. Rowe, 3 B.T.A. 1228 (1926); Bercaw v. Commissioner, 165 F.2d 521 (4th Cir. 1948), *affirming* 6 CCH Tax Ct. Mem. 27 (1947); Mildred Bauman, 10 CCH Tax Ct. Mem. 31 (1951).

[11] Hary M. Leet, 14 CCH Tax Ct. Mem. 39 (1955), *aff'd* 230 F.2d 845 (6th Cir. 1956) (taxpayer's auto did not have a mechanism which automatically disengaged the starter when the motor was running; a child pressed the starter button and damaged the starter).

[12] Harry M. Leet, 14 CCH Tax Ct. Mem. 39 (1955), *aff'd* 230 F.2d 845 (6th Cir. 1956).

[13] Winters v. United States, 58-1 USCT ¶ 9205 (N.D. Okla. 1958), *rev'd on other grounds* 261 F.2d 675 (10th Cir. 1958), *cert. denied* 359 U.S. 943 (1959) (damage to landscaping); Rev. Rul. 54-85, 1954-1 CUM BULL. 58 (damage to residential property — soil shrinkage during period of drought). *But cf.* Kemper v. Commissioner, 269 F.2d 184 (8th Cir. 1959), *affirming* 30 T.C. 546 (1958) (evidence was insufficient to establish the trees died of drought or any other casualty); Buttram v. Jones 87 F. Supp. 322 (W.D. Okla. 1943) (damage to landscaping loss denied for failure to show change in value); Louis Broido, 36 T.C. 786 (1961) (taxpayer failed to show a difference in value before and after the drought); Dick H. Woods, 19 CCH Tax Ct. Mem. 388 (1960) (damage to residence — soil settled causing foundation to crack — loss denied for failure to show loss in value); Rev. Rul. 55-367, 1955-1 CUM. BULL. 25 ("the drying up of a well resulting from prolonged lack of rain is not such an unusual or unexpected happening and involves no such sudden, identifiable event fixing a point at which a loss can be measured as to constitute a casualty loss. . . .").

[14] A.R.R. 4725, III-1 CUM. BULL. 143 (1924) (damage to plant).

[15] INT. REV. CODE of 1954 § 165(c)(3); see, United States v. Koshland, 208 F.2d 636 (9th Cir. 1953); Miree v. United States, 62-2 USCT ¶ 9756 (N.D. Ala. 1962) (apartment houses); Sears v. United States, 59-1 USCT ¶ 9302 (N.D. Ohio 1959); Virgil R. Williams, 19 CCH Tax Ct. Mem. 106 (1960) (warehouse, carpentry shop and hotel); Melvin Mailloux, 20 CCH Tax Ct. Mem. 942 (1961), *rev'd on other grounds,* 320 F.2d 60 (5th Cir. 1963) (household furnishings and equipment); Ticket Office Equipment Co., 20 T.C. 272 (1953), *acq.* 1953-2 CUM. BULL. 6 *aff'd per curiam on other grounds,* 213 F.2d 318 (2nd Cir. 1954) (Plant and contents including machinery, supplies and inventory items); Bernard L. Shackleford, 7 CCH Tax Ct. Mem. 694 (1948) (house and furnishings); J. H. Anderson, 7 CCH Tax Ct. Mem. 811 (1948) (house and furnishings); Lorraine Turpentine Co., 20 B.T.A. 423 (1930) (distillery); Fred Frazer, 10 B.T.A. 409 (1928) (apartment house); George B. Friend, 8 B.T.A. 712 (1927), *acq.* VII-2 CUM. BULL. 14 (1928).

flood,[16] freeze,[17] high waves,[18] hurricane,[19] lightning,[20] rain,[21] snow

[16] See, Ferguson v. Commissioner, 59 F.2d 893 (10th Cir. 1932), *reversing* 23 B.T.A. 364 (1931) (farmland flooded); Hutchings v. Glenn, 41-2 USTC ¶ 9673 (W.D. Ky. 1941) (architect's plans and drawing destroyed by flood); Smith, Trustee v. Commissioner, 19 F. Supp. 377 (D.N.H. 1937) (flood washed away bank necessitating repair to a penstock); Harris Hardwood Co., 8 T.C. 874 (1947), *acq.* on this issue, 1947-2 CUM. BULL. 2 (damage to plant used in manufacture of hardwood flooring); Doyle E. Collup, 21 CCH Tax Ct. Mem. 128 (1962) (inundation of lake front property including house); Frank R. Hinman, 12 CCH Tax Ct. Mem. 1347 (1953) (flash flood washing away top soil). *But see* J. G. Boswell Co., 34 T.C. 539 (1960) *aff'd* 302 F.2d 682 (9th Cir. 1962), *cert. denied* 371 U.S. 860 (1962); Citizens Bank of Weston v. Commissioner, 252 P.2d 425 (4th Cir. 1958) *affirming* 28 T.C. 717 (1957); Central Arizona Ranching Co., 23 CCH Tax Ct. Mem. 1304 (1964).

[17] United States v. Barret, 202 F.2d 804 (5th Cir. 1953) (destruction of landscaping; the case also involved the question of when the actual injury and hence the "loss" occurred); Ferris v. United States, 62-1 USTC ¶ 9448 (D. Vt. 1962) (unusual conditions of precipitation, freezing and thawing, and temperature caused garage wall to collapse); Stanley Kupiszewski, 223 CCH Tax Ct. Mem. 1559 (1965); Donald G. Graham, 35 T.C. 273 (1960), *acq.* 1961-2 CUM. BULL. 4 (destruction of exotic plants); Robert H. Montgomery, 6 CCH Tax Ct. Mem. 77 (1947) (destruction of rare and exotic palm trees); Seward City Mills, 44 B.T.A. 173 (1941), *acq.* 1941-1 CUM. BULL. 9 (ice jam on river damaged foundation of a mill); I.T. 3921, 1948-2 CUM. BULL. 32 (partial damage to trees held in trade or business); O.D. 1076, 5 CUM. BULL. 138 (1921) (damage to flooring and furniture caused by freezing and bursting of water pipes in a residence). *But cf.* Dean L. Phillips, 9 CCH Tax Ct. Mem. 501 (1950) (automobile motor frozen); Samuel Greenbaum, 8 B.T.A. 75 (1927) (a water pipe in the cellar froze and burst, causing a flood in the cellar; the court disallowed the deduction — "a frozen water pipe is a common occurrence").

[18] Ferst v. Edwards, 129 F. Supp. 606 (D. Ga. 1955) (beach home collapsed after sand was washed away); Rev. Rul. 53-79, 1953-1 CUM. BULL. 41 (physical damage to buildings, boathouses, docks, seawalls on Great Lakes as a result of their being battered by wave action). *But cf.* Edward W. Banigan, 10 CCH Tax Ct. Mem. 561 (1951) ("The alleged loss by damage to the automobile by salt water is not due to casualty. . . .").

[19] Biddle v. United States, 175 F. Supp. 203 (E.D. Pa. 1959) (damage to residential property); Graham M. Brush, 21 CCH Tax Ct. Mem. 649 (1962) (damage to residential property); Philip Allen, 1 CCH Tax Ct. Mem. 14 (1962) (damage to residential property); Jay W. Howard, 18 CCH Tax Ct. Mem. 413 (1959) (damage to residential landscaping); Western Products Co., 28 T.C. 1196 (1957), *acq.* 1958-1 CUM. BULL. 6 (damage to landscaping); Oceanic Apartments, Inc., 13 CCH Tax Ct. Mem. 944 (1954) (damage to resort hotel); Gilbert J. Kraus, 10 CCH Tax Ct. Mem. 1071 (1951) (damage to beach house); Carl A. Haslacher, 9 CCH Tax Ct. Mem. 314 (1950) (damage to residential landscaping); Isabelle B. Krome, 9 CCH Tax Ct. Mem. 178 (1950); Mary F. Cary, 7 CCH Tax Ct. Mem. 724 (1948) (damage to residential landscaping); G.C.M. 21013, 1939-1 CUM. BULL. 101 (damage to landscaping); I.T. 3304, 1939-2 CUM. BULL. 158 (damage to residence).

[20] S. F. Horn, 18 CCH Tax Ct. Mem. 177 (1959) (damage to trees); Harry M. Leet, 14 CCH Tax Ct. Mem. 39 (1955), *aff'd* 230 F.2d 845 (6th Cir. 1956) (damage to tree).

[21] Clapp v. Commissioner, 321 F.2d 12 (9th Cir. 1963), *affirming* 36 T.C. 905 (1961) (artificial beach washed away by unprecedented rain); Kipp v. Bingler, 64-2 USTC ¶ 9711 (W.D. Pa. 1964) (involving a mud slide); Schirmer v. United States, 59-2 USTC ¶ 9572 (N.D. Calif. 1959) (extraordinary rain caused soil slide); Delbert P. Hesler, 13 CCH Tax Ct. Mem. 972 (1954) (drought followed by unusual rainfall caused soil to subside and produce cracks in foundation); Clarence E. Stewart, 12 CCH Tax Ct. Mem. 921 (1953) (rain storm flooded basement); A. J. Coburn, 12 CCH Tax Ct. Mem. 275 (1953) (damage to residential property). *But cf.* Rupert Stuart, 20 CCH Tax Ct. Mem. 938 (1961) (mere presence of water damage is not sufficient to show that it was the result of a casualty).

and ice storm,[22] sonic boom,[23] squall,[24] sudden subsidence of soil, cave-in or slide,[25] thunderstorm,[26] vandalism,[27] wind (tornado).[28]

The following events (involving both natural causes and human intervention) have been held not to constitute "casualties" within the meaning of section 165(c)(3): damage caused by

---

[22] Whipple v. United States, 25 F.2d 520 (D. Mass. 1928); Mary Cheney Davis, 16 B.T.A. 65 (1929), *acq.* VIII-2 CUM. BULL. 13 (1929) (damage to landscaping); John S. Hall, 16 B.T.A. 71 (1929), *acq.* VIII-2 CUM. BULL. 21 (1929) (damage to landscaping). *But cf.* Paul E. Jackson, 13 CCH Tax Ct. Mem. 1175 (1954) (damage to residential and rental property).

[23] Rev. Rul. 60-329, 1960-2 CUM. BULL. 67 (compared to wind damage).

[24] Ralph Walton, 20 CCH Tax Ct. Mem. 653 (1961) (severe squall from Lake Erie — destruction of trees).

[25] Tank v. Commissioner, 270 F.2d 477 (6th Cir. 1959), *reversing* 29 T.C. 677 (1958) (damage to residence located on river bank due to subsidence of the bank caused apparently by dredging operations conducted in the river); Stowers v. United States, 169 F. Supp. 246 (S.D. Miss. 1958) (damage caused by slide or cave-in of a bluff upon which taxpayer's residence was situated which while it did not damage the house did block the access to the house); Harry Johnston Grant, 30 B.T.A. 1028 (1934), *acq.* XIII-2 CUM. BULL. 8 (1934) (surface began to sink when substratum "sticky clay or quick sand and clay" was set in motion); Rev. Rul. 57-524, 1957-2 CUM. BULL. 141 (damage to residence caused by a "mine cave," *i.e.,* the collapse of mine excavations beneath the surface). *But cf.* Kipp v. Bingler, 64-2 USTC ¶ 9711 (W.D. Pa. 1964); Daniel F. Ebbert, 9 B.T.A. 1402 (1928). See also, Delbert P. Hesler, 13 CCH Tax Ct. Mem. 972 (1954). *But see,* Schirmer v. United States, 59-2 USTC ¶ 9572 (N.D. Calif. 1959) (gradual erosion of soil by action of the wind or water is not a casualty); Texas and Pacific Ry. Co., 1 CCH Tax Ct. Mem. 863 (1943); I.T. 1567, II-1 CUM. BULL. 90 (1923); Rev. Rul. 53-79, 1953-1 CUM. BULL. 41.

[26] David W. Murray Jr., 212 CCH Tax Ct. Mem. 1302 (1961) (destruction of trees); Andrew A. Maduza, 20 CCH Tax Ct. Mem. 1302 (1961) (rain caused taxpayer's property to flood, destruction of trees and shrubs).

[27] Charles Gutwirth, 40 T.C. 666 (1963) (vandalism and theft in residence occupied by troops); Burrell E. Davis, 34 T.C. 586 (1960), *acq.* in result only, 1963-2 CUM. BULL. 4 (vandals broke into a house being constructed for petitioners and damaged certain new appliances owned by the petitioneers and placed by them on the premises). *But cf.* Edward W. Banigan, 10 CCH Tax Ct. Mem. 561 (1951) (damage by "small boys" to hot water heater, hen coop, fence, and platform trailer; the court holding "the law does not recognize loses due to vandalism nor can any of the losses be allowed under the casualty section").

