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ROYALTY OWNER RIGHTS UNDER DIVISION ORDERS

Si M. Bondurant*

I. INTRODUCTION

While there is considerable literature in various legal publications discussing the usage of division orders in the oil and gas industry,¹ most of it has been written from the vantage point of the purchaser of production. This is only natural because purchasers are more organized than royalty owners and deal on a daily basis with problems that arise from the purchase of oil and gas production. However, royalty owners are increasingly more sophisticated and cognizant of their rights and lately have become much more litigious. This Article will analyze the rights of royalty owners (royalty owners will be used interchangeably with lessors

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1. Bailey, *Division Orders*, 18 INST. ON MIN. L. 21 (1971) [hereinafter Bailey]; Bounds, *Division Orders*, 5 INST. ON OIL & GAS L. & TAX'N 91 (1954) [hereinafter Bounds]; Boyd, *Crude Oil Purchasing—Its Title Opinions and Division Orders*, 18 INST. ON OIL & GAS L. & TAX'N 233 (1965) [hereinafter Boyd]; Brannan, *Division Orders*, 8 E. MIN. L. INST. 12-1 (1987) [hereinafter Brannan]; Browder, *Estoppel, Waiver, and Ratification Affecting Mineral and Leasehold Rights*, 10 ROCKY MTN. MIN. L. INST. 139 (1965); Cabbage, *Royalty Problems Management*, 29 ROCKY MTN. MIN. L. INST. 691 (1983); Ethridge, *Oil and Gas Division Orders*, 19 MISS. L.J. 127 (1948) [hereinafter Ethridge]; Gregg, *Title Examination and Division Orders*, 19 INST. ON OIL & GAS L. & TAX'N 29 (1968) [hereinafter Gregg]; Hollimon, *Division Orders—A Primer*, 34 INST. ON OIL & GAS L. & TAX'N 313 (1983) [hereinafter Hollimon]; Hooper & Schleier, *Current Use and Effect of Division and Transfer Orders*, 18 S. TEX. L.J. 531 (1977) [hereinafter Hooper & Schleier]; Knowlton & Morrow, *Division Orders: Contract, Distribution Mechanism, and Curative Tool*, in INST. ON OIL AND GAS AGREEMENTS 12-1 (1983); Lange, *The Production of Oil and Gas and Some of the Problems Reached by It*, 22 INST. ON OIL & GAS L. & TAX'N 113 (1971); Lear, *First Purchaser Suspense Accounts*, 33 ROCKY MTN. MIN. L. INST. 17-1 (1988); Pierce, *Resolving Division Order Disputes: A Conceptual Approach*, 35 ROCKY MTN. MIN. L. INST. 3-1 (1990) [hereinafter Pierce]; Rain, *A Further Look at Division Orders and Problems in Accounting and Payment of Proceeds from Oil and Gas*, 8 ROCKY MTN. MIN. L. INST. 69 (1963) [hereinafter Rain]; Twenhafel, *Oil-Gas Division Orders: Their Origin, Varieties, and Usage*, 27B ROCKY MTN. MIN. L. INST. 1479 (1982) [hereinafter Twenhafel].

throughout this Article) as sellers of production and how those rights may be affected by the execution of oil and gas division orders.

II. HISTORY OF THE DIVISION ORDER

There is no authoritative source for the origin of the division order in any of the literature on the subject. Division orders apparently were in common use by the turn of the century.² We do know that the division order originated in the early days of the oil industry when oil was the primary product sold. It was sold to third-party purchasers who were neither operators nor owners of any of the oil and gas interests and who were in the business of buying crude oil as a raw material for the refining business.³ Crude oil at that time was marketed primarily through pipelines and later railroads and eventually trucks which purchased the oil at the well and hauled for hire the production to market. Generally, the purchasers would assume the responsibility of distributing the proceeds to the owners.⁴ The purchasers developed the division order to provide protection from liability in making distribution of proceeds from production.⁵ The nature of the relationship, between a third-party purchaser making payment to working interest owners and royalty owners, should be kept in mind when reading many of the early cases construing division orders as this relationship is often not clearly set out.

Over the years, the nature of selling and marketing production has changed. In today's typical marketing arrangement, the operator will often be the party responsible for distributing proceeds from the sale of production. Frequently, several working interest owners will separately market production. Thus, royalty owners may receive payments from several different parties under several different division orders.⁶

III. DEFINITION OF DIVISION ORDER

There is no unanimity as to precisely what a division order is or how to define one. While there is a general consensus that the purpose of a

2. *Nonamaker v. Amos*, 76 N.E. 949 (Ohio 1905); *Childers v. Neely*, 47 W. Va. 70, 34 S.E. 828 (1899).

3. Hooper & Schleier, *supra* note 1, at 532. See generally Twenhafel, *supra* note 1, at 1483-89.

4. Hooper & Schleier, *supra* note 1, at 532.

5. Hooper & Schleier, *supra* note 1, at 532.

6. This type of situation can give rise to an array of problems. See Smith, *Gas Marketing By Co-Owners: Disproportionate Sales, Gas Imbalances and Lessors' Claims to Royalty*, 39 BAYLOR L. REV. 365 (1987).

division order is to facilitate the sale of oil and/or gas to a purchaser,⁷ there is considerable confusion over the legal relationships of the parties to a division order,⁸ and the division order's effect as a legal instrument.⁹ It has been defined by courts and commentators as:

[T]he contract under which the production is purchased or accepted for transportation by the pipe line company.¹⁰

[T]he operative instrument of transfer, whether called a contract or not, and until revoked is binding on the parties, who thereunder declare their present ability and intent to transfer, sell, or otherwise dispose of the oil to the pipeline, and their entitlement to payment for this same transfer.¹¹

[A] continuing order or direction to the purchaser to receive the production and account for it on the terms stated to the persons who execute the division order in the proportions set opposite the seller's name until some different direction is given.¹²

[A]n order to the person or company purchasing the production from the land directing that person or company to make payment for the value of the products taken in the proportions set out in the division order.¹³

It has been described variously as an executed, bilateral contract,¹⁴ a unilateral contract,¹⁵ an element of a contract,¹⁶ and not really a contract.¹⁷ The differences in definitions and descriptions stem partially from the fact that there are various types of division orders in existence, and that the relationship of the parties determines the type of division order used. There is no standard division order and the relationship of the parties must always be considered when interpreting these instruments. The courts have not always clearly understood this. While there is no authoritative definition of a division order, it is, broadly stated, the

7. See Brannan, *supra* note 1, at 12-3; Gregg, *supra* note 1, at 29-30; Hollimon, *supra* note 1, at 313-14.

8. See Ethridge, *supra* note 1, at 130 ("The courts . . . [by 1948] have not formulated a clear and precise analysis of an order's contractual nature and the juridical facts occurring subsequent to its execution."). They still haven't some 40 years later. See Smith, *Royalty Issues: Take-or-Pay Claims and Division Orders*, 24 TULSA L.J. 509, 535 (1989) ("There are too many cases saying too many things without clearly articulating the legal theories used.").

9. Compare *Holmes v. Kewanee Oil Co.*, 233 Kan. 544, 664 P.2d 1335 (1983), *cert. denied*, 474 U.S. 953 (1985) with *Exxon Corp. v. Middleton*, 613 S.W.2d 240 (Tex. 1981).

10. *Stanlind Oil & Gas Co. v. Terrell*, 183 S.W.2d 743, 745 (Tex. Civ. App. 1944 writ ref'd.).

11. *Pan Am. Petroleum Corp. v. Long*, 340 F.2d 211, 223 (5th Cir. 1964), *cert. denied*, 381 U.S. 926 (1965).

12. Gregg, *supra* note 1, at 29-30.

13. Bounds, *supra* note 1, at 91.

14. See Ethridge, *supra* note 1, at 131 & n.10 and cases cited therein.

15. Ethridge, *supra* note 1, at 133.

16. *Wolfe v. Prairie Oil & Gas Co.*, 83 F.2d 434 (10th Cir. 1936) (by implication).

17. Hooper & Schleier, *supra* note 1, at 533.

instrument through which an interest owner authorizes another party to make distribution of the proceeds from the sale of production.

IV. TYPES OF DIVISION ORDERS

There are three basic types of division orders. The first type is the standard third-party purchaser division order. This is a division order from both lessor and lessee directed to a third-party purchaser who assumes the responsibility for disbursing proceeds from production directly to the royalty owner and the working interest owner for their respective shares of proceeds. This was the form of division order that was standard in the early days of the industry.¹⁸ These division orders will generally require that the owners furnish abstracts of title for examination by the purchaser's attorney. However, this is rarely demanded anymore because purchasers over the years have come to rely on title opinions from outside attorneys. This type of division order sets out the basic terms of the contract for sale and purchase between the parties in the absence of a written sales contract. Generally, a third-party purchaser will initially purchase the oil under an oral agreement and division orders will be issued subsequently. This type of division order was established primarily to protect the purchaser of production for payments made to the interest owners and is generally used only for the sale of oil.