[28] Barry v. United States, 175 F. Supp. 308 (W.D. Okla. 1958) (windstorm which blew away approximately 4 inches of top soil in 36 hours); David W. Murray Jr., 21 CCH Tax Ct. Mem. 7 (1962) (strong wind caused retaining wall to collapse); Louis A. Edwards, 19 CCH Tax Ct. Mem. 925 (1960) (damage to trees); Richard E. Stein, 14 CCH Tax Ct. Mem. 191 (1955) (destruction of a barn); William O. Lindley, 11 CCH Tax Ct. Mem. 355 (1952) (damage to trees and shrubbery on residential site); Rev. Rul. 53-79, 1953-1 CUM. BULL. 41 (damage to buildings, boathouses, docks, seawalls, etc. on the Great Lakes as a result of their being battered by wind). *But cf.* Maude T. Fearing, 21 CCH Tax Ct. Mem. 800 (1962), *aff'd on other grounds,* 315 F.2d 495 (8th Cir. 1963) (destruction of tree and water damage but taxpayer failed to show difference in market values before and after the wind storm); Philip Handelman, 20 CCH Tax Ct. Mem. 878 (1961) (destruction of yacht sails but failure to prove cost or whether loss was compensated by insurance).

household pets,[29] damage done by moths or rodents,[30] death of livestock from disease, or old age,[31] dismissal from employment,[32] insect damage to and disease of trees and plants,[33] ordinary wear and tear or usual deterioration from use and age,[34] property lost or misplaced,[35] routine breakage of household or personal items,[36]

---

[29] J. Raymond Dyer, 20 CCH Tax Ct. Mem. 705 (1961) ("the breakage of ordinary household equipment such as china or glassware through negligence of handling or by a family pet is not a 'casualty loss' under section 165(c)(3) in our opinion." The fact that "the breakage of the vase was not occasioned by the cat's ordinary perambulations on the top of the particular piece of furniture, but by its extraordinary behavior there in the course of having its first fit" makes no difference).

[30] Edward W. Banigan, 10 CCH Tax Ct. Mem. 561 (1951) (rats); Rev. Rul. 55-327, 1955-1 CUM. BULL. 25 (moths).

[31] Rev. Rul. 61-216, 1961-2 CUM. BULL. 134; I.T. 3696, 1944 CUM. BULL. 241, modified by Rev. Rul. 59-102, 1959-1 CUM. BULL. 200; see INT. REV. CODE of 1954 § 1033(e); Treas. Reg. § 1.1033(e)-1 (1957); INT. REV. CODE of 1954 § 1231; Treas. Reg. § 1.1231-1(e) (1957).

[32] Evelyn R. Marks, 22 CCH Tax Ct. Mem. 1128 (1963) (dismissal as a teacher and loss of unused sabbatical and sick leave).

[33] Appleman v. United States, 338 F.2d 729 (7th Cir. 1964), *cert. denied*, 380 U.S. 956 (1965); Burns v. United States, 174 F. Supp. 203 (N.D. Ohio 1959), *aff'd per curiam*, 284 F.2d 436 (6th Cir. 1960); Internal Revenue Service Field Release No. 56, 5 CCH 1957 STAND. FED. TAX REP. ¶ 6668; Rev. Rul. 57-599, 1957-2 CUM. BULL. 142. See also, Matheson v. Commissioner, 54 F.2d 537 (2nd Cir. 1931), *affirming* 18 B.T.A. 674 (1930), *acq.* IX-2 CUM. BULL. 38 (1930) (pilings exposed by action of storms and eaten by worms). The rule may be different with respect to timber held in a trade or business. Orono Pulp & Paper Co. v. United States, 34 F.2d 714 (D. Me. 1929) (damage to pulp wood timber over a two-year period by spruce bud worm); Oregon Mesabi Corporation, 39 B.T.A. 1033 (1939) *acq.* 1944 CUM. BULL. 22.

[34] Clinton H. Mitchell, 42 T.C. 953 (1964) (tire blow-outs caused by overloading a trailer); Charlie L. Wilson, 22 CCH Tax Ct. Mem. 914 (1963) (casualty loss claimed for two automobile tires and damages to interior of home caused by leaky roof); Emil A. Wold, 22 CCH Tax Ct. Mem. 732 (1963) (breakdown of automobile engine); Henry W. Rice, 15 CCH Tax Ct. Mem. 1350 (1956) (engine ruined due to break in oil line of automobile which permitted all the oil to escape); Harry M. Leet, 14 CCH Tax Ct. Mem. 39 (1955), *aff'd* 230 P.2d 845 (6th Cir. 1956) (damage to fuel pump and muffler allegedly "sustained from flying stones while driving over the temporary road. . . .").

[35] Keenan v. Bowers, 91 F. Supp. 771 (E.D.S.C. 1950) (ring accidentally flushed down toilet); O.D. 526, 2 CUM. BULL. 130 (1920); Emily Marx, 13 T.C. 1099 (1949), *acq.* 1950-1 CUM. BULL. 3; Edgar F. Stevens, 6 CCH Tax Ct. Mem. 805 (1947) (ring lost while hunting). *Cf.* William Fuerst, 10 CCH Tax Ct. Mem. 208 (1951) (diamond bracelet apparently misplaced rather than stolen).

[36] J. Raymond Dyer, 20 CCH Tax Ct. Mem. 705 (1961) (vase broken by cat); Robert M. Diggs, 18 CCH Tax Ct. Mem. 443 (1959), *aff'd* 281 F.2d 326 (2nd Cir. 1960), *cert. denied* 364 U.S. 908 (1960) (glassware and china" . . . accidentally broken in the course of ordinary handling, by domestic help in the course of cleaning or by the family cat."); E. M. Taylor, 11 CCH Tax Ct. Mem. 651 (1952) ("During the calendar year 1948 he dropped his watch on the sidewalk in front of his home and expended $8.50 as the cost of repair. . . . It clearly does not constitute a casualty loss. . . ."); Willard I. Thompson, 15 T.C. 609 (1950) *acq.* this issue, 1951-1 CUM. BULL. 3, *rev'd on other grounds*, 193 F.2d 586 (10th Cir. 1951) ("As to the breakage of watch: This was a personal expense and the breakage does not partake of the nature of fire, storm, or shipwreck. . . ."); Charles J. Voigt, 8 CCH Tax Ct. Mem. 662 (broken glasses).

seizure of nonbusiness property by Police or other government officers,[37] termite,[38] and dry rot damage.[39]

---

[37] Charles K. Richter, 24 CCH Tax Ct. Mem. 461 (1965); William J. Powers, 36 T.C. 1191 (1961) (seizure of automobile by officials in East Germany); A. Gilbert Formel, 9 CCH Tax Ct. Mem. 782 (1950) ("The loss of money through seizure by the customs officers of a foreign country in the course of their execution of their official duties is not a loss from a casualty. . . . Again, even if the seizure were an illegal seizure . . . that is not a 'casualty' within the meaning of the statutory provision."); Thomas F. Gurry, 27 B.T.A. 1237 (1933) (fee paid to attorney for services rendered in recovering award compensating taxpayer for seizure of private automobile during WWI); Fred J. Hughes, 1 B.T.A. 944 (1925) (seizure of private stock of liquors by police officers); I.T. 4086, 1952-1 CUM. BULL. 29; Rev. Rul. 62-197, 1962-2 CUM. BULL. 66. A special exception to the above rule applies in cases of losses arising from confiscation of property by the Cuban government (any political subdivision thereof, or any agency or instrumentality of the government). INT. REV. CODE OF 1954 § 165(i)(1)(A) (1964); The Revenue Act of 1964, § 238, 78 Stat. 19. The loss is treated as a casualty loss, INT. REV. CODE of 1954 § 165(i)(1), but applies only to property (1) not used in a trade or business; and (2) not held for the production of income. INT. REV. CODE of 1954 § 165(i)(1)(B). Business property is governed by the general rules under section 165(i). The following requisites must be satisfied before the loss may be deducted: (1) the taxpayer claiming the loss must have been a citizen of the United States or resident alien, on December 31, 1958; (2) seizure must have taken place before January 1, 1964; (3) if the property involved is *tangible,* it must have been held and been located in Cuba on December 31, 1958. INT. REV. CODE of 1954 § 165(i)(1)(A)-(B). In connection with (3), *intangible* property may have been acquired after December 31, 1958. Thus, the special relief provided does not apply to: (1) business property; (2) tangible personal property acquired after December 31, 1958, and (3) losses incurred after December 31, 1963, or before December 31, 1958. The loss is deemed to have occurred on October 14, 1960, unless it is established that the loss was sustained on some other day. INT. REV. CODE of 1954 § 165(i)(2)(A). In determining the amount of loss, the fair market value of property held by the taxpayer on December 31, 1958, is treated as the market value of the seized asset regardless of the date when the expropriation actually took place. Intangible property acquired after December 31, 1958, the date of taking, is used for value purposes. INT. REV. CODE of 1954 § 165(i)(2)(B). Regardless of the time limits applicable generally to refund claims, a refund or credit of any overpayment attributable to a certain confiscation loss may be made as allowed if the claim is made before January 1, 1965. No interest is allowed on any refund or credit for any period from February 26, 1964. INT. REV. CODE of 1954 § 165(i)(3). See Rev. Rul. 65-87, 1965-1, CUM. BULL. 111 (repossession of household furniture because of default on the loan is not a casualty); Aaron F. Vance, 36 T.C. 547 (1961).

[38] United States v. Rogers, 120 F.2d 244 (9th Cir. 1941); Fleinstein v. United States, 173 F. Supp. 893 (E.D. Mo. 1954); Leslie C. Dodge, 25 T.C. 1022 (1956):

> It is thus seen that the weight of authority is to the effect that generally, termite damages does not give rise to a deductible casualty loss. This is for the reason that it does not occur suddenly, unexpectedly or from an unusual cause; it is rather in the nature of a gradual erosion or deterioration of property.

Charles J. Fay, 42 B.T.A. 206 (1940), *aff'd* per curiam, 120 F.2d 253 (2nd Cir. 1941); Rogers v. United States, *supra.* Only in exceptional cases where the invasion and measurable damage have occurred within a relatively short period of time has the loss been held deductible as a casualty loss. Rosenberg v. Commissioner, 198 F.2d 46 (8th Cir. 1952); Shopmaker v. United States, 119 F. Supp. 705 (E.D. Mo. 1953); Rev. Rul. 63-232, 1963-2 CUM. BULL. 97. For taxable years beginning after November 12, 1963, the Internal Revenue Service will disallow casualty loss deductions for any termite damage — "fast" termite damage not excepted. Rev. Rul. 63-232, *supra.* For taxable years beginning prior to November 12, 1963, a casualty loss deduction will be allowed by the Internal Revenue Service only in those situations where the damage caused by he termites extended over a period of 15 months or less. Rev. Rul. 59-277, 1959-2 CUM. BULL. 73 (*revoked by* Rev. Rul. 63-232, *supra.*) Rosenberg v. Commissioner, 198 F.2d 46 (8th Cir. 1952), *reversing* 16 T.C. 1360 (1951) (house inspected in April 1946 and found free of termites, termite damage discovered in April 1947); Shopmaker v. United States, 119 F. Supp. 705 (E.D. Mo. 1953) (house inspected in December 1949, termites discovered on February 8, 1951, the court treating the invasion or swarming of the termites as the casualty event); Buist v. United States, 164 F. Supp. 218 (E.D.S.C. 1958)

(summer cottage inspected and found free of termites in September 1953, termite damage discovered in June 1954); E. G. Kilroe, 32 T.C. 1304 (1959), *acq.* 1960-1 CUM. BULL. 4 (house inspected by bank in May 1953, thereafter by exterminating company on January 9, 1954, and January 19, 1955, the court stating:

> Bearing in mind the fact that an inspection had been made in 1953 when the house was purchased and that annual inspections were made on the premises each year thereafter, the last having been made in January 1955 — about 3 months before the discovery of the termite damage in question — plus the fact that there had been no exterior evidence of termite activity and that there were 'fresh channels' in the kitchen wall and floor, we are persuaded that the time within which the damage or loss occurred was within a relatively short time prior to discovery in 1955. From the record as a whole, we conclude that there was not termite activity in petitioners' house between May 1953 and January 1955, and that the petitioners are entitled to a casualty loss deduction for the damage in question.

Henry F. Cate, Jr., 21 CCH Tax Ct. Mem. 1146 (1962) (infestation existed for approximately six months); Allan M. Winsor, 18 CCH Tax Ct. Mem. 383 (1959), *aff'd* 278 F.2d 634 (1st Cir. 1960) (damage in the house had taken place in about a year and a half). No deduction is or was allowable for any year where the termite infestation and subsequent damage occurred over periods of several years. Rev. Rul. 59-277, *supra* (*revoked by* Rev. Rul. 63-232). Although the Internal Revenue Service has changed its position, there is no indication that the courts will not permit the deduction for a casualty loss arising from damage caused by the "fast termite." See Leslie C. Dodge, 25 T.C. 1022 (1956); E. G. Kilroe, 32 T.C. 1304 (1959), *acq.* 1960-1 CUM. BULL. 4; Hale v. Welch, 38 F. Supp. 754 (D. Mass. 1941).