The second type is an indemnity division order. This is a division order from the lessee to the purchaser, whereupon the purchaser pays the lessee for 100% of the production and the lessee assumes the responsibility for disbursing royalties. This type of division order has become much more common in recent years as the method of marketing oil and gas has evolved. The burdens of ascertaining title, reconciling accounts and effecting settlements of proceeds for the royalty owners are shifted from the third-party purchaser to the lessee/operator. When the lessee/operator is selling 100% of the production, there will generally be a written sales contract between the lessee/operator and the purchaser. One commentator has noted that the practice of the industry has relegated this type of division order to nothing more than a stipulation of interest and that in all probability, the division order has no legal, practical or logical role, except for stipulations of interest among separate sellers.¹⁹

The third type of division order is the lessee/purchaser division order. This type of division order is a direction from the royalty owner to

18. Twenhafel, *supra* note 1, at 1498-99.

19. Twenhafel, *supra* note 1, at 1500.

the lessee to assume responsibility for disbursing proceeds to the royalty owner. In most instances, lessees have simply adopted the forms of third-party purchaser division orders, inserting their names in place of the names of third-party purchasers.²⁰ The division orders have not been properly crafted to distinguish between the dual role of the lessee/purchaser and the solitary role of the third-party purchaser. This type of division order has been in common use in connection with sales of gas for many years and is now probably the most frequently used division order for both oil and gas.

In addition to the three basic types of division orders described above, a distinction should be made between division orders governing the sale of oil and those governing the sale of natural gas. Sometimes they will be issued separately, and sometimes one division order will cover both products.

V. RIGHTS OF ROYALTY OWNERS AS SELLERS OF PRODUCTION

A. *The Lease As the Basic Contract*

As between a lessor and lessee, the lease is the basic contract for the sale of the royalty owner's share of production and contains the terms that control this sale.²¹ Standard form leases generally provide different rights to royalty owners for oil production sold as opposed to gas production. Usually, the lease will provide that the lessor reserves a fractional share of the oil which the lessee agrees to deliver to the credit of the lessor in the pipeline or other connection to the lessee's well. Frequently, the oil royalty clause will authorize the lessee to purchase the lessor's share of oil royalty at the posted market price. In contrast, the standard gas royalty clause reserves to the lessor a fractional share of the proceeds or market value of the gas produced, sold or used. Under this type of reservation, title to all of the gas vests in the lessee and the lessor has only a monetary claim.²²

The lease form most commonly in use in the Gulf Coast region today contains the following provisions for royalty on oil and gas:

As royalty, lessee covenants and agrees: (a) To deliver to the credit of lessor, in the pipe line to which lessee may connect its wells, the equal one-eighth part of all oil produced and saved by lessee from said land, or from time to time, at the option of lessee, to pay lessor the average

20. Twenhafel, *supra* note 1, at 1501.

21. Rain, *supra* note 1, at 77; Twenhafel, *supra* note 1, at 1503-04.

22. See Gregg, *supra* note 1, at 31.

posted market price of such one-eighth part of such oil at the wells as of the day it is run to the pipe line or storage tanks, lessor's interest, in either case, to bear one-eighth of the cost of treating oil to render it marketable pipe line oil.

(b) To pay lessor on gas and casinghead gas produced from said land (1) when sold by lessee, one-eighth of the amount realized by lessee, computed at the mouth of the well, or (2) when used by lessee off said land or in the manufacture of gasoline or other products, the market value, at the mouth of the well, of one-eighth of such gas and casinghead gas.²³

As can be seen by an examination of the above clauses, the lessor has a right to take oil royalty in kind because the lessee agrees to *deliver* oil to the credit of lessor to the stated point, but as to gas agrees to *pay* lessor only for the gas sold or used. While there are many variants in oil and gas royalty clauses in the various leases still in common use today, virtually all standard form leases contain the same distinction in treatment of royalty for oil and royalty for gas. Most modern forms, such as the one above, give an option to the lessee to pay for royalty oil. In addition, it is generally held that the lessee has not only the right, but the obligation to market the oil on the lessor's behalf should he refuse to take his royalty oil in kind.²⁴

B. *Necessity of Execution of Division Order As Prerequisite for Receiving Payment*

When the lessee is also the purchaser and has issued division orders, it appears to be the consensus of those who have addressed the issue that there is no necessity for the royalty owner to execute a division order prior to receiving payment for royalties unless the lease specifically requires it.²⁵ There really should be little dissent from this proposition. The lease is a binding contract between lessor and lessee which establishes the obligation of the lessee to account to his lessor for royalty. The lease contract establishes the rights of the parties and contains the protections that are necessary for the lessee in his dual role as purchaser and lessee.

23. PRODUCERS FORM 88 (9-70) WITH POOLING PROVISION (Hederman Bros. Jackson, Miss.) (for use in Mississippi, Alabama, and Florida).

24. Lear, *supra* note 1, at 17-6 (citing Wolfe v. Texas Co., 83 F.2d 425, 430 (10th Cir.), *cert. denied*, 299 U.S. 553 (1936), and Cook v. Tompkins, 713 S.W.2d 417, 421 (Tex. App.—Eastland 1986)); Pierce, *supra* note 1, at 3-7.

25. TXO Prod. Corp. v. Page Farms, Inc., 287 Ark. 304, 698 S.W.2d 791 (1985); Boyd, *supra* note 1, at 256; Brannan, *supra* note 1, at 12-11; Holliman, *supra* note 1, at 332.

There is a sharp division of opinion as to the necessity of the execution of a division order by royalty owners as a prerequisite to receiving payment for production sold to a third-party purchaser. Advocacy groups for royalty owners vehemently proclaim that there is no necessity for a royalty owner to execute to anyone a division order that is anything more than a stipulation of interest.²⁶ Purchasing companies and their attorneys are adamant that there is no obligation for a third-party purchaser to pay any royalty owner in the absence of an executed division order acceptable to the purchaser.²⁷

Purchasers argue that the purchaser is a stranger to the lease and has no contractual relationship with the royalty owner except through its division orders. They contend that they are lawfully in possession of the oil by virtue of its delivery from the lessee as agent for the royalty owner, but that no payment is due until a division order is executed pursuant to the custom and usage in the industry. Royalty owners generally respond that they cannot be forced to sign a division order which might diminish their rights because they are not required to do so by their leases.

There appear to be only two reported decisions on the issue of whether a royalty owner can be required to sign a division order to a third-party purchaser in order to receive royalty payments. The cases are split and neither may have great influence outside its jurisdiction.

The Ohio Supreme Court in *Blausey v. Stein*,²⁸ confronted a situation in which a lessor had sued her lessee to cancel a lease based on cessation of production and failure to pay royalty. The lessor had refused to sign division orders as a prerequisite to receiving royalty payments. The court disposed of the issue of the division orders in the following language:

A division order is a direction and authorization to the purchaser of oil to distribute the purchase price in a specified manner. Its purpose is to assure that the purchaser pays only those parties who are entitled to payment. . . . By signing the division order, the lessor is simply verifying that he has a right to royalty payments.

The record indicates that appellant has refused to sign a division

26. The National Association of Royalty Owners (NARO) has long advocated this position and strongly supported the royalty owner plaintiffs in *Hull v. Sun Refining & Marketing Co.*, 60 OKLA. B.J. 2358 (October 7, 1989) (1989 WL 109791).

27. See Appellant's Brief in Chief at 10-11, and Brief of Amicus Curiae Koch Oil Co. at 7-12, *Hull v. Sun Refining & Marketing Co.*, 60 OKLA. B.J. 2358 (October 7, 1989) (1989 WL 109791) (No. 71, 179); See also *Boyd*, *supra* note 1, at 262-63; *Brannan*, *supra* note 1, at 12-12 to -13; *Holliman*, *supra* note 1, at 332-33; *Twenhafel*, *supra* note 1, at 1508-10.

28. 61 Ohio St. 2d 264, 400 N.E.2d 408 (1980). The opinion does not explicitly state that the division orders were tendered by a third-party purchaser but implies as much.

order for the oil sold by appellee in 1975. Because of her refusal, the purchaser has not tendered payment for accrued royalties. . . . We hold that the requirement that appellant execute a division order prior to receiving her royalty payments does not contravene any specific provision of the lease, and is not such a burden that it can be considered an attempted modification of the lease.²⁹

The court in *Blausey* failed to cite authorities or support its holding with reasoned arguments. The opinion ignores a large body of law which holds that a lessor may be doing far more by executing a division order than "simply verifying that he has a right to royalty payments."³⁰ Thus, it is doubtful that *Blausey* will have much effect outside the State of Ohio.

The second case, *Hull v. Sun Refining & Marketing Co.*,³¹ was recently decided by the Oklahoma Supreme Court in favor of the royalty owner. In *Sun*, the royalty owners had clear and undisputed title to both the surface and the mineral interests to the property in question. They executed a lease with a royalty provision requiring the lessee to deliver the equal one-fourth part of all oil produced and saved from the leased premises to the lessors' credit. The lessors made no independent arrangements to sell their oil or take their oil in kind. Their lessee, on his own behalf and as agent for the lessors, entered into an oral sale and purchase agreement with Sun for the sale and purchase of oil from the well.³² Sun contended that long-standing custom and practice in the industry implied that all owners in the well would have to sign a standard industry division order acceptable to Sun before being entitled to receive payment for production.³³ The lessors refused to sign the standard form division order tendered by Sun. In response to objections voiced by the lessors, Sun prepared a new division order.³⁴ The lessors refused to sign the revised division order and tendered to Sun a stipulation and division of interest form. Sun rejected this substituted "division order" because it failed to specify the terms of the purchase to Sun's satisfaction and did

29. *Id.* at 267, 400 N.E.2d at 410-11 (citations omitted).