[39] United States v. Rogers, 120 F.2d 244 (9th Cir. 1941); Rudolf L. Hoppe, 42 T.C. 820 (1964):

> Section 165(c)(3) speaks of losses arsing from "fire, storm, shipwreck, or other casualty . . . ." And the term "casualty" has been interpreted to mean "an accident, a mishap, some sudden invasion by a hostile agency; it exludes the progressive deterioration of property through a steadily operating cause." Fay v. Helvering, 120 F.2d 253 (C. A. 2); United States v. Rogers, 120 F.2d 244, 246 122 F.2d 485 (C. A. 9); Matheson v. Commissioner, 54 F.2d 537, 539 (C. A. 2); Leslie C. Dodge, 25 T. C. 1022, 1026. Thus, the foregoing cases have denied deductions for losses due to such causes as termites, dry rot, and rust.
>
> An exception to this rule appears to have developed in recent years in the case of the "fast termite," where it has been held that termite damage may qualify as a casualty loss if it occurs within a realtively short period of time. Rosenberg v. Commissioner, 198 F.2d 46 (C. A. 8); Joseph Shopmaker v. United States, 164 F. Supp. 218 (E.D.S.C.). And this Court has undertaken to follow this line of cases in E. G. Kilroe, 32 T. C. 1304, 1306, 1307 (1959) stating that the "term 'suddenness' is comparative, and gives rise to an issue of fact," noting that the claimed deductions for termite losses were disallowed in some cases while allowed in others.
>
> The alleged casualty before us involves dry rot rather than termites, but we do not understand either of the parties to suggest that anything here turns upon this difference. Accordingly, the question before us under Kilroe is the factual one whether the dry rot discovered in petitioners' house in November 1959 was of comparatively recent origin so as to qualify for the requisite degree of "suddenness." Petitioners' position in substance is that the fungus infestation began as the result of the unusually heavy rains in January, February, March and April of 1958; that the ensuing damage occurred over the following period of some 18 to 22 months; and that such period is sufficiently short to justify classifying the loss as characterized by the necessary "suddenness" to qualify as a "casualty."
>
> We might well hesitate to say that a period of some three months that we approved in Kilroe may be expanded to some 18 to 22 months without subjecting the whole theory of "comparative suddenness" to a reductio ad absurdum, but we do not reach that point because we cannot find that the dry rot in question had its beginning at the time of those rains in the first part of 1958 rather than at some substantially earlier date. Petitioners' contention that the fungus infestation began with those rains is based upon the assumption that their house was free of dry rot after the September 1956 inspection and repair of the property as recommended in the inspection report. Although we had the impression at the time of the trial that there might be a basis for that assumption, a careful study of the record has satisfied us that the assumption is without foundation.

C. *Burden of Proof*

The above list of casualty events is an "open end" list, *i.e.,* other events may constitute casualties within the meaning of section 165(c)(3) if the taxpayer can demonstrate an identifiable event (act of man or nature) which was sudden, unexpected or of an unusual nature. Of course, the taxpayer may lose the deduction, even if the identifiable event is one well established within the casualty class, if he fails to show the other requisites, *i.e.,* the sudden, unexpected or unusual nature[40] of the event.

III. Necessity of Actual Loss in Value

As with any claimed loss, the taxpayer must have actually parted with something of value, the loss of which was not only the result of actual physical damage to his property but also a loss in value which can be measured with reasonable accuracy.

Cast in terms of negligence law, the taxable event is a combination of a "trauma" (actual physical damage to taxpayer's property) resulting from a "cause" (storm, fire, collision, etc.) which was the "probable" cause of the damage.[41]

In short, there must be an event (the casualty) which directly culminates in actual physical damage, *i.e.,* a loss which is both immediate and measurable.[42] Thus a prospective loss or an economic loss without actual physical damage is not sufficient for tax pur-

---

[40] Kipp v. Bingler, 64-2 USTC ¶ 9711 (W.D. Pa. 1964) (failure to show that a slide was caused by rain storm and not excavation); Clyde v. Jackson, 24 CCH Tax Ct. Mem. 309 (1965); Rudolph L. Hoppe, 42 T.C. 820 (1964) (failure to show that dry rot occurred with sufficient suddenness to qualify as a casualty loss); Jane V. Elliott, 40 T.C. 304 (1963), *acq.* 1964-1 INT. REV. BULL. 5; Maude T. Fearing, 21 CCH Tax Ct. Mem. 800 (1962), *aff'd on other grounds,* 315 F.2d 495 (8th Cir. 1963); Rupert Stuart, 20 CCH Tax Ct. Mem. 938 (1961) (water damage shown, but failed to show evidence of a sudden or destructive force, or an identifiable event in the nature of a casualty); Henry M. Leet, 14 CCH Tax Ct. Mem. 39 (1955), *aff'd* 230 F.2d 845 (6th Cir.1956).

[41] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 3 (March 1964): "The reduction in value of property because it is in or near a disaster area and there is the possibility that the area might again have a similar disaster is not a casualty loss. A loss is allowed only for the actual physical damage to your property resulting from the casualty." See Kemper v. Commissioner, 269 F.2d 184 (8th Cir. 1959), *affirming* 30 T.C. 546 (1958). Actual damage does not include a "reserve" for repairs; James I. Goski, 24 CCH Tax Ct. Mem. 828 (1965). The damage or loss must be the immediate and direct result of the casualty, *i.e.,* a result directly connected with and following the casualty event. For example, a loss resulting from the sale of a taxpayer's residence to a conservancy district under condemnation proceedings, was not deductible as a casualty loss although the district was created as part of a flood prevention program initiated because of a flood in the area. II-1 CUM. BULL. 92 (1923). Philip Allen, 1 CCH Tax Ct. Mem. 14 (1942). *But cf.* INT. REV. CODE § 1033(f) and Treas. Reg. § 1.1033(f)-1 dealing with the sale or exchange of livestock solely on account of drought.

[42] The casualty event is the identifiable event fixing the onset of the damage and the physical injury closes the transaction. See Ferguson v. Commissioner, 59 F.2d 893 (10th Cir. 1932); Louis Broido, 36 T.C. 786 (1961); J. G. Boswell Co., 34 T.C. 539 (1960), *aff'd* 302 F.2d 682 (9th Cir. 1962), *cert. denied* 371 U.S. 860 (1962).

poses. For example, although the taxpayer's farm land was in fact flooded, no loss deduction was allowed for an alleged loss due to a reduction in cotton "history," *i.e.,* the possibility that the taxpayer might suffer a reduction in his acreage allotment for the planting of supported cotten due to his inability to plant cotton while the land was flooded. Since there in fact had been no reduction of the acreage in the year the loss was claimed, the loss was at best speculative and prospective.[43]

In *Leonard J. Jenard,*[44] involving the destruction of a taxpayer's residence by fire, the taxpayer claimed he was entitled to a loss deduction of $13,622.60 — an amount achieved by subtracting from the amount of the alleged difference in the fair market value of the residence before and after the fire ($32,000) the insurance recovery of $18,377.40. Although it was stipulated as a fact that a contractor engaged by the taxpayer restored the building to its condition immediately before the fire (at a cost of $23,782.47) the taxpayer, nevertheless, maintained that he suffered a loss by reason of the fire which was more than the cost of restoring the house to the condition it was in before the fire. This additional loss was based upon the argument that:

> [A] burned building suffers a loss in market value, over and above the cost of restoring it to its condition before the fire; . . . a loss of value results because a prospective buyer in the market for a house would, upon learning of the fire, fear that there may have been latent structural weaknesses caused by the fire which were not repaired; and, therefore, the very occurrence of the fire serves

---

[43] Central Arizona Ranching Co., 23 CCH Tax Ct. Mem. 1304 (1964); J. G. Boswell Co., 34 T.C. 539 (1960), *aff'd* 302 F.2d 682 (9th Cir. 1962), *cert. denied* 371 U.S. 860 (1962).

[44] Leonard J. Jenard, 20 CCH Tax Ct. Mem. 346 (1961). See also Clarence A. Peterson, 30 T.C. 660 (1958), *appeal dismissed,* involving a claimed casualty loss arising from rainstorms. The Court noted:

> Each of petitioners' expert witnesses was of the opinion that immediately preceding the rainstorm here involved, the fair market value of the petitioner's property was equal to its cost to that time, or $87,053. One of the witnesses was of the opinion that the fair market value of the property immediately after the rainstorm was between $50,000 and $60,000 and the other thought such value was approximately $65,000. The foregoing opinions were based in part on the amount of physical damage to the property and in part on what the witnesses considered would have been an almost complete lack of prospective purchasers for or demand for the property. Neither of the witnesses stated the portion of the decline in value testified to by him which he attributed to physical damage or the portion which he attributed to lack of demand. Each of the witnesses expressed the opinion that petitioners' property has returned to the value it had immediately prior to the rainstorm and one of them was of the opinion that it had returned to that value by March 1954.
>
> From the foregoing we think it is apparent that petitioners in claiming a loss of $25,000 are not only seeking a deduction on account of the physical damage to the property but also are seeking a deduction for a fluctuation in the value of the property which they have continued to own and which they have continued to occupy as a residence since March 1, 1952.

to decrease the fair market value in an amount in excess of repair costs.

While the Tax Court did allow a deduction of $5,405.07 difference between the cost of repair ($23,782.47) and the insurance recovery ($18,377.40), it rejected any contention that a loss resulted from the prospect that potential purchasers might discount the value of the house because of the fire, stating:

> Ascertaining the fair market value before and after the fire is merely the tool used for measuring the extent of the casualty loss. When the property suffers a repairable loss, the loss is measured by the difference between the fair market value immediately befor the fire and the fair market value immediately after the fire in its partially damaged state. Obviously, the fair market value of such property in its damaged state amounts to no more than an estimate or determination of what it will cost to repair the damage and restore it to its former condition and subtracting that sum from the fair market value before the fire. Here that sum is stipulated and now allowed as the extent of petitioner's casualty loss. He is not entitled to more because the property must bear the stigma of having once been damaged by fire, and this fact alone might make prospective future purchaser wary of buying. Fair market value is determined by elements of value that inhere in the property and not the groundless fears of prospective buyers.
>
> A complete answer to petitioner's contention is found in that portion of the statute excluding losses covered by insurance. Clearly a taxpayer whose casualty damaged property is restored to its prior condition by insurance funds, suffers no deductible loss under the statute. And yet the full force of petitioner's argument here would mean that if he had insurance coverage that paid the entire repair bill for restoring the property to its former state, in the sum of $23,782.47, he would still have a casualty loss in the sum of $8,217.53. That the statute intended no deducation for a fully insured casualty loss is too clear for argument.

Based on the same theory the IRS, In *I.T. 1567*,[45] refused to allow a deduction because of a loss allegedly sustained through depreciation in the value of a residence situated adjacent to the sea on account of the action of the sea on such property during storms.

---

[45] II-1 CUM. BULL. 90 (1923); See also Frank P. Kendall, 17 CCH Tax Ct. Mem. 809 (1958) (wherein the taxpayer claimed a casualty loss in the amount of the difference betwen what he believed the beach cottage was worth and the amount he received from its sale alleging that a storm in that year frightened away prospective purchasers). The Court in denying the loss stated:

> . . . even if we assume, *arguendo*, a loss in the fair market value of the property occurring in 1953, the record affirmatively indicates that such a loss in value was not the result of physical damage caused by a storm or storms in that year but was the result of fear on the part of prospective buyers of damages that might be sustained in future years as a result of storms, contemplated as possible and even probable, but which had not yet occurred and which might never occur. Obviously such a fear on the part of prospective buyers was not caused by a history of storm damages extending over a period of several, and probably many, years.

But cf. Bank of American Nat'l Tr. & Savings Ass'n Exr. v. United States 51-1 USTC ¶ 9110 (S.D. Calif. 1950).

The IRS noted that the taxpayer had not been compelled to spend any money in repairing the damage done by the storms and that it had not been necessary to move the residence on account of its exposure to the action of the sea and ruled that the alleged loss was only conjectural or indeterminable and did not represent a closed and completed transaction.

Similarly in *Citizens Bank of Weston v. Commissioner*,[46] the taxpayer was denied a casualty loss deduction for the value of basement storage space which the bank claimed had lost its usefulness due to the history of floods and the threat of future floods in the area. The court found that the flood had not materially altered the physical condition of the basement and that, although the bank officers had testified that the bank had permanently abandoned the basement, it still retained dominion over the basement and could, upon future reconsideration, again use the space.[47]

Finally, not only must there be an event which results directly in actual physical damage, but the damage must be to property belonging to the taxpayer. For example, a shareholder is not entitled to claim the casualty loss resulting to property owned by the corporation even though the shareholder is assessed by the corporation for the cost of repairs.[48] Nor is the taxpayer entitled to deduct as a casualty loss damages paid to another for injury to the other party's property or person unless the damage resulted from an accident arising in the course of business.[49] Thus, where the taxpayer is involved in an accident not arising in the course of business, he is entitled to claim only his damage as a casualty loss and he may

---

[46] Citizens Bank of Weston v. Commissioner, 252 F.2d 425 (4th Cir. 1958), *affirming* 28 T.C. 717 (1957).

[47] The Court of Appeals recited the following with respect to the Tax Court's holding, Citizens Bank of Weston v. Commissioner, 252 F.2d 425, 427 (4th Cir. 1958):

> The Tax Court held that the fear of a future loss furnishes no basis for a current deduction; and even if such fear diminished the market value — a fact not found by the Tax Court — this would be a mere fluctuation, for which no deduction may be made until a loss is actually realized by the sale or other disposition of the property.

[48] West v. United States, 163 F. Supp. 739 (E.D. Pa. 1958), *aff'd* per curiam, 259 F.2d 704 (3rd Cir. 1958); Earl S. Orr, 19 CCH Tax Ct. Mem. 789 (1960); Estate of Myrtle P. Dodge, 20 CCH Tax Ct. Mem. 1811 (1961) (taxpayer sold the property in 1956 to one Link who apparently rented it to one Recupero who severely damaged the building and stole some of the fixtures; taxpayer discovered the abandonment in December 1957 but did not foreclose until sometime in 1958; *held*, taxpayer "offered no satisfactory evidence that he actually owned the premises in 1957." Thomas J. Draper, 15 T.C. 135 (1950) (parents not entitled to claim a casualty loss for the destruction by fire of clothing belonging to an adult daughter although the daughter was still being supported by the parents.).

[49] Stern v. Carey, 119 F. Supp. 488 (N.D. Ohio 1953); C. W. Stoll, CCH Tax Ct. Mem. 731 (1946); Luther Ely Smith, 3 T.C. 696 (1944) *acq.* this issue, 1944 CUM. BULL. 26 (amount paid to library for damage to book inadvertently left on a bus); B. M. Peyton, 10 B.T.A. 1129 (1928); Samuel E. Mulholland, 16 B.T.A. 1331 (1929); L. Oransky, 1 B.T.A. 1239 (1925). See, 4 CUM. BULL. 159 (1921) indicating that the costs expended in defending a damage suit are not deductible as a casualty loss.

not deduct any amount paid to the other party involved by way of settlement or on a judgment.

A life tenant is entitled to deduct the full amount of the casualty loss (not merely that portion of the loss theoretically attributable to the life interest) for injury to property subject to the life estate.[50] In a lease situation, the party bearing the risk of the loss is entitled to the deduction.[51] Thus, if the lessee is bound by a covenant in the lease to restore and replace the leased buildings if they are destroyed, or if he is required to surrender the property to the lessor upon expiration of the lease "in as good order and condition as reasonable use and wear thereof will permit," then the risk is upon the lessee and he will be allowed the deduction.[52] If, on the other hand, the lessee is under no obligation to repair the damage or to make replacements, then the lessee is not entitled to deduct the full amount of the loss. In this case, since the casualty loss affects the value of both the lessee's interest and the lessor's reversion, the loss must be apportioned between them.[53] Similarly, a taxpayer committed to bear the risk of loss by a contract to purchase property is entitled to the casualty loss deduction.[54]

IV. Amount of Casualty Loss

A. *Introduction*

The discussion which follows sets forth the rules applicable to computing the amount of the loss. As in the preponderance of tax matters, the amount of loss is a question of proof. In short, a taxpayer seeking a casualty loss deduction must establish three facts: (1) that he suffered a loss, (2) the amount of the loss,[55] and (3) that his loss was caused by a "casualty."

---

[50] Bliss v. Commissioner, 256 F.2d 533 (2nd Cir. 1958), 27 T.C. 770 (1957); Lena L. Steinert, 33 T.C. 447 (1959), *acq.* 1960-1 CUM. BULL. 6; INT. REV. CODE of 1954 § 611(b)(2).

[51] See generally, Camp Wolters Land Co. v. Commissioner, 160 F.2d 84 (5th Cir. 1947), *reversing* on this issue, 5 T.C. 336 (1945), *acq.* 1945 CUM. BULL. 2.

[52] I.T. 2150, IV-1 CUM. BULL. 147 (1925); I.T. 3850, 1947-1 CUM. BULL. 20.

[53] Bonney v. Commissioner, 247 F.2d 237 (2nd Cir. 1957), *affirming* 24 T.C. 199 (1955), *acq.* 1956-2 CUM. BULL. 5, *cert. denied* 355 U.S. 923 (1957).

[54] Collins v. United States, 193 F. Supp. 602 (D. Mass. 1961), *aff'd and rev'd on other grounds,* 300 F.2d 821 (1st Cir. 1962), 303 F.2d 142 (1st Cir. 1962).

[55] Buttram v. Jones, 87 F. Supp. 322 (W.D. Okla. 1943); Leonard P. Tomlinson, 22 CCH Tax Ct. Mem. 662 (1963) (auto accident, taxpayer only produced a check issued for auto body work which was in an amount less than the claimed loss and was dated prior to the date of the accident); William S. Herreshoff, 22 CCH Tax Ct. Mem. 667 (1963); Jane U. Elliott, 40 T.C. 304 (1963), *acq.* 1964-2 CUM. BULL. 5; Maude T. Fearing, 21 CCH Tax Ct. Mem. 800 (1962), *aff'd on other grounds,* 315 F.2d 495 (8th Cir. 1963); Oceanic Apartments, Inc., 13 CCH Tax Ct. Mem. 944 (1954); Estate of R. D. McDaniel, 20 CCH Tax Ct. Mem. 1551 (1961); Benjamin J. Checkoway, 19 CCH Tax Ct. Mem. 1174 (1960); Paul E. Jackson, 13 CCH Tax Ct. Mem. 1175 (1954); Clarence E. Stewart, 12 CCH Tax Ct. Mem. 921 (1953); Philip Allen, 1 CCH Tax Ct. Mem. 14 (1942).

The Tax Guide For Small Business[56] gives the following summary of the proof necessary to substantiate the loss deduction:

> Proof of Casualty Loss. A deduction is allowed only for damages to or losses of property owned by you. You must substantiate the amount of any casualty loss. You should be prepared to submit evidence when it occurred:
>
> 1. Nature of casualty and when it occurred;
>
> 2. Loss was the direct result of the casualty;
>
> 3. That you were the owner of the property at the time of the loss;
>
> 4. Cost of other adjusted basis of the property, supported by purchase contract, checks, receipts, etc.;
>
> 5. Depreciation allowed or allowable, if any;
>
> 6. Values before and after casualty (pictures and appraisals before and after the casualty are pertinent evidence); and
>
> 7. The amount of insurance or other compensation received, including the value of repairs, restoration, and cleanup provided without cost of relief agencies.

In outline form, the following are the elements of proof necessary to demonstrate qualification for a casualty loss deduction:

(a) An identifiable event which reflects the constituent elements of a casualty, viz., the sudden, unexpected, or unusual nature of the event;[57] the year in which the event occurred,[58] and if the event itself merely opened the loss transaction, the year in which the loss transaction was closed should also be included;[59] and finally, the causal connection between the event and injury.[60]

(b) Taxpayer is the person or entity entitled to claim the loss.[61]

---

[56] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, PUB. NO. 334, TAX GUIDE FOR SMALL BUSINESS, p. 93 (1965).

[57] See cases cited at note 40, *supra.*

[58] Jane U. Elliott, 40 T.C. 304 (1963), *acq.* 1964-2 CUM. BULL. 5; Paul E. Jackson, 13 CCH Tax Ct. Mem. 1175 (1954).

[59] United States v. Barret, 202 F.2d 804 (5th Cir. 1953); Nourse v. Birmingham, 73 F. Supp. 70 (S.D. Iowa 1947); Williard T. Burkett, 10 CCH Tax Ct. Mem. 948 (1951).

[60] Rev. Rul. 59-102, 1959-1 CUM. BULL. 200. A mere showing that the identifiable event present in your case is similar to that approved in other cases as a "casualty," does not necessarily establish the existence of a "casualty" in your case. *Compare* O.D. 1076, 5 CUM. BULL. 138 (1921), *with* Samuel Greenbaum, 8 B.T.A. 75 (1927), the former allowing a loss arising from the freezing and bursting of water pipes; the latter disallowing the loss.

[61] The person or persons entitled to deduct the loss is determined by how title to the property is held. For example, if the property is held by a husband and wife as tenants by the entirety, and separate returns are filed, each spouse is entitled to deduct one-half the loss. Gilbert J. Krause, 10 CCH Tax Ct. Mem. 1071 (1951). *But see* I.T. 3304, 1939-2 CUM. BULL. 158 holding that although the property was held as tenants by the entirety, if the husband defrayed all the expenses in repairing the property, the husband was entitled to claim the full loss, assuming, of course, that, if he claimed the entire deduction, his wife does not attempt to claim any deduction on her return.

(c) A description of the property sufficient to establish that it is the property which sustained the injury.[62]

(d) The cost or adjusted basis of the property.[63]

(e) The fair market value of the property immediately before and after the casualty event.[64]

(f) The amount of salvage value,[65] insurance proceeds or other compensation recovered.[66]

Failure to establish salvage value and/or the amount of the insurance recovery, if any, or particularly that there was no insurance recovery is a common failure.[67] This blunder in the handling of the case may be one which cannot be corrected.[68]

B. *Business Property*

(a) Amount of Loss

In the case of property used in a trade or business or held for the production of income, the amount of the loss arising from partial injury or destruction of the property is the LESSER of either (1) the difference in the fair market value of the property immediately preceding and immediately after the casualty event; or (2) the amount of the adjusted basis for determining the loss from the sale

---

[62] David W. Murray, Jr., 21 CCH Tax Ct. Mem. 7 (1962); Benjamin J. Checkoway, 19 CCH Tax Ct. Mem. 1174 (1960); Richard E. Stein, 14 CCH Tax Ct. Mem. 191 (1955); Gilbert J. Kraus, 10 CCH Tax Ct. Mem. 1071 (1951); Isabelle B. Krome, 9 CCH Tax Ct. Mem. 178 (1950); Benard L. Shackleford, 7 CCH Tax Ct. Mem. 694 (1948); Greenwood Packing Plant, 46 B.T.A. 430 (1942), *acq.* 1942-1 CUM. BULL. 8, *rev'd on other grounds,* 131 F.2d 787 (4th Cir. 1942).

[63] Including date of acquisition and if appropriate, the allocation of basis if the property destroyed or damaged is comprised of several types of property. Philip Handelman, 20 CCH Tax Ct. Mem. 878 (1961); Melvin Mailloux, 20 CCH Tax Ct. Mem. 942 (1961), *rev'd on other grounds,* 320 F.2d 60 (5th Cir. 1963); Benjamin J. Checkoway, 19 CCH Tax Ct. Mem. 1174 (1960); Virgil R. Williams, 19 CCH Tax Ct. Mem. 106 (1960) (allocation); John W. Snyder, 14 CCH Tax Ct. Mem. 1218 (1955); Paul E. Jackson, 13 CCH Tax Ct. Mem. 1175 (1954); Nat Lewis, 13 CCH Tax Ct. Mem. 1167 (1954).

[64] Schirmer v. United States, 59-2 USTC ¶ 9572 (N.D. Calif. 1959); Samuel Abrams, 23 CCH Tax Ct. Mem. 1546 (1964); William S. Herreshoff, 22 CCH Tax Ct. Mem. 667 (1963); Maude T. Fearing, 21 CCH Tax Ct. Mem. 800 (1962), *aff'd on other grounds,* 315 F.2d 495 (8th Cir. 1963); Isabelle B. Krome, 9 CCH Tax Ct. Mem. 178 (1950).

[65] Except where salvage value is used to determine the market value immediately after the fire, or other casualty.

[66] Hubinger v. Commissioner, 36 F.2d 724 (2d Cir. 1929), *affirming* 13 B.T.A. 960 (1928), *cert. denied* 281 U.S. 741 (1929); Ferst v. Edwards, Adm'r, 129 F. Supp. 606 (D. Ga. 1955); John W. Snyder, 14 CCH Tax Ct. Mem. 1218 (1955); I.T. 4032, 1950-2 CUM. BULL. 21; Treas. Reg. § 1.165-1(c) (1960).

[67] *E.g.,* Philip Handelman, 20 CCH Tax Ct. Mem. 878 (1961); Emanuel Hollman, 38 T.C. 251 (1962).

[68] *See,* Goodman v. Commissioner, 200 F.2d 681 (2nd Cir. 1953), affirming the Tax Court's denial of a motion for rehearing filed because the taxpayer, claiming medical expenses, neglected to show that such expenses were "not compensated for by insurance or otherwise."

or other disposition of the property involved.[69] The amount thus determined is then adjusted ". . . for any insurance or other compensation received."[70]

---

[69] Treas. Reg. § 1.165-7(b)(1) (1960); INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES, AND THEFTS, p. 7 (March 1964). Practically speaking the adjusted basis of the property is the measure of the loss, *see* United States v. Koshland, 208 F.2d 636 (9th Cir. 1953), Frank R. Hinman, 12 CCH Tax Ct. Mem. 1347 (1953); and, if there is no cost basis, there is no deduction, Belcher v. Patterson, 1960-2 USTC ¶ 9733 (N.D. Ala. 1960). Unfortunately, the regulations are silent on what is meant by "immediately" after the casualty event. Obviously the property has no value when the flood waters are washing through the premises, or the building is in the grip of the conflagration. Is the value measured when the flood subsides or the embers cool? The question is in a sense academic since the statute is aimed at "permanent" loss in value (*see* Jenard, *supra* note 44 and Citizens Bank of Weston, *supra* note 46. Presumably the practical approach would be to consider the property's worth immediately after the event (when the fire burned out, the flood subsided, etc.) which in all likelihood is salvage or residual value (depending, of course, on how severely the casualty affected the property) and then discount that loss of value for factors which would occur or are likely to occur within a "reasonable" time after the casualty event. The taxpayer, of course, is allowed a deduction for his clean-up expense, either as a separate item (ordinary business expense) or as part of his decrease in value, so that this is not a major consideration. It is, of course, difficult to foretell what events are likely to occur and to measure or fix a "reasonable" time. Nonetheless, it would appear that "immediately after" value should take into consideration what the property will sell for after the property is repaired, the debris removed, the damage assessed or clearly marked for the buyer to see (so that the buyer can determine how much he would discount the purchase price in order to pay for the rebuilding) and after the immediate shock has worn off in the public's mind. This approach is not based on the casualty loss regulations but is suggested by the general approach to value found in the Code. For example, Treas. Reg. § 20.2031-1(b), speaking to the general valuation rules, states: "The fair market value of a particular item of property includible in the decedent's gross estate is not to be determined by a *forced sale* price." (emphasis added), and Treas. Reg. § 20.2031-2(e), concerning the valuation of stock, states: "If the executor can show that the block of stock to be valued is so large in relation to the actual sales on the existing market that it could not be liquidated in a *reasonable time* without depressing the market, the price at which the block could be sold as such outside the usual market . . . may be a more accurate indication of value than market quotations." (emphasis added). These regulations indicate that as a practical matter the IRS will not accept as the loss in value the amount determined at the height of the casualty event. *See* J. G. Boswell Co., *supra* note 43.