30. *Id.* at 267, 400 N.E.2d at 410. See, e.g., *Murdock v. Pure-Lively Energy 1981-A, Ltd.*, 108 N.M. 575, 775 P.2d 1292 (1989) (royalty owner by execution of division order waived any claim to interest on suspended funds); *Puckett v. First City Nat. Bank*, 702 S.W.2d 232 (Tex. App.—Eastland 1985, writ ref'd n.r.e.) (division order changed basis for calculating royalty from market value to proceeds). See *infra* note 129.

31. 60 OKLA. B.J. 2358 (October 7, 1989) (1989 WL 109791).

32. Sun is a third-party purchaser and is in no way affiliated with the lessee of the royalty owners.

33. See Appellant's Brief in Chief, *supra* note 27, at 10-12.

34. See Appellant's Brief in Chief, *supra* note 27, at 5.

not warrant title to the oil. Sun suspended all payments to the lessors for their royalty oil, and the lessors sued.

The trial court split the baby in half, holding that the lessors did not have to execute either of the division orders tendered by Sun to be legally entitled to the suspended proceeds, but that the stipulation of interest submitted to Sun was insufficient to require Sun to pay.³⁵ The trial court listed ten terms that a division order must contain to entitle a royalty owner to receive payment and held that the royalty owners must be paid upon the execution of the "court approved" division order.³⁶ Both sides appealed.

Sun framed the major issue in the case as follows:

This case only involves the situation where a third-party oil purchaser with no prior relationship to the royalty owner seeks to require the royalty owner to execute a division order prior to being entitled to receive payment for proceeds of production, all in accordance with the oil purchase contract and the custom of the oil purchasing industry.³⁷

Sun argued that the lessee, as agent of the lessors, has implied authority to sell the royalty owner's oil and to include as part of the contract of sale the requirement that the royalty owner execute a division order to the oil purchaser.³⁸ The division order would include terms and provisions acceptable to the purchaser so long as said terms were neither unlawful nor unconscionable and were consistent with standard industry practice and usage of the trade.³⁹

35. *Hull v. Sun Refining & Marketing Co.*, No. 86-327 (Dist. Ct. of Seminole County, Okla.)

36. The terms that the Oklahoma trial court felt were essential to a division order are:

- a. Purchaser's name and address
- b. Effective date of purchase
- c. Lease/unit/property name
- d. Description of property
- e. Warranty
- f. Reference to payments in accordance with federal and state laws
- g. Notice of change of ownership
- h. Division of interest
- i. Name, address and tax I.D. number of interest owner
- j. Signature of interest owner

Id.

37. Appellant's Brief in Chief, *supra* note 27, at 13.

38. Appellant's Brief in Chief, *supra* note 27, at 6-8.

39. Appellant's Brief in Chief, *supra* note 27, at 20-22. The test proposed by Sun would subject royalty owners to treatment as merchants under the Uniform Commercial Code and impute to them knowledge of custom and usage in the industry, something other courts have recently refused to do. *See, e.g., Piney Woods Country Life School v. Shell Oil Co.*, 726 F.2d 225, 236 (5th Cir. 1984), *cert. denied*, 471 U.S. 1005 (1985); *TXO Prod. Corp. v. Page Farms, Inc.*, 287 Ark. 304, 698 S.W.2d 791, 792 (1985). *But see Wolfe v. Shell Petroleum Corp.*, 83 F.2d 438 (10th Cir.), *cert. denied*, 299 U.S. 553 (1936); *Wolfe v. Texas Co.*, 83 F.2d 425 (10th Cir.), *cert. denied*, 299 U.S. 553 (1936).

The lessors countered that their lease established the terms under which their royalty payments were due and the scope of the authority granted the lessee to sell to the purchaser the royalty owner's oil.⁴⁰ They agreed that the purchaser had a valid contract to purchase 100% of the production from the well pursuant to its contract with the lessee. They contended that there was no need for a separate contract between the purchaser and the royalty owner. Because the purchaser assumed the obligation to pay royalty owners directly, it must comply with the lease provisions in making this payment.⁴¹ The royalty owners then argued that the lessee cannot do indirectly what it cannot do directly; the lessee "cannot require the lessor to execute a division order and cannot, by entering into an oil purchase contract, give the purchaser the right to require the lessor to execute one."⁴²

The Oklahoma Supreme Court, by a vote of 6-3, ruled in favor of the royalty owners on rather narrow grounds, holding *inter alia* that under title 52, section 540 of the Oklahoma Statutes, the failure to execute a division order does not justify suspension of royalties in the absence of unmarketable title, and that the agent lessee could not bind the principal-lessor to a trade usage requiring execution of a division order as it was against public policy.⁴³ The court construed the Oklahoma statute to allow suspension of royalty payments only when a legitimate question as to marketability of title existed.⁴⁴ The court found that the statute required payment of royalty proceeds within the stated time if title were marketable, and therefore, that requiring the execution of a division order as a condition precedent to payment violated the terms of the statute.⁴⁵

40. Appellees/Cross-Appellants' Answer Brief and Brief in Chief at 21, *Hull v. Sun Refining and Marketing Co.*, 60 OKLA. B.J. 2358 (Oct. 7, 1989) (1989 WL 109791) (No. 71,179).

41. *Id.*

42. *Id.*

43. *Hull v. Sun Refining and Marketing Co.*, 60 OKLA. B.J. 2358, 2361 (Oct. 7, 1989) (1989 WL 109791).

44. *Id.*

45. *Id.* The court noted that title 52, section 540 of the Oklahoma Statutes was amended effective July 1, 1989, and refused to express an opinion concerning the effect the amendment might have on future cases questioning execution of division orders as a precedent to payment. *Id.* at 2363 n. 7. The dissent felt that the amendment will require division orders to be executed in the future in Oklahoma for a person to be legally entitled to receive payment. The dissenters declared that the effect of the majority opinion is to create a four year "window" (1985-89) during which the law deviates from preceding and succeeding law. *Id.* at 2364. The amendment added the following language:

B. A division order is an instrument for the purpose of directing the distribution of proceeds from the sale of oil, gas, casinghead gas or other related hydrocarbons which warrants in writing the division of interest and the name, address and tax identification

Though the court's holding was in favor of the royalty owners, the opinion is not without fodder for future fights by purchasers in jurisdictions which have no payment statutes similar to Oklahoma's. The court found that under the common law, it was a recognized custom and usage of the oil and gas industry that royalty holders execute division orders before receiving royalty payments.⁴⁶ The court also noted that division orders are binding upon royalty owners until revoked, even though the division order may abrogate or alter rights under the lease.⁴⁷ The court reasoned that under these circumstances, purchasers could force acquiescence to conditions unfavorable to royalty owners by threatening to withhold payments under a pretext of complying with custom and usage.⁴⁸ The court held that such custom and usage was repugnant to the express provisions of the Oklahoma statute and, therefore, void.⁴⁹

The court only briefly focused on the issue of the lessee's agency authority. The court brushed aside this issue, stating that the power of an agent to bind its principal "does not extend to customs and usages which are either illegal or contrary to public policy."⁵⁰ The court found the requirement that a lessor execute a division order before receiving royalty payment to be violative of the public policy as announced in title 52, section 540 of the Oklahoma Statutes, and any such custom and usage could not survive its enactment.⁵¹

The court's holding is grounded in its interpretation of who is "legally entitled" to receive royalty payments under the Oklahoma statute. Finding that anyone whose title is marketable is legally entitled to receive royalty payments, the court disposes of the other issues based on its statutory interpretation.⁵² Thus, the court's opinion is of limited analytical

number of such interest owner with a provision requiring notice of change of ownership. A division order is executed to enable the purchaser of the production from the leasehold to make remittance directly to the interest owners for their royalty interest, and is not intended to and does not relieve the lessee of any liabilities or obligations under the oil and gas lease. A division order which varies the terms of any oil and gas lease is invalid to the extent of the variance unless those changes have been previously agreed to by the affected parties. This subsection shall only apply to division orders executed on or after July 1, 1989.

S.107, 42nd Leg., 1989 Okla. Sess. Laws ch. 241, codified as amended at OKLA. STAT. tit. 52, § 540(B) (Supp. 1989) (repealing OKLA. STAT. tit. 52, §§ 567, 568 (Supp. 1988)).

This language is basically a legislative compromise between the opposing forces in the *Sun* case.

46. *Sun*, 60 OKLA. B.J. at 2361.

47. *Id.*

48. *Id.*

49. *Id.*

50. *Id.* at 2362.

51. *Id.*

52. *Id.* at 2361.

value for resolving future disputes as it does not address the process by which division orders are formed, the nature of the instrument or the scope of authority of the lessee as agent for the royalty owners.⁵³ The opinion will probably be used by royalty owners to support their position that division orders are not required to be executed as a precedent to receiving royalty payment in states where statutes like Oklahoma's exist, and by purchasers to support their position that the common law requires that division orders be executed prior to receiving royalty payments pursuant to trade custom and usage in the industry. The Oklahoma Supreme Court did the Texas two-step, avoiding any decision of the hard issues and providing the practitioner with little guidance for resolving future disputes.

VI. EFFECT OF EXECUTION OF DIVISION ORDERS

A. *Common Elements of a Division Order*

To a large extent, the effect of the execution of a division order depends on the covenants, terms, and provisions of the division order.⁵⁴ While there currently exists no standard or model form division order, there are core terms that have remained relatively constant over the years.⁵⁵ Core terms found in virtually every division order are as follows:

- (1) A warranty or certification of the title of the owner to the interest shown in the division order;
- (2) Terms relating to the delivery of the product and transfer of title to purchaser;
- (3) Terms setting forth the price and the time and method of payment;
- (4) A description of the property covered by the division order;
- (5) Provisions for furnishing evidence of title and granting the purchaser the right to suspend payment in the event of conflicting claims; and
- (6) Provisions requiring the owner to provide the purchaser with written notice of changes or transfers of ownership.⁵⁶

53. Professor David E. Pierce expressed his hope that the court would use this case to expound upon these more difficult issues. Pierce, *supra* note 1, at 3-27.

54. See *Bankers Life Ins. Co. v. Scurlock Oil Co.*, 447 F.2d 997, 1003 n.9 (5th Cir. 1971); Lowe, *Developments In Non-Regulatory Oil and Gas Law*, 39 INST. ON OIL & GAS L. & TAX'N 1-1, 1-21 to -22 (1988).

55. Compare Ethridge, *supra* note 1, at 129-30 with Holliman, *supra* note 1, at 316.

56. See Brannan *supra* note 1, at 12-9 to -10; Holliman, *supra* note 1, at 316; Hooper & Schleier, *supra* note 1, at 542-43; Twenhafel, *supra* note 1, at 1488-89.

In addition to the above terms, most division orders in current use also contain language purporting to ratify the lease and perhaps the gas contract, minimum payment provisions, specific terms as to revocability, terms that bind the parties to the division order regardless of whether all of the named interest owners sign, authorization to make certain deductions from the purchase price, and provisions extending the division order to the heirs, successors and assigns of the parties executing it.⁵⁷ Although the basic terms of the division order have remained unchanged over at least the last fifty years, the division order itself seems to have grown and lengthened with the body of case law interpreting the rights of purchasers and sellers of production. As certain problems arise through litigation, such as the obligation to pay royalty based on market value, new clauses have been added in an attempt to deal with these problems through the terms of the division order. Seldom are any clauses deleted.⁵⁸

B. *Revocability of Division Orders*

As a general rule, most division orders are by their specific language made revocable at the will of either party. This is almost universally true as to division orders covering the purchase of oil. Some will provide forty-eight hours notice and others, thirty or sixty days notice. Commonly, oil division orders will begin with the language "until further written notice from you or from the undersigned" you are entitled to purchase the interest covered by the division order. When the language of the division order itself clearly manifests the parties' intention that it may be revocable by either party, this intention will be enforced by the courts.⁵⁹

When the division order by its terms is not explicitly made revocable, however, the cases are not so clear as to a royalty owner's right to revoke a division order. Gas division orders, in particular, will frequently provide that they shall be in force and effect for a stated period of time, for the life of the lease, or so long as the gas sales contract is in

57. See Brannan *supra* note 1, at 12-9 to -10; Holliman, *supra* note 1, at 316; Hooper & Schleier, *supra* note 1, at 542-43; Twenhafel, *supra* note 1, at 1488-89.

58. Most division orders still retain a clause requiring that full and complete abstracts of title be furnished by the seller upon the request of the purchaser though purchasers have relied on Division Order Title Opinions from outside attorneys for years and most sellers no longer have abstracts of their property. Also, virtually every division order currently in use in Mississippi and Alabama retains the clause authorizing the purchaser to withhold money without interest even though this is prohibited by statutes in both states.

59. See Boyd, *supra* note 1, at 256; Holliman, *supra* note 1, at 320-21.

effect. There are several cases in various jurisdictions that hold that division orders can be made irrevocable, either by the specific language of the division order or by the language coupled with the actions of the parties.⁶⁰ However, more recent decisions in Texas have apparently found this line of authority unpersuasive.⁶¹ In *Exxon Corp. v. Middleton*,⁶² some of the division orders at issue expressly provided that they would remain in effect for the life of the leases and set out the formula to be used in calculating royalties for gas proceeds to be distributed pursuant to the division order.⁶³ The Texas Court of Civil Appeals ruled that the division orders were valid written agreements modifying the gas royalty clause of the lease and that the royalty owners were not entitled to revoke or rescind the orders unilaterally.⁶⁴ The Supreme Court reversed the Court of Appeals without any discussion as to the issue of whether some of the division orders had been made irrevocable. The court declared that the division orders had been revoked by the filing of suit by the royalty owners, but that the lessees to whom the division orders were directed were protected as to royalty settlements made until such revocation.⁶⁵ The court noted that the division orders did not refer to any specific gas contracts and simply declared that they were revocable at will. The court failed to state why.

C. *Payments Made Pursuant to Division Orders*

As a general rule payments made pursuant to a division order, whether by third-party purchasers or lessees, are binding upon the royalty interest owner until the division order is revoked, at least to the extent that all funds due the royalty interest owners have been paid out to others.⁶⁶ Although in such situations the purchaser will be protected, a

60. *Union Producing Co. v. Driskell*, 117 F.2d 229 (5th Cir. 1941) (gas division order which specifically provided that royalty owner's gas was to be sold to pipeline; lessee drilled additional wells in reliance thereon); *Simpson v. United Gas Pipe Line Co.*, 196 Miss. 356, 17 So. 2d 200 (1944) (gas division order incorporating gas sales contract executed to third party purchaser who relied and acted thereon); *Headley v. Hoopergarner*, 60 W. Va. 626, 55 S.E. 744 (1906) (oil division order—no terms of instrument given). The court's analysis in *Simpson* was criticized by Judge Ethridge in his seminal article on division orders. See Ethridge, *supra* note 1. Also, the courts in both *Simpson* and *Union Producing Co.* appear to have based their decisions primarily on the actions of the parties in reliance on the division orders.

61. See, e.g., *Exxon Corp. v. Middleton*, 613 S.W.2d 240 (Tex. 1981); *Butler v. Exxon Corp.*, 559 S.W.2d 410 (Tex. Civ. App.—El Paso 1977, writ ref'd n.r.e.).

62. 613 S.W.2d 240 (Tex. 1981).

63. *Id.* at 247-250.

64. *Id.* at 250.

65. *Id.* at 250-51.

66. See, e.g., *Dale v. Case*, 217 Miss. 298, 64 So. 2d 344 (1953); *Cabot Corp. v. Brown*, 754 S.W.2d 104 (Tex. 1987); *Exxon Corp. v. Middleton*, 613 S.W.2d 240 (Tex. 1981); *Chicago Corp. v.*

royalty owner who has executed a division order that credits the royalty owner with a lesser interest than is actually owned may assert a claim for unjust enrichment against the party who was overpaid.⁶⁷

In a recent decision by the Texas Supreme Court, *Gavenda v. Strata Energy, Inc.*,⁶⁸ the Texas Supreme Court modified the general rule that settlements made pursuant to division orders are binding until the division orders are revoked. In *Gavenda*, the landowner had conveyed a tract of land reserving an undivided one-half non-participating term royalty interest in the property. The holder of the executive rights subsequently executed an oil and gas lease providing for a lessor's royalty of one-eighth. Division orders were prepared by the lessee/operator which erroneously credited the Gavendas with an undivided one-sixteenth royalty interest rather than a one-half royalty interest pursuant to a division order title opinion by the lessee's attorney. The Gavendas executed the division orders and accepted payment thereunder for several years. Two days before the Gavendas' term royalty interest was to expire, the Gavendas revoked the division order and subsequently filed suit demanding payment of some \$2.4 million in underpaid royalties owed them under the one-half term royalty interest reserved by them.⁶⁹ The parties stipulated that the deed reserved a full one-half royalty, or one-half of gross production. The operator, Strata, had apparently sold some overriding royalty and some of its working interest ownership.

The Texas Supreme Court stated that the only issue was whether, under the facts of the case, the division orders were binding until revoked.⁷⁰ The Texas Supreme Court reviewed its general jurisprudence that division orders bind underpaid royalty owners until they are revoked. The court explained that the reasoning underlying this rule was the detrimental reliance of the purchasers and operators and declared that when the purchaser or operator has paid out all of the proceeds owed pursuant to the division orders, but errs in the distribution of these

Wall, 156 Tex. 217, 293 S.W.2d 844 (1956). *But see* *Holmes v. Kewanee Oil Co.*, 233 Kan. 544, 664 P.2d 1335 (1983), *cert. denied*, 474 U.S. 953 (1985) and *Maddox v. Gulf Oil Corp.*, 222 Kan. 733, 567 P.2d 1326 (1977), *cert. denied*, 434 U.S. 1065 (1978) (execution of division orders which attempt to alter the lease provisions will not deprive the royalty owner of the amounts due under the lease—Kansas is an exception to the general rule).