[70] Treas. Reg. § 1.165-1(c) (1960); INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 7 (March 1964), *and see, e.g.,* Miree v. United States, 1962-2 USTC ¶ 9756 (N.D. Ala. 1962); Ticket Office Equipment Co., 20 T.C. 272 (1953), *acq.* 1953-2 CUM. BULL. 6, *aff'd per curiam on other grounds,* 213 F.2d 318 (2nd Cir. 1954); Gilbert J. Kraus, 10 CCH Tax Ct. Mem. 1071 (1951). Salvage value is used only in a complete destruction situation wherein the adjusted basis alone is used as the measure of the loss. In other words if the difference in market values is used to determine the amount of loss, then salvage value is a part of the "after" value of the property and is not again deducted from the difference and this is so even if the adjusted basis is lower, all that is allowable as a deduction is the amount of the basis. For example, if the fair market value of an item is $1,000, the basis $900, and salvage value of "after" casualty value is $50, the economic loss is $950, but because the amount deductible is the "lesser" amount between market values and basis, only $900 is deductible. Salvage value of $50 is *not* again deducted from the $900 to reduce the loss to $850, Sears v. United States, 59-1 USTC ¶ 9302 (N.D. Ohio 1959). Salvage value, of course, remains an element of proof to establish the loss. Hubinger v. Commissioner, 36 F.2d 724 (2nd Cir. 1929), *affirming* 13 B.T.A. 960 (1928), *cert. denied* 281 U.S. 741 (1929); Frances L. Davis, 9 CCH Tax Ct. Mem. 306 (1950).

If the property is totally destroyed, and if the fair market value of such property immediately before the casualty is less than the adjusted basis of such property, the amount of the adjusted basis of such property is treated as the amount of the loss.[71] The amount deductible, of course, is decreased by salvage value, insurance, or other recovery.[72]

An example demonstrating the computation of the allowable loss deduction where the property is completely destroyed, is as follows:[73]

> *Example*: You owned a building used in your business which had an adjusted (depreciated) basis of $20,000, exclusive of land, at the time it was completely destroyed by a hurricane. Its fair market value just before the hurricane was only $15,000. Since this was business property, and since it was completely destroyed, your deductible loss is your adjusted basis of $20,000, decreased by salvage value, insurance, or other recovery.

(b) "Single Property" Rule

A loss incurred in a trade or business or in any transaction entered into for profit is determined under the rules set forth in paragraph (a) above by reference to the single identifiable property damaged or destroyed.[74] The regulations give this example:

> Thus, for example, in determining the fair market value of the property before and after the casualty in a case where damage by casualty has occurred to a building and ornamental or fruit trees used in a trade or business, the decrease in value shall be measured by taking the building and trees into account separately, and not together as an integral part of the realty, and separate losses shall be determined for such building and trees.[75]

Another example is *United States v. Koshland*,[76] involving these

---

[71] Treas. Reg. § 1.165-7(b)(1) (1960) as amended, T.D. 6786, 1965-1 CUM. BULL. 107; INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 7 (March 1964).

[72] Treas. Reg. § 1.165-1(c) (1960); I.T. 4032, 1950-2 CUM. BULL. 21. Salvage value in this situation must be deducted in computing the amount of the loss since it has not yet been considered in the computation. Insurance "or other recovery" includes replacement property, etc., as well as cash. For example, in Ray Durden, 3 T.C. 1 (1944), *acq.* 1944 CUM. BULL. 8, to arrive at the deduction, the court subtracted the insurance proceeds and the value of the driveway laid down by the county in settlement of damage caused to the taxpayer's house by blasting. Obviously, if the taxpayer has made up the loss by repairs the cost of which were deducted as business expenses, he is not entitled to a casualty loss deduction. J. G. Boswell Co., 34 T.C. 539 (1960), *aff'd* 302 F.2d 682 (9th Cir. 1962), *cert. denied* 371 U.S. 860 (1962); Central Arizona Ranching Co., 23 CCH Tax Ct. Mem. 1304 (1964).

[73] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 7 (March 1964).

[74] Treas. Reg. § 1.165-7(b)(2) (1960); United States v. Koshland, 208 F.2d 636 (9th Cir. 1953). The "single property" rule raises the importance of a proper allocation of purchase price among various properties acquired in a single transaction. See, *e.g.*, Virgil R. Williams, 19 CCH Tax Ct. Mem. 106 (1960); Stanley Kupiszewski, 23 CCH Tax Ct. Mem. 1559 (1964).

[75] Treas. Reg. § 1.165-7(b)(2) (1960).

[76] 208 F.2d 636 (9th Cir. 1953).

facts: Taxpayer and her husband purchased a hotel in 1925 for the sum of $185,000 plus accrued real property taxes. For depreciation purposes, $53,000 was allocated to the building. By 1946, taxpayer had been allowed a total of $52,684 as depreciation for the hotel building and had made improvements of $2,092.16. On May 20, 1946, the hotel building was destroyed by fire. The taxpayer received proceeds of the fire incurance policies on the hotel property in the amount of $45,000. In December 1946, she sold the land, in the condition it had been left by the fire, for $50,000. The taxpayer claimed that, under section 165 she sustained a deductible fire loss of $43,166 in 1946, this being the difference between the adjusted basis of the land and building at the time of the fire ($138,166) and the sum of the market value of the property after the fire ($50,000) and the insurance proceeds ($45,000). The court, relying upon the "single property" rule, held that the "property" destroyed in this case was the hotel building and since at the time of the fire the building had an adjusted basis of $1,408, the insurance proceeds ($45,000) more than compensated for the loss.[77]

An example demonstrating the computation of the allowable loss deduction under the "single property" rule, is as follows:[78]

> *Example (2)*: In 1958 A purchases land containing an office building for the lump sum of $90,000. The purchase price is allocated between the land ($18,000) and the building ($72,000) for purposes of determining basis. After the purchase A planted trees and ornamental shrubs on the grounds surrounding the building. In 1961 the land, building, trees, and shrubs are damaged by hurricane. At the time of the casualty the adjusted basis of the land is $18,000 and the adjusted basis of the building is $66,000. At that time the trees and shrubs have an adjusted basis of $1,200. The fair market value of the land and building immediately before the casulty is $18,000 and $70,000, respectively, and immediately after the casulty is $18,000 and $52,000 respectively. The fair market value of the trees and shrubs imme-- diately before the casualty is $2,000 and immediately after the casualty is $400. In 1961 subject to section 1231 and §1.1231-1. The amount of the deduction allowable under section 165(a) with respect to the building for the taxable year 1961 is $13,000, computed as follows:
>
> | | |
> |---|---|
> | Value of property immediately before casualty ..... | $70,000 |
> | Less: Value of property immdeiately after casualty ..... | 52,000 |
> | Value of property actually destroyed ..... | 18,000 |

[77] The facts set forth in the *Koshland* case indicate that the taxpayer might have had a gain. To the extent that insurance proceeds or other compensation, exceeds the depreciated cost or other adjusted basis of the property destroyed or damaged, the difference is a gain from an involuntary conversion. INT. REV. CODE of 1954 §§ 1033, 1245 and 1250.

[78] Treas. Reg. § 1.165-7(b)(3) (1960), *Example (2)*.

Loss to be taken into account for purposes of section 165(a):	
Lessor amount of property actually destroyed ($18,000) or adjusted basis of property ($66,000)	$18,000
Less: Insurance received	5,000
Deduction allowable	13,000

The amount of the deduction allowable under section 165(a) with respect to the trees and shrubs for the taxable year 1961 is $1,200, computed as follows:

Value of property immediately before casualty	$ 2,000
Less: Value of property immediately after casualty	400
Value of property actually destroyed	1,600
Loss to be taken into account for purposes of section 165(a) Lessor amount of property actually destroyed ($1,600) or adjusted basis of property ($1,200)	1,200

Prior to the adoption of the final version of Treasury Regulation § 1.165-7(b)(2), the loss in a partial loss situation was ". . . the proportion of the adjusted basis determined under section 1011 which the value of the destroyed property bears to the value of the entire property, reduced by any insurance or other compensation received in respect of the property."[79] Proposd Treasury Regulation § 1.165-3(c)(1) gives the following example of the computation:

> *Example.* A purchased an automobile for $4,200 on January 1, 1955, and at once devoted it to business use. The expected life of the automobile was 6 years. On January 1, 1957, the automobile sustained damages through casualty. The value of the automobile immediately before the casualty was $2,000. The value of the automobile immediately after the casualty is $1,500. A is compensated by insurance in the amount of $300. The amount of the allowable deduction to A is $400 (loss of $700 less insurance of $300), computed as follows:

Cost	$4,200
Less: Depreciation for 1955 and 1956 at $700 per year	1,400
Adjusted basis at time of casualty	2,800
Value before casualty	2,000
Value after casualty	1,500
Value of destroyed property	500
Allowable loss $\frac{(\ 500\ )}{(\$2,000)} \times \$2,800$	700
Less: Insurance received	300
Allowable deduction	$ 400

The above stated method of computing the amount of the loss has the sanction of several court decisions[80] although it was ques-

[79] Proposed Treas. Reg. § 1.165-3 (c)(1), 21 Fed. Reg. 4925 (1956).

[80] G.C.M. 6122, VIII-2 CUM. BULL. 115 (1929); Fred Fazer, 10 B.T.A. 409 (1928); Bessie Knapp, 23 T.C. 716 (1955).

tioned in *Alcoma Association, Inc. v. United States.*[81] It may still have some validity in rare situations where the taxpayer is unable to allocate any basis to the separate properties acquired for a single purchase price. It should be noted that the former rule gives a higher deduction than that afforded by the rule applicable under the final regulations (lesser of market value or adjusted basis) where the adjusted basis of the asset is in excess of its market value before the casualty.[82]

(c) Inventory

The *Tax Guide for Small Business* (1964),[83] p. 83, sets forth the following rules for the treating of casualty losses with respect to inventory.[84]

> LOSS OF INVENTORY. The manner of reporting your casualty or theft loss of inventory or items held for sale to customers will depend upon whether you have received or will recover any part of your loss from insurance or other reimbursement. If no recovery or other reimbursement is anticipated, the loss will be automatically reflected in cost of goods sold where your opening and closing inventories are properly reported. This loss should not be claimed again as a casualty loss. If you wish to show the loss separately, an offsetting credit either to opening inventory or to purchases is required.
>
> Insurance proceeds received in the year of the loss must be included in gross income if you reflect the loss in closing inventory. However, the recovery should not be included in gross income if you show the loss separately and offset the insurance against the loss. The insurance must be accounted for in your return. If the insurance is not received by the end of the year, you must remove the amount of the loss from cost of goods sold.
>
> Should your creditors forgive, in the year of the loss, part of what you owe them because of your inventory loss, such amounts must be taken into account as income, or you must make appropriate adjustments to your cost of goods sold.
>
> If suppliers replace damaged or destroyed inventory items in the year of loss at no cost to you, no adjustments should be made.

(d) Converted Property

In the case of property which originally was not used in a trade or business or held for income-producing purposes and which

---

[81] 239 F.2d 365 (5th Cir. 1956).

[82] See, *e.g.*, Barry v. United States, 175 F. Supp. 308 (W.D. Okla. 1958). *Cf.* Frank R. Hinman, 12 CCH Tax Ct. Mem. 1347 (1953).

[83] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, PUB. NO. 334, p. 83 (1964).

[84] See also Treas. Reg. § 1.165-7(a)(4) (1960); INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 7 (March 1964). *But see,* Ticket Office Equipment Co., 20 T.C. 272 (1953), *acq.* 1953-2 CUM. BULL. 6, *aff'd* per curiam *on other grounds,* 213 F.2d 318 (2nd Cir. 1954); Lorraine Turpentine Co., 20 B.T.A. 423 (1930), *acq.* this issue, X-1 CUM. BULL. 39 (1931).

12.	Loss sustained on furnishings (lesser of 10 or 11)	$ 500
13.	Less: estimated insurance recovery	None
14.	Casualty loss on furnishings	$ 500
15.	Total loss (7 plus 14)	$4,500
16.	Less $100 reduction	100
17.	Casualty loss deduction	$4,400

(i) *"From Each Casualty"*

Congress has indicated that the determination of whether the loss arises from a single or multiple casualty is to be liberally made[92] in favor of a single casualty. Events closely related in origin generally give rise to a single casualty.[93] Examples illustrating the determination of whether the incident gave rise to a single event include the following:[94]

> *Example 1.* Thieves broke into your home in January 1964 and stole a diamond ring and a fur coat. You sustained a loss of $150 on the ring and $200 on the coat. This is a single theft, and the $100 limitation is applied to the total amount of your loss of $350. Your deductible loss from the theft is the excess over $100, or $250.
>
> *Example 2.* Your family car was damaged in an accident in January 1964 and the amount of your loss, after insurance recovery, was $75. In February 1964 your car was damaged in another accident and this time your loss after insurance recovery was $90. The $100 limitation must be applied to each separate casualty loss, and since neither accident resulted in a loss of over $100, you are not entitled to any deduction for these accidents.
>
> *Example 3.* In March 1964 hurricane winds blew the roof from your residence and caused flood waters that further damaged your house and demolished your furniture and personal automobile. This is considered to be a single casualty and the $100 limitation is applied against the total loss sustained as the result of the wind and flood waters. You do not have to compute separately the amount of loss caused by the wind and the amount caused by the water, nor do you compute separately the loss sustained on your house, your furniture, and your automobile in applying the $100 limitation.

Individual taxpayers other than husband and wife are subject to a separate $100 floor with respect to each casualty, even though property of other persons is damaged in connection with the same event.[95] For example, if fire damages a house and household goods of the owner, as well as the property of a visiting relative which

---

[92] H.R. Rep. No. 749, 88th Cong., 1st Sess., p. A46 (1963); *See,* Treas. Reg. § 1.165-7(b)(4)(ii) (1960), as amended, T.D. 6786, 1965-1 CUM. BULL. 107.

[93] *Ibid.*

[94] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 5 (March 1964). Example 3 as quoted in the text is based on the example given in H.R. Rep. No. 749, *supra* note 92, at A46.

[95] Treas. Reg. § 1.165-7(b)(4)(iii) (1960), as amended, T.D. 6786, 1965-1 CUM. BULL. 107; H.R. Rep. No. 749, *supra* note 92, at A46.

is in the same house, the owner is subject to one $100 floor and the visiting relative is subject to a separate $100 floor.[96]

(ii) *Jointly Owned Property — Joint Returns*

As indicated above, where two or more individuals (other than husband and wife) suffer losses from the same casualty, the $100 reduction is applied separately to each and this is so whether or not the property is held jointly or in some other form of common ownership.[97] For example, if two brothers jointly own a house in which both live, and a fire destroys the house, each brother would be entitled to one-half of the loss and each would be required to apply a separate $100 reduction to his share of the loss.

For purposes of applying the $100 floor, a husband and wife filing a joint return for the taxable year in which the loss is allowed as a deduction are treated as one individual. If a husband and wife file a joint return, only one $100 floor applies for each casualty regardless of whether the loss is sustained with respect to jointly owned or separately owned property. If a husband and wife file separate returns, each is subject to a $100 floor for each casualty, regardless of whether the property damaged is owned jointly or separately.[98] For example, if a loss from fire to their personal residence is sustained by a husband and wife who own their home jointly, a single $100 reduction is applied to such loss in determining the amount deductible on their joint return. However, if they file separate returns, the loss must be split equally between them and each must apply a separate reduction of $100 to his or her share of that loss.[99]

(iii) *Floor Applies in Year of Deduction*

The $100 — deductible rule applies to all losses sustained after December 31, 1963, in taxable years ending after that date.[100] Thus, the rule applies if the loss occurred in 1964 even though under Int. Rev. Code of 1954 § 165 (h) the taxpayer deducted the loss on his 1963 return.[101] The IRS has indicated, however, that

---

[96] See, *ibid.*

[97] Treas. Reg. § 1.165-7(b)(4)(iii) (1960), as amended, T.D. 6786, 1965-1 CUM. BULL. 107; INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 6 (March 1964).

[98] Treas. Reg. § 1.165-7(b)(4)(iii) (1960), as amended, T.D. 6786, 1965-1 CUM. BULL. 107; H.R. Rep. No. 749, *supra* note 92, at A46.

[99] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 6 (March 1964).

[100] Treas. Reg. § 1.165-7(b)(4)(i) (1960), as amended, T.D. 6786, 1965-1 CUM. BULL. 107.

[101] *Ibid.*; INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 6 (March 1964).

even if the casualty event occurred in 1963 or prior years, but the loss could not be claimed because of an expectation of reimbursement or recovery, the $100 reduction applies to any part of the loss deducted in years after December 31, 1963.[102] The theory being that the loss is not actually sustained until the prospect of recovery is ended.

(iv) *Property Used Partly in Business*

In the case of a casualty loss of property used partially for business and partially for personal purposes, the $100 floor applies only to the net loss attributable to the portion of the property used for personal purposes. For example, if a casualty causes damage in the amount of $1000 to a taxpayer's automobile having an adjusted basis of $2000, which is used 50 percent for business and 50 percent for personal purposes, and the taxpayer's insurance recovery with respect to the casualty is $900, the taxpayer has a net loss of $100. Fifty percent of this loss, or $50, is considered a business loss, and is fully deductible. The remaining $50 of loss is personal, and is nondeductible because of the $100 floor.[103]

(c) Agregation Rule

In determining the amount of a casualty loss involving real property and improvements thereon not used in a trade or business or in any transaction entered into for profit, the improvements (such as buildings and landscaping) to the property damaged or destroyed are considered an integral part of the property and no separate basis need be apportioned to such improvements.[104]

(d) Reimbursement in Later Year

If the taxpayer is reimbursed for his loss (assuming that the prospect of recovery in the year of the casualty event did not warrant postponing the deduction) in a year or years after the loss had been deducted, the recovery is included in income in the later year under the rules provided in Internal Revenue Code of 1954 § 111.[105]

---

[102] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 6 (March 1964).

[103] Treas. Reg. § 1.165-7(b)(4)(iv) (1960), as amended, T.D. 6786, 1965-1 CUM. BULL. 107.

[104] Buttram v. Jones, 87 F. Supp. 322 (W.D. Okla. 1943); Louis A. Edwards, 19 CCH Tax Ct. Mem. 925 (1960); Dick H. Woods, 19 CCH Tax Ct. Mem. 388 (1960); William O. Lindley, 11 CCH Tax Ct. Mem. 355 (1952); Western Products Co., 28 T.C. 1196 (1957), *acq.* 1958-1 CUM. BULL. 6; G.C.M. 21013, 1939-1 CUM. BULL. 101; Treas. Reg. § 1.165-7(b)(2)(ii) (1960), as amended, T.D. 6786, 1965-1 CUM. BULL. 107; Treas. Reg. § 1.165-7(b)(3) (1960), *Example 3.*

[105] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, PUB. NO. 334, TAX GUIDE FOR SMALL BUSINESS, p. 83 (1964); Treas. Reg. § 1.111-1(a)(1) (1956).

V. MEASURE OF DAMAGES

A. *Introduction*

As indicated above, the major factor in determining the amount of the casualty loss is the amount by which the asset has decreased in value, i.e., in general terms, the decrease in relative market values.[106] Obviously, this calls for a demonstration of the decrease or, in other words, proof of the loss by the application of acceptable standards for measuring the damages. To achieve the desired result, the taxpayer must adopt a method of valuation.

The regulations issued pursuant to section 165 seemingly indicate that there are two equally acceptable methods of reflecting the amount of loss, first, appraisals and, secondly, cost of repairs and replacements.[107] The taxpayer, however, must not be misled and lose sight of the theory involved, viz., the loss is measured by the difference in *market values* of the asset before and after the casualty event.[108] Hence, proof of the cost of repairs is not sufficent to show the amount of loss absent evidence clearly demonstrating that the cost of repairs is indicative and corroborative of the difference in market values.[109] This principle is illustrated by the fact that the taxpayer is entitled to deduct the amount of his loss (the difference in market values) irrespective of whether this amount exceeds or is less than the cost of repairs.[110] The taxpayer should not forget that a sale of the property after the casualty, though not essential to reflect the loss, is one of the best indications of the amount of the loss, and, for example, if the asset is sold for a price equal to or more than adjusted basis (if higher) or market value of the property before the casualty, taxpayer has no loss regardless of the testimony of his appraisers and the cost of repairs.[111] Finally, the taxpayer, in proving his case, must keep in mind the type of property involved (business or nonbusiness) and whether the "separate property" or aggregation rules apply. Thus, if the aggregation rule

---

[106] See Helvering v. Owens, 305 U.S. 468 (1939).

[107] Treas. Reg. § 1.165-7(a)(2) (1960).

[108] Helvering v. Owens, *supra* note 106.

[109] Hubinger v. Commissioner, 36 F.2d 724 (2nd Cir. 1929) *affirming* 13 B.T.A. 960 (1928), *cert. denied* 281 U.S. 741 (1929); Paul E. Jackson, 13 CCH Tax Ct. Mem. 1175 (1954); Robert H. Montgomery, 6 CCH Tax Ct. Mem. 77 (1947); Ray Durden, 3 T.C. 1 (1944), *acq.* 1944 CUM. BULL. 8; George B. Friend, 8 B.T.A. 712 (1927), *acq.* VII-2 CUM. BULL. 14 (1928). *But cf.* Clarence E. Stewart, 12 CCH Tax Ct. Mem. 921 (1953).

[110] A.R.R. 4725, III-1 CUM. BULL. 143 (1924); Miree v. United States, 62-2 USTC ¶ 9756 (N.D. Ala. 1962); Graham M. Brush, 21 CCH Tax Ct. Mem. 649 (1962). *But cf.* Clapp v. Commissioner, 321 F.2d 12 (9th Cir. 1963), *affirming* 36 T.C. 905 (1961). Taxpayers are well advised to consider appraisals as the major element of proof since the difference in market values may in some instances exceed repairs.

[111] *E.g.*, Dick H. Woods, 19 CCH Tax Ct. Mem. 388 (1960).

is thereafter converted to either of these uses, the loss is treated in the same way as the loss from any other business property, except that if the fair market value of the property on the date of conversion is less than the adjusted basis of the property at that time, the fair market value is used as the basis for determining the amount of loss.[85] Where the property is held partly for nonbusiness purposes and partly for business purposes or for the production of income, the casualty loss deduction must be computed as though two separate pieces of property were involved — one business and the other personal.[86]

C. *Nonbusiness Property*

(a) Amount of Loss

In the case of nonbusiness property, I.T. 4032,[87] sets forth the following rule:

> It is held that the amount of loss which is deductible . . . in the case of depreciable nonbusiness property, is the difference between the value of the property immediately preceding the casualty and its value (including salvage value) immediately after the casualty, but not in excess of an amount equal to the adjusted basis of the property, reduced by any insurance or compensation received. In other words, the amount of insurance or other compensation received must be applied to the amount of the loss otherwise determined, whether measured by the difference between the value of the property immediately before and immediately after the casualty, or limited to the adjusted basis of the property . . . .

This is the same rule applicable to business property except that it does not include the business property provision dealing with the total destruction of the asset.[88]

An example demonstrating the computation of the allowable loss deduction in a situation where nonbusiness property is partially destroyed is as follows:[89]

Example (1). In 1956 B purchases for $3,600 an automobile

---

[85] Treas. Reg. § 1.165-7(a)(5) (1960) as amended T.D. 6712, 1964-1 (Part 1) CUM. BULL. 107; Treas. Reg. § 1.165-9(b) (1960), as amended, T.D. 6712, 1964-1 (Part 1) CUM. BULL. 107.

[86] G.C.M. 8628, IX-2 CUM. BULL. 112 (1930), Rev. Rul. 286, 1953-2 CUM. BULL. 20; INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 8 (March 1964).

[87] 1950-2 CUM. BULL. 21; Gilbert J. Kraus, 10 CCH Tax Ct. Mem. 1071 (1951); Rev. Rul. 54-85, 1954-1 CUM. BULL. 58; Rev. Rul. 79, 1953-1 CUM. BULL. 41; Treas. Reg. § 1.165-7(b) (1960), as amended T.D. 6786 1965-1 CUM. BULL. 107.

[88] *See also,* Helvering v. Owens, 305 U.S. 468 (1939); Buttram v. Jones, 87 F. Supp. 322 (W.D. Okla. 1943); J. H. Anderson, 7 CHH Tax Ct. Mem. 811 (1948); G.C.M. 21013, 1939-1 CUM. BULL. 101 G.C.M. 16255, XV-1, CUM. BULL. 115 (1936); Treas. Reg. § 1.165-7(a) (1960), as amended, T.D. 6786, 1965-1 CUM. BULL. 107.