67. *Hershey v. Hershey*, 3 Ill. App. 2d 307, 122 N.E.2d 69 (1954); *Dale v. Case*, 217 Miss. 298, 64 So. 2d 344 (1953); *Hafeman v. Gem Oil Co.*, 163 Neb. 438, 80 N.W.2d 139 (1956). Of course, the overpaid party may still be able to interpose equitable defenses such as waiver, estoppel and laches against any claim should the facts warrant them.

68. 705 S.W.2d 690 (Tex. 1986).

69. *Id.* at 691.

70. *Id.* at 690.

proceeds, it should be protected from any double liability for the amount of the overpayment.⁷¹ The court stated that because the purchasers and operators have relied on the division order representations without personal benefit from the errors, they should be protected. In such circumstances, no unjust enrichment exists.⁷² However, applying the law to the facts of the *Gavenda* case, the Texas Supreme Court held that the division orders and the payments made pursuant thereto were not binding on the Gavendas:

Strata both erroneously prepared the division and transfer orders and distributed the royalties. Because of its error, Strata underpaid the Gavenda family by 7/16th royalty, retaining part of the 7/16th royalty for itself. It profited, unlike the operators in *Exxon v. Middleton*, at the royalty owner's expense. It retained for itself . . . part of the proceeds owed to the royalty owners. Therefore, Strata is liable to the Gavendas for whatever portion of their royalties it retained, although it is not liable to the Gavendas for any of their royalties it paid out to various overriding or other royalty owners.⁷³

After remand, the Court of Appeals declined to give Strata credit for payments to overriding royalty and working interest owners who were assignees of Strata.⁷⁴ Strata was allowed credit only for the royalty payments made to lessor royalty owners.⁷⁵ Apparently, the court decided that because Strata had sold the overriding royalty and working interest, it had thereby profited at the Gavendas' expense and could not receive credits for the payments made to its assignees.

D. *Market Value Litigation and Responses of Lessees Thereto*

Much litigation was spawned in the late 1960s, 1970s and early 1980s between royalty owners and lessee/purchasers over the payment of gas royalties based on current market value, as provided in many standard lease forms, as opposed to the net proceeds received by the lessee by virtue of its long-term gas sales contract. Because of the nature of marketing gas and the regulatory restrictions placed on gas purchasers and

71. *Id.* at 692.

72. *Id.* Professor Lowe is mystified by the distinctions relating to division orders made by the Texas Supreme Court, finding *Gavenda* irreconcilable with *Exxon v. Middleton*. See Lowe, *supra* note 54, at 1-22 n. 82. He is not alone. Strata, who paid the royalty owner a lesser interest than he was entitled to, is not protected, while Exxon and Sun, who paid the royalty owners a lesser value than they were entitled to, are. The distinction is a fine one.

73. *Gavenda*, 705 S.W.2d at 692-93.

74. *Strata Energy, Inc. v. Gavenda*, 753 S.W.2d 789, 791 (Tex. App.—Houston [14th Dist.] 1988).

75. *Id.* at 790.

producers, gas has been marketed until recently under long-term contracts. In the "market value royalty litigation," the royalty owners argued that their leases provided that they be paid the market value of the gas when produced, regardless of the price received by the producer under its long-term contract. Producers, quite naturally, contended that the contract price entered into at an arm's length basis *is* the market value and the proper basis on which royalty payments should be made.

The results of this litigation have been mixed. Texas,⁷⁶ Kansas,⁷⁷ Mississippi,⁷⁸ (and probably Montana,⁷⁹ North Dakota, and West Virginia⁸⁰) have favored the royalty owners, concluding that market value royalty payment obligations may be based on a price greater (and perhaps lower)⁸¹ than the contract price. Oklahoma,⁸² Arkansas,⁸³ and Louisiana⁸⁴ have rejected this view holding that in most circumstances the proceeds received by a lessee under an arm's length gas sales contract constitute the market value.

These "market value royalty" cases have caused considerable consternation to producers of gas. To force lessees to pay royalty on prices greater than they were receiving was felt by many commentators and all producers to be rather harsh, although clearly supported by established legal principles. The Texas Supreme Court in *Middleton* gave some protection to the lessee by virtue of the language of the division orders that the royalty owners had executed. The Texas Supreme Court held that these division orders were binding until revoked, even though they had the effect of amending the lease royalty provisions to provide for payment of the lessor's royalty based on one-eighth of the price received by the lessee, rather than one-eighth of the market value as provided in the

76. *Exxon Corp. v. Middleton*, 613 S.W.2d 240 (Tex. 1981); *Texas Oil & Gas Corp. v. Vela*, 429 S.W.2d 866 (Tex. 1968).

77. *Holmes v. Kewanee Oil Co.*, 233 Kan. 544, 664 P.2d 1335 (1983), *cert. denied*, 474 U.S. 953 (1985); *Lightcap v. Mobil Oil Corp.*, 221 Kan. 448, 562 P.2d 1, *cert. denied*, 434 U.S. 876 (1977).

78. *Piney Woods Country Life School v. Shell Oil Co.*, 539 F.Supp. 957 (S.D. Miss. 1982), *aff'd in part, rev'd in part*, 726 F.2d 225 (5th Cir. 1984), *cert. denied*, 471 U.S. 1005 (1985) (court on remand held that royalty owners failed to prove that market value of gas sold was any different than contract price Shell paid, No. J74-0307(W) (S.D. Miss. April 24, 1989)).

79. *Montana Power Co. v. Kravik*, 179 Mont. 87, 586 P.2d 298 (1978) (*dicta*—lessee was both producer and purchaser).

80. *Amerada Hess Corp. v. Conrad*, 410 N.W.2d 124 (N.D. 1987) and *Teavee Oil & Gas, Inc. v. Hardesty*, 297 S.E.2d 898 (W. Va. 1982) (Both cases held that tax statutes based on market value of gas meant current market value and not contract price.).

81. *See infra* p. 590.

82. *Tara Petroleum Corp. v. Hughey*, 630 P.2d 1269 (Okla. 1981).

83. *Hillard v. Stephens*, 276 Ark. 545, 637 S.W.2d 581 (1982).

84. *Henry v. Ballard & Cordell Corp.*, 418 So. 2d 1334 (La. 1982).

lease.⁸⁵

As a result of these market value royalty cases,⁸⁶ many producers have changed their division order forms in an effort to shield themselves from liability for "excess" royalty obligations, *i.e.*, having to pay royalty on anything other than the price they received from the sale of production. They have drafted certain clauses to attempt to achieve this result. The exact approach chosen may have telling consequences for producers and may present royalty owners with another grab at the golden ring.⁸⁷

The following division order provisions illustrate the different approaches taken by producers to address this matter:

Producer No. 1—You . . . are hereby granted the right, until further written notice, to receive the oil and gas from said well . . . Gas received under the provisions hereof shall be paid for to the party or parties entitled thereto according to the schedule of interest shown herein at the prices received by you for such gas. . . . Market value of production at the well as that term is used in any of the oil, gas and mineral leases affecting the lands covered by this Division Order shall be the price received by you under any sales contract entered into between you and any third party.

Producer No. 2—Each of the undersigned declares and agrees that you are hereby authorized, until further written notice as herein provided, to receive from each of the undersigned in the particular interest or proportion credited to him, oil and gas, subject to the following terms and conditions: . . . The oil and gas received and purchased under the provisions of this division order shall be paid to the owners set out herein at . . . the sales price received by you less any applicable transportation and marketing charges, and the undersigned agrees that this price shall be conclusively presumed to be the market value at the well of the oil and gas sold or used as provided for in the royalty provisions of the oil, gas and mineral lease or leases through which payments are made to the undersigned. . . . *This division order is executed subject to all applicable gas contracts.* You may discontinue your authority to purchase any oil hereunder by giving at least 48 hours prior written notice. An interest owner may terminate this division order *as to oil* by giving you at least 48 hours prior written notice.

Producer No. 3—Settlements for gas and/or casinghead gas produced from the property covered by this Division Order shall be based upon the net proceeds received by the working interest owners from the sale

85. Exxon Corp v. Middleton, 613 S.W.2d 240, 250 (Tex. 1981).

86. Many division order forms were changed after the Supreme Court's decision in Phillips Petroleum Co. v. Wisconsin, 347 U.S. 672 (1954), which held that the Federal Power Commission had the power to regulate the price received by a producer selling in interstate commerce. See Hooper & Schleier, *supra* note 1, at 537-39.

87. Or fleece, depending on one's point of view. See *infra* pp. 590-93.

of such gas and/or casinghead gas computed at the wells. You are authorized to deduct from such proceeds the cost incurred in compressing, treating, dehydrating and transporting such gas and/or casinghead gas for delivery in computing the net proceeds at the wells payable as royalty. . . . Each of the Owners who owns a royalty interest (landowner's royalty) in the property hereinabove described, by the execution of this Division Order, *hereby adopts, ratifies and confirms* each oil and gas lease, and *each gas purchase contract, together with any amendments thereof, to which this Division Order applies*. . . . This contract shall remain in full force and effect until cancelled by any party hereto upon giving 60 days written notice in advance of any such cancellation.