[89] Treas. Reg. § 1.165-7(b)(3) (1960), as amended, T.D. 6786, 1965-1 CUM. BULL. 107, *Example (1).*

which he uses for nonbusiness purposes. In 1959 the automobile is damaged in an accidental collision with another automobile. The fair market value of B's automobile is $2,000 immediately before the collision and $1,500 immediately after the collision. B receives insurance proceeds of $300 to cover the loss. The amount of the deduction allowable under section 165(a) for the taxable year 1959 is $200, computed as follows:

Value of automobile immediately before casualty	$2,000
Less: Value of automobile immediately after casualty	1,500
Value of property actually destroyed	500
Loss to be taken into account for purposes of section (165a): Lessor amount of property actually destroyed ($500) or adjusted basis of property ($3,600)	500
Less: Insurance received	300
Deduction allowable	200

(b) $100 - Deductible Provision

Pursuant to section 165(c)(3)[90] a casualty loss described in (c)(3) ("loss of property not connected with a trade or business") which arises after December 31, 1963, is deductible only to the extent that the amount of the loss to the taxpayer arising from each casualty exceeds $100.

An example demonstrating the inclusion of the $100 deductible provision in the computation of the allowable loss, is as follows:[91]

Example. Mr. Lee's home, which cost him $4,000, including land, was partially destroyed by a flood following a storm in March 1964. The value of the property (building and land) immediately before the storm was $7,500 and the value immediately after the storm was $2,500. His household furnishings were completely destroyed. They cost him $1,250 but had a fair market value before the storm of $500. His insurance did not cover this type of damage and he estimated no recovery. His casualty loss is $4,500, but his deduction is limited to $4,400, computed in the following manner:

1.	Value of property before storm	$7,500
2.	Value of property after storm	2,500
3.	Decrease in value of property	$5,000
4.	Adjusted basis of property (Cost in this case)	4,000
5.	Loss sustained on property (lesser of 3 or 4)	$4,000
6.	Less: estimated insurance recovery	None
7.	Casualty loss on property	$4,000
8.	Value of furnishings before storm	$ 500
9.	Value of furnishings after storm	None
10.	Decrease in value of furnishings	$ 500
11.	Adjusted basis of furnishings (cost)	1,250

[90] Revenue Act of 1964 § 208, 78 Stat. 19; Treas. Reg. § 1.165-7(b)(4) (1960), as amended, T.D. 6786, 1965-1 CUM. BULL. 107.

[91] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 5 (March 1964).

applies, taxpayer has failed his burden of proof if he proves only the market value of one of the units of property involved as, for example, showing the value of trees and shrubs, but not the value of the entire property.[112]

B. *Appraisals — Expert Witnesses*

Treasury Regulation § 1.65-7(a)(2)(i) provides:

> In determining the amount of loss deductible under this section, the fair market value of the property immediately before and immediately after the casualty shall generally be ascertained by competent appraisal. This appraisal must recognize the effects of any general market decline affecting undamaged as well as damaged property which may occur simultaneously with the casualty, in order that any deduction under this section shall be limited to the actual loss resulting from damage to the property.

The Internal Revenue Service has also indicated that "[a]ppraisals should be made by an experienced and reliable appraiser. The appraiser's knowledge of sales of comparable property, conditions in the area, his familiarity with your property before and after the casualty, and the method used by him are important elements in proving a casualty loss.[113]

In deciding to secure expert assistance in determining the amount of the loss, the taxpayer should keep these practical considerations in mind:

(a) As is obvious but bears repeating, the more competent and skilled the appraiser, the more likely it is that the taxpayer will succeed in his burden of proof.[114] Since the appraisal fee may be deducted as an expense of determining tax liability if the taxpayer itemizes his deductions, the taxpayer should not lose sight of the fact that the government is paying part of the expense. The usual compulsion to proceed as cheaply as possible should not, therefore, be the only factor considered particularly when the cost of a skilled appraiser may reap larger ordinary income deductions.

(b) The taxpayer should keep in mind that the government (i) instead of producing expert testimony on its behalf, may rely solely on the presumption of correctness in which case the taxpayer will

---

[112] Western Products Co., 28 T.C. 1196, 1218 (1957), *acq.* 1958-1 CUM. BULL. 6. *Cf.* Mary Cheney Davis, 16 B.T.A. 65 (1929), *acq.* VIII-2 CUM. BULL. 13 (1929).

[113] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 8 (March 1964); INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, PUB. NO. 334, TAX GUIDE FOR SMALL BUSINESS, p. 92 (1965).

[114] Mary F. Cary, 7 CCH Tax Ct. Mem. 724 (1948) (hurricane damage to trees; taxpayer relying on the testimony of a real estate appraiser to show decrease in market value and a forest engineer and former park commissioner to show cost of replacement, was allowed the full deduction claimed.); Graham M. Brush, 21 CCH Tax Ct. Mem. 649 (1962) (Tax Court relied on taxpayer's experts.).

ordinarily prevail if his expert has some degree of competence;[115] or (ii) the Service may rely on its own valuation engineer who will suffer, by comparison with a local expert, for lack of familiarity with the local conditions.[116]

(c) While the Court will be the final arbiter of the witnesses' qualifications,[117] any witness familiar with the property is better than no witness, even if the witness called is the taxpayer himself,[118] and the taxpayer is likely to be allowed some part of his deduction even if his expert is held less qualified than the Service's witness.[119]

(d) In preparing to give testimony or supplying background information to the appraiser, the taxpayer should not overlook such facts as the assessed value for real estate tax purposes, value fixed for insurance coverage, and after the casualty, the amount of insurance claim and insurance settlement, prior listing of the property

---

[115] Royal Little, 31 T.C. 607 (1958), *acq.* 1959-1 CUM. BULL. 4, *aff'd on other grounds,* 273 F.2d 746 (1st Cir. 1960) (taxpayer relying on the deposition of a local realtor and appraiser, prevailed on the full amount of the deduction claimed since the Commissioner offered no evidence in opposition and the Tax Court found taxpayer's expert adequately qualified to value the property before and after the storm.).

[116] Biddle v. United States, 175 F. Supp. 203 (E.D. Pa. 1959) (The Court relied more heavily on taxpayer's expert although he had seen the property two years before the storm and rendered his appraisal after seeing the property more than four years after the storm, than upon the Internal Revenue Service's witness who had visited the property two years after the storm and had not seen it before the storm.). *But cf.* William O. Lindley, 11 CCH Tax Ct. Mem. 355 (1952) and Ralph Walton, 20 CCH Tax Ct. Mem. 653 (1961) where the court relied on the Internal Revenue Service's experts as being more qualified than taxpayer's witnesses.

[117] *E.g.,* J. H. Anderson, 7 CCH Tax Ct. Mem. 811 (1948); Donald G. Graham, 35 T.C. 273 (1960), *acq.* 1961-2 CUM. BULL. 4.

[118] Nat Lewis, 13 CCH Tax Ct. Mem. 1167 (1954) (taxpayer was sustained on his own uncontradicted testimony); Carl A. Haslacher, 9 CCH Tax Ct. Mem. 314 (1950) (taxpayer, trying his own case, testified for himself, his testimony being based on what he learned from speaking with others. The IRS called an expert who had not seen the property until three years after the storm. The Tax Court, commenting that the taxpayer's own testimony was not as strong as it might have been if he called experts more knowledgeable and experienced than himself, did allow a deduction of $1,300, an amount between the taxpayer's high of $1,800 and the government's low of $750.). *Cf.* Melvin Mailloux, 20 CCH Tax Ct. Mem. 942 (1961), *rev'd on other grounds,* 320 F.2d 60 (5th Cir. 1963) (The Tax Court sustained the government because the taxpayer was (1) not an expert appraiser; (2) the items lost were listed from memory; (3) no attempt to find their depreciated value; and (4) no description of the lost items.); Bernard L. Shackleford, 7 CCH Tax Ct. Mem. 694 (1948) (Tax Court while considering taxpayer's testimony relied more heavily on the testimony of expert called by the taxpayer.).

[119] S. F. Horn, 18 CCH Tax Ct. Mem. 177 (1959) (taxpayer claiming $10,000 was allowed $5,000); Jay Howard, 18 CCH Tax Ct. Mem. 413 (1959) (taxpayer claimed $1,275, the IRS allowed $192, and Tax Court sustained a deduction of $750 after discounting the taxpayer's expert's testimony for lack of familiarity with the property); Doyle E. Collup, 21 CCH Tax Ct. Mem. 128 (1962) (the Tax Court after considering the testimony, lowered the value of the property as appraised before the storm from $29,000 to $26,000 but accepted the appraised value for the property after the storm); Ralph Walton, 20 CCH Tax Ct. Mem. 653 (1961) (taxpayer claimed $3,000; the IRS allowed $1,460; and the Tax Court $2,000); William O. Lindley, 11 CCH Tax Ct. Mem. 355 (1952) (taxpayer claimed $25,000 but the Tax Court allowed $7,500 by weighing the testimony of the witnesses on both sides).

for sale, other attempts to sell the property and other similar facts which have the effect of "pegging" value.[120]

(e) The taxpayer should not forget the value of demonstrative evidence, i.e., photographs, diagrams, etc., in proving the amount of loss particularly as corroborative of the testimony of witnesses. The cost of producing this type evidence is treated in the same manner as the cost of appraisals.[121]

C. *Repairs and Replacement Cost*

Treasury Regulation § 1.165-7(a)(2)(ii) provides:

> The cost of repairs to the property damaged is acceptable as evidence of the loss of value if the taxpayer shows that (a) the repairs are necessary to restore the property to its condition immediately before the casualty, (b) the amount spent for such repairs is not excessive, (c) the repairs do not care for more than the damage suffered, and (d) the value of the property after the repairs does not as a result of the repairs exceed the value of the property immediately before the casualty.

Included in such costs are clean-up expenses.[122] Whatever the "sanctity" of the Service's regulations, taxpayers should remember that in court they must satisfy the market value tests propounded by *Owens* and may well fail their burden unless they tie the cost of repairs into market value.[123] This is not to say that the cost of repairs and replacements cannot be relied upon in dealing with the Service or that in some cases the courts do not consider these costs as a more reliable indicator of the loss in value than the testimony of experts.[124] Indeed, in some reported decisions the courts appear to rely solely upon the cost of repairs.[125] But as indicated in discussing appraisals, some evidence is better than no evidence and

---

[120] Gilbert J. Kraus, 10 CCH Tax Ct. Mem. 1071 (1951); Ferst v. Edwards, 129 F. Supp. 606 (D. Ga. 1955) (the Court relied upon the value found by a real estate appraisal when the property was listed for sale). *But cf.* Andrew A. Maduza, 20 CCH Tax Ct. Mem. 1302 (1961) which stated that the listing of the property for sale does not rise to the dignity of an appraisal of its fair market value.

[121] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 8 (March 1964).

[122] *Ibid.*

[123] See cases cited, *supra* note 109.

[124] Clapp v. Commissioner, 321 F.2d 12, 13 (9th Cir. 1963), *affirming* 36 T.C. 905 (1961).

> Petitioners contend that they had a right to a deduction for the market value of the sand lost; not for the cost of its replacement. The court, however, did not purport to allow the deduction as one for the cost of replacement. It looked to the cost of replacement as evidence of market value before loss. This method of ascertaining the amount of the loss is sanctioned by Treasury Regulation § 1.165-7(a)(2)(ii), and the court did not err in employing it here. . . . But, for the reasons which we have already stated, the court could well have determined that the appraisal offered was not competent and that replacement cost was the most reliable evidence.

Andrew W. Maduza, 20 CCH Tax Ct. Mem. 1302 (1961).

the taxpayer, if he introduces evidence of the cost of repairs and replacements, is likely to succeed in at least a part of the deduction claimed.[126]

The taxpayer would be well advised to consider proving his case from both points of view, first, expert testimony on the relative market values, and second, proof of the cost of repairs or replacements. In point of fact, a review of the decisions dealing with the casualty losses indicates that both elements of proof were present in most cases in which the taxpayer was sustained by the court in the full amount of the deduction claimed.[127] Evidence of cost of repairs and replacements may also be used to support a shaky or less qualified witness.

D. *Automobiles*

The Internal Revenue Service has indicated in several sources[128] that: "The so-called bluebooks issued periodically by various automobile organizations are useful in determining the value of motor vehicles. The amount offered for your vehicle as a trade-in on a new vehicle is not usually a measure of the true value of the vehicle." The Service, however, has sanctioned the use of "trade-in" value in situations where there are appraisals of the "trade-in" value of the automobile both before and after the casualty.[129] Clearly, taxpayers may not rely upon the appraisal of the "trade-in" value to establish the fair market value of the automobile before the casualty and the actual price at which the auto is sold on the open market after the accident as evidence of market value after the casualty.[130]

VI. MISCELLANEOUS MATTERS

A. *Relationship to Section 1231 of the Internal Revenue Code.*

The Commissioner's original position on the integration of

---

[125] Schirmer v. United States, 59-2 USTC ¶ 9572 (N.D. Calif. 1959); Winters v. United States, 58-1 USTC ¶ 9205 (N.D. Okla. 1958), *rev'd on other grounds,* 261 F.2d 675 (10th Cir. 1958), *cert. denied* 359 U.S. 943 (1959); Smith v. Commissioner, 19 F. Supp. 377 (D.N.H. 1937); Jane U. Elliott, 40 T.C. 304 (1963), *acq.* 1964-1 (Part 1) CUM. BULL. 4.

[126] David W. Murray, Jr., 21 CCH Tax Ct. Mem. 7 (1962); Richard E. Stein, 14 CCH Tax Ct. Mem. 191 (1955).

[127] *E.g.,* Mary F. Cary, 7 CCH Tax Ct. Mem. 724 (1948); Mary Cheney Davis, 16 B.T.A. 65 (1929), *acq.* VIII-2 CUM. BULL. 13 (1929).

[128] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 8 (March 1964); INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, PUB. NO. 334, TAX GUIDE FOR SMALL BUSINESS, p. 92 (1965).

[129] G.C.M. 16255, XV-1 CUM. BULL. 115 (1936); Gus S. Caras, 23 CCH Tax Ct. Mem. 1103 (1964) (dicta).

[130] Gus S. Caras, *supra* note 129. Ordinarily, if the taxpayer has $50 or $100 deductible collision insurance on an automobile, the amount of loss would be the $50 or $100, but under the new rules concerning $100 deductible floor, no loss would be allowable.

Int. Rev. Code of 1954 § 1231 (Section 117(j) of the 1939 Code) and 165 (Section 23(e) and (f) of the 1939 Code) was set forth in Treasury Regulation 118, Section 39.117(j)-1(a)(2):

> For the purpose of this section, the "involuntary conversion" of property is the conversion of such property into money or other property as a result of destruction in whole or in part, theft or seizure, or an exercise of the power of requisition or condemnation or the threat or imminence thereof. Losses upon the destruction in whole or in part, theft or seizure, requisition or condemnation of property are treated as losses upon an involuntary conversion whether or not there was a conversion of the property into money or other property. For example, if a capital asset held for more than six months, with an adjusted basis of $400, is stolen, and the loss from this theft is not compensated for by insurance or otherwise, the $400 loss is included in the computations under section 117(j).

Substantially the same language was incorporated in the initial regulations adopted under Int. Rev. Code of 1954 § 1231.[131] The Commissioner's position, however, has not gone without challenge. In *Maurer v. United States*,[132] and *Oppenheimer v. United States*,[133] both decided under the original regulation, the courts held that uninsured losses arising from the destruction (drought, windstorm) of ornamental trees and shrubs on residential property were deductible in full as casualty losses under Int. Rev. Code of 1954 § 165 and did not have to be first applied against Int. Rev. Code of 1954 § 1231 gains.

To alleviate the hardship of the Commissioner's interpretation,[134] Congress amended Int. Rev. Code of 1954 § 1231 (section 49 of the Technical Amendments Act of 1958) as follows:

> (a) TREATMENT AS ORDINARY LOSS. — Section 1231(a) (relating to property used in the trade or business and involuntary conversions) is amended by adding at the end thereof the following new sentence: "In the case of any property used in the trade or business and of any capital asset held for more than 6 months and held for the production of income, this subsection shall not apply to any loss, in respect of which the taxpayer is not compensated for by insurance in any amount, arising from fire, storm, shipwreck, or other casualty, or from theft."
>
> (b) EFFECTIVE DATE. — The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1957.

---

[131] See Treas. Reg. § 1.1231-1(e), 1957-2 CUM. BULL. 547, 550.

[132] 284 F.2d 122 (10th Cir. 1960), *reversing* 178 F. Supp. 223 (D. Kan. 1959). In Rev. Rul. 61-54, 1961-1 CUM. BULL. 398, the IRS announced that it will not follow the *Maurer* Case.

[133] 220 F. Supp. 194 (W.D. Mo. 1963).

[134] See S. Rep. No. 1983, 85th Cong., 2nd Sess. 74-75 (1958) 203-204.

Based upon the legislative history of the section,[135] the Commissioner amended Treasury Regulation § 1.1231-1(e)[136] to provide that section 1231 does not apply to losses arising with respect to ". . . both property used in the trade or business and any capital asset held for more than 6 months and held for the production of income, which losses arise from fire, storm, shipwreck, or other casualty, or from theft, and which are not compensated for by insurance in any amout. . . ."

In short, casualty losses arising from the destruction of capital assets held for personal uses (e.g., residential property) or assets used in trade or business or held for production of income which were partially insured must still be applied first to section 1231 gains.[137] This interpretation of the 1958 amendment has not, however, been accepted by the courts.[138]

B. *Personal Expenses Incident to Casualty*

The expenditure by a taxpayer of amounts for temporary hotel or apartment accommodations for the period during which his home was without heat, light, and/or other utilities or of amounts for the cost of temporary lights, fuel, and moving expenses, constitute personal expenses and may not be deducted as part of the casualty loss.[139] Amounts received through insurance for reimbursement of

---

[135] S. Rep. No. 1983, 85th Cong., 2nd Sess. 203-204 (1958):

> . . . The amendment applies with respect to, for example, loss incurred as the result of the destruction of a taxpayer's oil tanks which he used for oil storage in his trade or business, but on which he was unable to obtain insurance. On the other hand, the amendment does not apply to loss arising from the destruction of theft of the taxpayer's uninsured personal automobile. The amendment is intended to benefit business taxpayer who, because of the special hazards of their business or for other reasons, carry their own insurance. . . .

[136] T.D. 6394, 1959-2 CUM. BULL. 186, 187.

[137] J. H. Anderson, 7 CCH Tax Ct. Mem. 811 (1948); INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 15 (March 1964). See also Treas. Reg. § 1.1231-1(e) (1957), as amended, T.D. 6394, 1959-2 CUM. BULL. 186, 187.

[138] Morrison v. United States, 230 F. Supp. 989 (E.D. Tenn. 1964); Killebrew v. United States, 234 F. Supp. 481 (E.D. Tenn. 1964); Hall v. United States, 64-2 USTC ¶ 9770 (E.D. Tenn. 1964). In view of the favorable judicial outlook, taxpayers should claim all casualty losses in full as regular section 165 losses. See also H.R. 7502, 89th Cong., 1st Sess. (1965), which would amend INT. REV. CODE of 1954 § 1231(a) by adding this sentence:

> In the case of any involuntary conversion of property . . . which is attributable to a storm, flood, fire, or other casualty designated by the President of the United States as a major disaster . . . this subsection shall not apply to such involuntary conversion whether resulting in gain or loss, if during the taxable year, the recognized losses from such conversion exceed the recognized gains from such conversions.

See also H.R. Rep. No. 556, 89th Cong., 1st Sess. (1965), and Senate Finance Committee Amendments to H.R. 7502, 7 CCH 1965 STAND. FED. TAX REP. ¶ 6161B.

[139] Rev. Rul. 59-398, 1959-2 CUM. BULL. 76; INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 3 (March 1964); Richard A. Dow, 16 T.C. 1230 (1951) (cost of providing the household with water during four-month period when the well was polluted was not deductible).

family living expenses due to the loss of the use of a residence are taxable income and are not offset against the allowable amount of the casualty loss.[140]

C. *Computation of Net Operating Loss*

Casualty losses, whether or not involving business property, are treated as attributable to a trade or business for the purpose of computing the net operating loss for carryback and carryover purposes.[141] However, the $100 nondeductible portion of the loss must be excluded in the computation. As stated in H. R. Rep. No. 749:[142]

> Under section 172(d)(4)(C) of the code a personal casualty or theft loss is not treated as a nonbusiness expense for purposes of computing a net operating loss. The $100 floor applies in the computation of the net operating loss, but the net operating loss carried back or carried over is not again reduced in the year to which carried.

Losses arising from expropriations by the Cuban Government are treated as regular casualty losses for net operating loss purposes and not as expropriation losses under section 172(k).[143]

D. *Cleanup Expense*

If the taxpayer is relying upon the cost of repairs or replacements as evidence of the decrease in the market value of the property after the casualty, the cost figure used should include the expense incurred in cleaning up the debris.[144] On the other hand, if the taxpayer is relying on the testimony of experts to establish the relative market values, he should insure that the amount of diminution in fair market value testified to by his witnesses is measured just after the loss has taken place and before cleanup has begun. The expense of cleaning up should be added to this permanent loss in value.[145] If a taxpayer does not actually incur any expense in cleaning, as where, for example, he sells the property as is, presumably he should add to the permanent loss in value an estimate for cleanup expense. This is so because the price the taxpayer could

---

[140] Rev. Rul. 59-360, 1959-2 CUM. BULL. 75, INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 7 (March 1964).

[141] Treas. Reg. § 1.165-7(d) (1960); INT. REV. CODE of 1954 § 172(d)(4)(c); Treas. Reg. § 1.172-3(a)(3)(iii) (1956); INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 10 (March 1964).

[142] H.R. Rep. No. 749, 88th Cong., 1st Sess., p. A47 (1963); see also S. Rep. No. 830, 88th Cong., 2nd Sess., p. 210 (1964).

[143] INT. REV. CODE of 1954 § 165(i)(2)(c).

[144] INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 8 (March 1964).

[145] Ralph Walton, 20 CCH Tax Ct. Mem. 653 (1961); David W. Murray, Jr., 21 CCH Tax Ct. Mem. 7 (1962).

receive for the property immediately after the casualty would be its bargained-for value less the cost of cleaning up the damage.[146]

E. *Rehabilitation Payments — Disaster Relief*

Amounts received by the taxpayer from his employer or from disaster relief agencies, in the form of cash or property for the purpose of restoring or rehabilitating property lost or damaged in a disaster, reduces the amount of the deductible loss.[147] If the reimbursement exceeds the taxpayer's basis in the property prior to the casualty, the amount of the excess cannot be used to increase the basis of the property,[148] but such payments do not come within the concept of gross income and should not be included in the gross income of the recipients for income tax purposes.[149] Such amounts are deductible by the employer as business expenses.[150]

Disaster relief received in the form of food, medical supplies, and other forms of subsistence received by the taxpayer which are not replacements of lost or destroyed property do not reduce the amount of the casualty loss deduction and do not represent taxable income.[151] The same rule applies to cash gifts used to repair the property but not restricted to that purpose.[152]

F. *Use and Occupancy Insurance*

Use the occupancy insurance proceeds are not proceeds from casualty, to the extent that such proceeds are reimbursemnt for actual loss of net profit in the business. Such proceeds are income and are taxed in the same manner as the profits for which they are substituted would have been taxed.[153]

G. *Basis Adjustments*

The *Tax Guide for Small Business*[154] sets forth the following explanation of the adjustments which must be made to the basis of the property after a casualty:

> The basis of property damaged or destroyed by a casualty must be reduced by the allowable loss deduction. The basis must be

---

146 Ralph Walton, *supra* note 145.

147 INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 7 (Mafch 1964); Rev. Rul. 53-131, 1953-2 CUM. BULL. 112.

148 *Ibid.*

149 *Ibid.*

150 *Ibid.*

151 *Ibid.*

152 Rev. Rul. 64-329, 1964-2 CUM. BULL. 58.

153 INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, DOC. NO. 5174, DISASTERS, CASUALTIES AND THEFTS, p. 7 (March 1964).

154 INTERNAL REVENUE SERVICE, U.S. DEP'T OF TREASURY, PUB. NO. 334, TAX GUIDE FOR SMALL BUSINESS, p. 92 (1965). See, *e.g.*, Ferst v. Edwards, 129 F. Supp. 606 (D. Ga. 1955).

further reduced by the amount of any insurance or other compensation which you receive.

Example 1. Your truck is involved in an accident and, after appraisals have been made, you determine the loss to be $200. You carry $50 deductible insurance and receive $150 from the insurance company. Your deductible casualty loss is $50 ($200 less $150 insurance recovered). The basis of your truck must be reduced by the amount of your casualty loss, $50; it must further be reduced by the $150 of insurance received.

Example 2. Your building, which is partially destroyed by fire, has a basis of $15,000. Its value was $30,000 just before the fire and $20,000 immediately after, and you collected $10,000 insurance. You have no casualty loss deduction since your recovery was equal to the value of the destroyed portion. The basis of your building is reduced by $10,000, the amount of recovery.

Of course, amounts which are not business expenses paid or incurred to replace or restore property damaged or destroyed as a result of a casualty are capital expenditures and should be added to the remaining basis of the property. These adjustments are required to determine your adjusted basis of the property.

Books Received

DRAFTING A UNION CONTRACT. By LeRoy Marceau. Boston: Little, Brown and Co. 1965. Pp. 305. $12.50. A discussion of the essential background information, the necessary tools, and the practical techniques of drafting a union contract.

JUDICIAL CONTROL OF ADMINISTRATIVE ACTION. By Louis L. Jaffe. Boston: Little, Brown and Co. 1965. Pp. 792. $20.00. A synthesis of the welter of divergent point of view affecting the understanding of administrative action, this book by Professor Jaffe develops the thesis that the agencies and the courts, acting within the matrix of legislative delegation of power, are in a partnership of law-making and law applying.

PUBLIC LAW PERSPECTIVES ON A PRIVATE LAW PROBLEM: AUTO COMPENSATION PLANS. By Walter J. Blum and Harry Kalven, Jr. Boston: Little, Brown and Co. 1965. Pp. vii, 88. A discussion of the role of an auto compensation plan in the proper scope of liability for negligence resultants from the operation of automobiles.

WHEN YOU'RE 65 . . . OR THEREABOUTS. By CCS Editorial Staff. New York: Commerce Clearing House. 1965. Pp. 64. $1.00. A discussion of the special benefits afforded those aged 65 or thereabouts under the recently enacted medicare program, the federal social security program, and special federal income tax rules.