Producer No. 4—[U]ntil further written notice from you or from us, the undersigned owners . . . authorize you . . . to receive such sales [from the named well] and to give credit as set forth on Exhibit A . . . *Settlement shall be based on the net proceeds at the well as determined by the price and on the terms stated in that certain gas sale contract to XYZ Pipeline Company from ABC Production Company dated November 1, 1979 and amended August 1, 1980, and any renewals or modifications thereof applicable to the property covered hereby; and the undersigned ratify said gas sales contract.*⁸⁸

Producer No. 1 attempts to amend or at least elucidate the lease royalty terms to stipulate that the "market value" of the production shall be the price received by the lessee under any gas sales contract. However, the division order clearly remains revocable.

Producer No. 2 generally adopts the same approach as No. 1, but goes somewhat further. It purports to make the division order "subject to" the applicable gas sales contract. The division order is specifically made revocable as to oil, but is silent as to gas, thus implying that it may not be revocable as to gas sales.

Producer No. 3 simply stipulates that settlements for gas sales made under the division order shall be based upon net proceeds, but does not attempt to define or clarify the term "market value." The division order is explicitly made revocable, but the royalty owner adopts and ratifies the gas sales contract. Thus, the ratification of the gas sales contract may make the division order irrevocable as to gas sales.

The last division order resembles No. 3, but is far more specific. It specifies that settlement shall be based on the price and terms of a designated gas sales contract and requires the royalty owners to ratify that contract. The division order does contain the language "until further

88. These are provisions in division orders from four producers, all of whom are selling gas from the same South Mississippi field to three different gas purchasers.

written notice"; such language is normally deemed to make the division order revocable. The ratification of a specific gas contract, however, may make the division order irrevocable as to gas sales.

What effect on the obligation of producers to pay royalty do the above division orders have? The "market value" cases arose and were decided in a period of rising prices. The litigation was prompted by a rising market price and lower long-term contract prices. The market forces that have been allowed to work have now swung the pendulum and the current market value is frequently below many of the contract prices. The legal reasoning supporting most of the decisions that granted royalty owners the right to receive a royalty payment based on a current market value higher than the contract price supports the converse situation equally. Indeed, the Fifth Circuit has said as much in *Piney Woods Country Life School v. Shell Oil Co.*, stating: "If the price of gas declines, a market value royalty clause would benefit a lessee who has contracted to sell gas at a favorable price."⁸⁹

There are no cases directly on point. Most lessees appear to be paying the contract price although some undoubtedly are paying a lower market value price. Under the reasoning of the *Middleton* court, all of the above lessees would appear to have to account to royalty owners on the basis of the prices they received and could not make payment at a lower current market value price without revoking the terms of the division orders.⁹⁰

E. *The Rights of Royalty Owners to Share in Take-or-Pay Settlements*

What market value litigation was to the 1970s and 1980s, royalty owners' claims to share in take-or-pay payments or settlements will be for the 1990s. Many gas sales contracts executed in the late 1970s and early 1980s contain what is known as a take-or-pay provision. These clauses generally require the pipeline purchaser either to take (and pay for at the contract price) a specified quantity of natural gas during each contract year (or month), or to pay for the contract minimum quantity regardless of whether it is taken. The purchaser is required to pay for any deficient takes at the end of the contract year and is then allowed to recoup the take-or-pay payments made by taking makeup gas at a later

89. 726 F.2d 225, 236 n.14 (5th Cir. 1984) (citations omitted).

90. We could be faced with the ironic situation of attorneys for royalty owners adopting the arguments of gas producers set out in the market value royalty cases and attorneys for producers responding with the royalty owners' former arguments.

date. As the pipelines' take-or-pay obligations began to mount, pipelines, by and large, refused to make further take-or-pay payments and frequently unilaterally reduced both the takes and the prices paid for the gas that was taken.⁹¹

The actions of the pipelines have spawned a cottage industry for gas contract litigators. The pipelines have paid out huge sums in take-or-pay payments, and even greater sums in take-or-pay settlements and damage awards.⁹² Billions of dollars still remain in dispute and many more settlements or court adjudications will be made in the near future as the pipelines work their way out of their take-or-pay liabilities. Royalty owners and their enterprising attorneys are about as likely to sit back and make no claims to share in these take-or-pay monies as they were content to receive below market value prices when gas prices were shooting up.⁹³

Indeed, the first shots fired in Round 2 of the take-or-pay wars were by the United States government. In *Diamond Shamrock Exploration Corp. v. Hodel*,⁹⁴ the Fifth Circuit consolidated and then reconciled conflicting cases from two Louisiana district courts and held that royalties to the United States were not due on take-or-pay payments received by producers under the terms of the government leases involved. The court ruled that royalties are not owed unless and until there is actual production, the physical severance of minerals from the ground.⁹⁵ Many gas producers who have recently received major take-or-pay settlements breathed a little easier after the *Diamond Shamrock* decision. However, it is too early to tell how persuasive the Fifth Circuit decision will be to other courts that consider the issue.⁹⁶ The *Diamond Shamrock* case

91. See generally Medina, McKenzie & Daniel, *Take or Litigate: Enforcing the Plain Meaning of the Take-or-Pay Clause in Natural Gas Contracts*, 40 ARK. L. REV. 185 (1987).

92. See, e.g., *Redhill Development Co. v. Tennessee Gas Transmission Co.*, a Texas state court decision discussed in *Natural Resources Law Newsletter*, Vol. 20, No. 4, Spring 1989. (The jury awarded \$700 million to the plaintiff. The matter was subsequently settled prior to appeal.) See also *Mobil Oil Exploration and Producing S.E., Inc. v. FERC*, 885 F.2d 209, 235 n.19 (5th Cir. 1989) (Judge Brown notes that eight pipelines have reached in the aggregate over \$3.9 billion in settlement of take-or-pay liability.).

93. Of course, the vast majority of royalty owners did not, in fact, sue their lessees to obtain a higher price than the lessee was receiving for gas sales, even though their lease clauses may have justified such a suit. However, there were enough suits brought to cause major revisions to the forms of leases and division orders.

94. 853 F.2d 1159 (5th Cir. 1988).

95. *Id.* at 1168.

96. A Wyoming court reached the same conclusion as the Fifth Circuit, holding that no royalty was due the State of Wyoming under a state lease for take-or-pay payments since no gas was "produced" as provided in the lease royalty clause. *State v. Pennzoil Co.*, 752 P.2d 975 (Wyo. 1988); accord *Frey v. Amoco Prod. Co.*, 708 F.Supp. 783 (E.D. La. 1989).

dealt with a federal lease, the interpretation of the federal lease provisions, and pertinent regulations. For that reason alone, it may be distinguishable from cases involving privately owned lands. One of today's pre-eminent oil and gas authorities, Professor John Lowe, concluded that "if the issue is decided by reference to literal lease terms, royalty owners probably should not share in take-or-pay payments."⁹⁷ But, as Professor Lowe pointed out, many courts when interpreting oil and gas leases look beyond the literal terms of the lease and focus on the broader general intention of the parties.⁹⁸ Many obligations not mentioned in the lease contract are implied by the courts, such as the implied covenant to market on the best available terms. It does not take a cosmic leap to conclude that the lessor may also be entitled to share in all the benefits of the lessee's marketing arrangements.⁹⁹

What effect will an executed division order containing language as recited above have on the obligation of producers to share with royalty owners the fruits of their take-or-pay settlements or payments from the pipelines? A strong argument can certainly be made that the royalty owners in the first two division orders above are made third-party beneficiaries of the gas contracts. In the last two division orders, the royalty owners specifically ratify, and thus become parties to, the gas sales contract. The last division order additionally provides that the royalty owners ratify a specific named, dated, and identifiable gas sales contract. Would not a party to the contract have a right to receive all of the benefits pursuant to the contract?

Courts have bound lessors to the terms of gas sales contracts which have been ratified by division orders.¹⁰⁰ There appears to be no reported decision where the issue of division orders entitling a royalty owner to share in take-or-pay payments or settlements has been adjudicated. No

97. Lowe, *Current Lease and Royalty Problems in the Gas Industry*, 23 TULSA L.J. 547, 563 (1988). See also Kramer, *Royalty Obligations Under the Gun--The Effect of Take-or-Pay Clauses on the Duty to Make Royalty Payments*, 39 INST. ON OIL & GAS L. & TAX'N, Ch. 5 (1988); Smith, *supra* note 8, at 513.

98. Lowe, *supra* note 97 at 563.

99. Lowe, *supra* note 97, at 563. Royalty owners will also undoubtedly argue that take-or-pay payments are nothing more than prepayments for production to be taken at a later date. Advance royalty payments for minerals to be mined at a later date have long been common in the mining industry. Also, the manner in which the lessee has paid royalties on entitlements or actual takes could affect the outcome of royalty obligation on take-or-pay payments. For a concise discussion of royalty owners' claims to take-or-pay proceeds and the effect of division orders thereon, see Smith, *supra* note 8, at 543-45.

100. *Simpson v. United Gas Pipe Line Co.*, 196 Miss. 356, 17 So. 2d 200 (1944); *Koenning v. Manco Corp.*, 521 S.W.2d 691 (Tex. Civ. App.—Corpus Christi), writ. ref'd n.r.e., 531 S.W.2d 805 (Tex. 1975).

producer is known by this writer that has shared take-or-pay payments with its royalty owners. The settlement of take-or-pay litigation frequently involves amendments to, or a buy-down or buy-out of, the gas contract. In all probability, a royalty owner would be entitled to share in such a settlement.¹⁰¹ Where the royalty owner is a party to the contract by virtue of its ratification in the division order, the royalty owner should certainly be entitled to participate in the fruits of a contract settlement. Some producers have shared at least a portion, if not all, of these gas contract settlements with their royalty owners. Others have shared nothing. Whether the royalty owners are legally entitled to share in these payments and settlements under the lease royalty clause, the general implied terms of the lease or pursuant to division orders, will undoubtedly be widely litigated in the coming years.

F. *Right to Interest on Suspended Funds*

Division orders almost universally authorize the purchaser to suspend funds upon certain stated conditions without any obligation for interest. A typical division order provision dealing with interest reads as follows:

Satisfactory abstracts or other evidence of title will be furnished to you at any time on demand. In the event of a failure to so furnish such evidence of title, or in the event of a claim or controversy, which in your opinion concerns title to any interest hereunder, you may hold the proceeds of all oil and withhold payments on all gas received by you hereunder, without interest and without any liability, until indemnity satisfactory to you has been furnished or until such claim or controversy has been settled to your satisfaction.

In three companion cases decided in the 1930s,¹⁰² the Tenth Circuit approved a purchaser's withholding of payments without obligation to pay interest to the lessor pending the resolution of title litigation. The lessor had refused to execute a division order to the third-party purchaser. The lessor sued claiming interest on the suspended royalties. The court looked to the common law and the usage generally adopted by

101. *Lowe, supra* note 97, at 563; *Smith, supra* note 8, at 544. *But see* Gerard J. W. Bos & Co., Inc. v. Harkins & Co., 883 F.2d 379 (5th Cir. 1989) (court held no fiduciary duty arose with respect to marketing by the unit operator by virtue of Mississippi Oil & Gas Board's force integration order, and that royalty owner had no claim against unit operator, who was not his lessee, for unit operator's settlement of its gas contract dispute with the pipeline).

102. *Wolfe v. Texas Co.*, 83 F.2d 425 (10th Cir.), *cert. denied*, 299 U.S. 553 (1936); *Wolfe v. Prairie Oil & Gas Co.*, 83 F.2d 434 (10th Cir. 1936); *Wolfe v. Shell Petroleum Corp.*, 83 F.2d 438 (10th Cir.), *cert. denied*, 299 U.S. 553 (1936).

those in the business of producing, marketing, and purchasing crude oil, and ruled that in cases in which the title was in dispute, the purchaser had a right to suspend the funds without liability for interest. Early Texas cases also upheld the right of the purchaser to suspend funds without obligation to pay interest when the division orders have provided that the purchaser could suspend payments in the event of a title dispute and no indemnity was furnished.¹⁰³

However, in Kansas and Louisiana it is clear that the purchaser is not authorized to suspend royalties without obligation for interest.¹⁰⁴ In *Maddox v. Gulf Oil Corp.*,¹⁰⁵ the Kansas Supreme Court held:

It was the duty of Gulf under the lease contracts it had with its royalty owners to market the gas at the best prices obtainable at the place where the gas was produced. The insertion in the division orders of matters contrary to the oil and gas leases, or contrary to the law, cannot be unilaterally imposed upon the lessor by the lessee or the purchaser. Here the unilateral attempt by Gulf in the division orders to amend the oil and gas leases, and thereby deprive the royalty owners of interest to which they were otherwise entitled, was without consideration. Therefore, the provisions in the division order regarding waiver of interest are null and void as determined by the trial court.¹⁰⁶

Although the *Maddox* case involved a division order from a lessee, the court indicated that the same rule would have applied had the division order been from a third-party purchaser.¹⁰⁷

In a poorly reasoned opinion with egregious results for the royalty owner, the New Mexico Supreme Court recently held in *Murdock v. Pure-Lively Energy 1981-A, Ltd.*¹⁰⁸ that an oil purchaser did not owe the royalty owner interest on proceeds withheld pending resolution of a title dispute. The linchpin of the Court's decision was the royalty owner's execution of a division order. The royalty owner's title was challenged before the well in question had been drilled and the operator/purchaser,

103. *Gulf Pipe Line Co. v. Nearen*, 135 Tex. 50, 138 S.W.2d 1065 (Tex. Comm'n App. 1940, opinion adopted); *Gulf Pipe Line Co. v. Mann*, 135 Tex. 49, 138 S.W.2d 1069 (Tex. Comm'n App. 1940, opinion adopted); *accord*, *Lasater v. Convest Energy Corp.*, 615 S.W.2d 340 (Tex. Civ. App.—Eastland 1981, writ ref'd n.r.e).

104. *Shutts v. Phillips Petroleum Co.*, 235 Kan. 195, 218-20, 679 P.2d 1159, 1179-80 (1984), *aff'd in part, rev'd in part*, 472 U.S. 797 (1985), *Maddox v. Gulf Oil Corp.*, 222 Kan. 733, 567 P.2d 1326 (1977), *cert. denied*, 434 U.S. 1065 (1978); *Fontenot v. Sunray Mid-Continent Oil Co.*, 197 So. 2d 715 (La. App.), writ ref'd, 250 La. 898, 199 So. 2d 915 (1967).

105. 222 Kan. 733, 567 P.2d 1326 (1977), *cert. denied*, 434 U.S. 1065 (1978).

106. *Id.* at 735, 567 P.2d at 1328.

107. *Id.*

108. 108 N.M. 575, 775 P.2d 1292 (1989). This case is a perfect illustration of why many royalty owners are leery of signing any division order.

Conoco, had suspended payment.¹⁰⁹ The royalty owner filed a quiet title action and was eventually successful in having the adverse claims dismissed. Conoco prepared a division order after the royalty owner had partially extinguished the adverse claim (and thus, a considerable time after the well had been producing and Conoco had been purchasing the oil) covering one-half of the royalty owner's interest. The royalty owner *deleted* the standard form provision which authorized Conoco to suspend proceeds without liability for interest. Conoco then paid the royalty owner one-half of the suspended proceeds without any interest. A few months later, Conoco sent the royalty owner an "amended division order" covering the remainder of his interest,¹¹⁰ which division order "restored the unauthorized deletion which Murdock made in the first Conoco-Murdock division order and provided that Conoco could withhold royalty payments without interest."¹¹¹ This division order was executed, and Conoco paid the proceeds for the remaining royalty without any interest. The royalty owner sued to recover interest for the period his royalty was suspended. The Court held that under the terms of the second division order, Conoco did not owe the royalty owner interest on the proceeds suspended pending resolution of the title dispute.¹¹² The Court in dicta indicated that even if the division order had not specifically provided that Conoco did not owe the royalty owner interest, "under the common law some courts hold interest would not be owed,"¹¹³ citing *Gulf Pipe Line Company v. Nearen*.¹¹⁴

The *Murdock* court's dicta concerning the common law is somewhat misleading. Courts may frequently state as a rule that prejudgment interest is not allowed under that name unless provided for by contract or statute, but then proceed to approve exceptions based on equity.¹¹⁵

The Texas cases¹¹⁶ and those of other common law juris-

109. A claim was also involved on wells where another party was the operator and Conoco, as purchaser, had paid the royalty proceeds to the operator who then suspended them. A judgment against this operator was rendered by the trial court and no appeal made. The operator must have been unable to adequately satisfy this judgment since the plaintiff sought to hold Conoco liable for interest on these proceeds as well.

110. The Court's opinion is not precisely clear as to whether the second division order was only for the remaining one-half of the royalty owner's interest or purported to cover the entirety of his interest and, thus, supersede the first division order. The Court treated it as if it were the latter.

111. *Murdock*, 108 N.M. at ___, 775 P.2d at 1295.

112. *Id.* at ___, 775 P.2d at 1297.

113. *Id.*

114. 135 Tex. 50, 138 S.W.2d 1065 (Tex. Comm'n App. 1940, opinion adopted).

115. *Phillips Petroleum Co. v. Stahl Petroleum Co.*, 569 S.W.2d 480, 486 (Tex. 1978).

116. *Phillips Petroleum Co. v. Hazlewood*, 534 F.2d 61 (5th Cir. 1976); *Phillips Petroleum Co. v. Adams*, 513 F.2d 355, 370 (5th Cir. 1975) ("Texas courts . . . realize that the right to interest is a

dictions¹¹⁷ overwhelmingly support the right of the royalty owner to be paid interest on suspended funds. The common law provides that interest will be due when a party suspending funds has retained and used or commingled those funds based upon the equitable doctrine for use and detention of money.¹¹⁸ The court in *Murdock* recognized that Conoco owed the royalty owner a duty of "utmost good faith," but concluded that it had no duty to pay the royalty owner interest for the detention of the money.¹¹⁹ A reasonably prudent operator would not place its own surplus funds in a non-interest bearing account so that only the bank could enjoy the interest from the use of the funds. The operator should have a duty to the royalty owner to treat these funds in the same manner as it would its own. The question is not whether interest should be paid on suspended proceeds, but rather who is entitled to this interest, the owner of the money or its custodian. The courts should always allow the royalty owner the right to receive interest on suspended proceeds unless there has been a clear waiver of that right, supported by valid consideration.

Many states now have statutes which require interest penalties for sums not timely paid to royalty owners.¹²⁰ However, these statutes are

marketplace concept and that the use of money is a mercantile privilege which should not go uncompensated, absent countervailing considerations."); *Fuller v. Phillips Petroleum Co.*, 408 F.Supp. 643 (N.D. Tex. 1976); *Phillips Petroleum Co. v. Stahl Petroleum Co.*, 569 S.W.2d 480 (Tex. 1978) (The Texas courts have not insisted on statutory rigidity in the allowance of interest when necessary to permit compensation for the use or detention of one's money); *MCZ, Inc. v. Smith*, 707 S.W.2d 672, 677 (Tex. App.—Houston [1st Dist.] 1986, writ ref'd n.r.e.) ("court can award prejudgment interest upon equitable principles to compensate one for another's possession and use of his funds"); *DeBenavides v. Warren*, 674 S.W.2d 353 (Tex. App.—San Antonio 1984, writ ref'd n.r.e.).

117. *Phillips Petroleum Co. v. Oldland*, 187 F.2d 780, 783 (10th Cir.), *cert. denied*, 342 U.S. 816 (1951). (Court of Appeals applying Colorado law found interest on suspended proceeds should be allowed on equitable principles due to the wrongful retention of royalty. The court stated that "[t]he mere fact that the validity of the claim was in dispute does not preclude the recovery of interest.") *Id.* *Shutts v. Phillips Petroleum Co.*, 240 Kan. 764, 732 P.2d 1286 (1987), *cert. denied*, ___ U.S. ___, 108 S.Ct. 2883 (1988) (class action suit wherein Kansas Supreme Court applied the laws of Texas, Oklahoma, Louisiana, New Mexico and Wyoming and found interest required on suspended royalty funds); *Schaffer v. Tenneco Oil Co.*, 278 Ark. 511, 647 S.W.2d 446 (1983); *Holmes v. Kewanee Oil Co.*, 233 Kan. 544, 664 P.2d 1335 (1983), *cert. denied*, 474 U.S. 953 (1985); *Bennion v. Utah State Bd. of Oil, Gas & Minerals*, 675 P.2d 1135, 1144 (Utah 1983); *Cf. Dilworth v. Fortier*, 405 P.2d 38 (Okla. 1964); *State Highway Comm'n v. Wunderlich*, 194 Miss. 119, 11 So. 2d 437 (1943).

118. See *supra* notes 116-17; see also *Lear*, *supra* note 1, at 17-49.

119. *Murdock v. Pure-Lively Energy 1981-A, Ltd.*, 108 N.M. 575, 775 P.2d 1292 (N.M. 1989). Conoco, in addition to purchasing production from the wells, owned an unleased mineral interest that was subject to a non-participating royalty interest owned by *Murdock*.

120. See ALA. CODE § 9-17-33 (Supp. 1987); ARK. STAT. ANN. § 15-74-601 to -04 (1987); IND. CODE ANN. § 32-5-9-1 (Burns 1987); LA. REV. STAT. ANN. § 31:212.23 (West 1989); MISS. CODE ANN. § 53-3-39 (Supp. 1989); MONT. CODE ANN. § 82-10-103 (1989); N.M. STAT. ANN. 1978 § 70-10-1 to -5 (Supp. 1987); N.D. CENT. CODE § 47-16-39.1 (Supp. 1989); OKLA. STAT. tit. 52, § 540 (Supp. 1989); TEX. NAT. RES. CODE ANN. §§ 91.401-406 (Vernon Supp. 1990); UTAH CODE ANN.

by no means identical,¹²¹ and the particular statute should be consulted to see precisely what it provides as to when interest is due and whether the right may be waived in a division order. Mississippi, after initially enacting its royalty owner interest bill in 1983, amended the statute two years later to provide that interest on undisbursed royalty may not be waived or reduced by a royalty owner entitled to such interest payment “unless said royalty owner shall attest to a statement which shall be typed in bold print on a separate form and attached to the relevant division order contract” specifically agreeing to waive the statutory right to interest by language as set out in the statute.¹²² Thus, in Mississippi, the language in the form division orders currently in use waiving interest on suspended funds is ineffective.

G. *Effect of Division Order on Specific Lease Terms*

When a division order is directed to the lessee, it is generally held that the lessee cannot amend the lease terms or execute a division order to escape obligations or liabilities under the lease.¹²³ Courts that hold that the lessee cannot amend the terms of the lease by language in the division order generally support this reasoning on a failure of consideration being passed between the parties to support a royalty owner’s relinquishment of his rights.¹²⁴ However, as evident in *Middleton* and other market value royalty cases, the royalty provisions under the lease have been effectively amended by division orders at least while the division orders remain unrevoked and the parties act pursuant thereto.¹²⁵ Also, the more specific terms of a division order often will be used to supplement less specific language of a lease.¹²⁶ In a recent Texas

§ 40-6-9 (Supp. 1989); WYO. STAT. §§ 30-5-301 to -303 (1983). In spite of such statutes, many purchasers will not pay interest on delinquent royalty payments unless the royalty owner specifically demands the payment of interest.

121. Compare N.D. CENT. CODE § 47-16-39.3 (“Royalty payments may not be withheld because an interest owner has not executed a division order.”) with N.M. STAT. ANN. 1978 § 70-10-5 (penalty provisions do not apply if royalty owner does not execute division order). The New Mexico statute is of limited value to royalty owners because it provides that the penalty provision shall not apply if the person entitled to payment has failed or refused to execute the payor’s “customary and reasonable” division order. Purchasers’ customary division orders allow them to suspend proceeds without liability for interest.

122. MISS. CODE ANN. § 53-3-39 (Supp. 1989).

123. E. BROWN, *THE LAW OF OIL AND GAS LEASES*, § 16.02, at 16-86 (2d ed. 1985); M. MERRILL, *COVENANTS IMPLIED IN OIL AND GAS LEASES*, § 209A (2d ed. Supp. 1964); Hollimon, *supra* note 1, at 345-46.

124. See, e.g., *Maddox v. Gulf Oil Co.*, 222 Kan. 733, 567 P.2d 1326 (1977), *cert. denied*, 434 U.S. 1065 (1978).

125. *Exxon Corp. v. Middleton*, 613 S.W.2d 240, 250 (Tex. 1981).

126. Twenhafel, *supra* note 1, at 1504-05.

decision,¹²⁷ the court refused to relieve lessees from payment of royalty where the operator/purchaser to whom division orders had been directed defaulted in payments due, stating:

[Our cases] do not excuse the lessees from payment of the lessors' royalty merely because there have been division orders executed by the lessors in favor of a purchaser of the leasehold oil and gas. We know of no authority that permits such use of a division order without express provision in the order for it.¹²⁸

Frequently, division orders will contain language explicitly ratifying the oil, gas, and mineral lease under which the production is sold. Even in the absence of specific language of ratification, courts have held that execution of division orders and acceptance of royalty payments pursuant thereto can serve to ratify a lease.¹²⁹

VII. POSSIBLE SOLUTION TO PROBLEMS ENCOUNTERED

The major problem encountered by royalty owners in executing division orders is the fear that the rights reserved to them under their lease will somehow be diminished, amended, modified or otherwise altered. As we have seen, this fear is not always unjustified.

One method of alleviating this fear is to insert a special provision in whatever lease form is executed by the mineral owner. One mineral owner who prepared a lease form included a provision that reads as follows:

If, in the event of production, a division order is circulated by lessee or by a purchaser of production, such division order will be a simple statement of interest containing no warranty or indemnity clauses and containing no clauses modifying in any way the terms of this lease. The insertion of any such clauses in a division order will be of no force and effect.

No potential lessee has refused to enter into a lease with this mineral owner because of this provision. Professor David Pierce, in his excellent

127. *Williams v. Baker Exploration Co.*, 767 S.W.2d 193 (Tex. App.—Waco 1989, writ ref'd).

128. *Id.* at 196. *But see Hollimon, supra* note 1, at 344-45, in which the author opines that oil division orders may transfer to the purchaser all of the lessee's duty to account for royalty and *Cook v. Tompkins*, 713 S.W.2d 417 (Tex. App.—Eastland 1986) in which the court held that the implied covenant to market was satisfied when the lessee delivered the royalty oil to the purchaser for lessor's account and the lessee had no obligation to see that the royalty owner was actually paid.

129. *See, e.g., Texas & Pac. Coal and Oil Co. v. Kirtley*, 288 S.W. 619 (Tex. Civ. App. 1926, writ ref'd); *Corey v. Sunburst Oil & Gas Co.*, 72 Mont. 383, 233 P. 909, *cert. denied*, 268 U.S. 698 (1925); *see also Boyd, supra* note 1, at 256; *Brannan, supra* note 1, at § 12-18 to -19; *Holliman, supra*, note 1, at 338-41; *Pierce, supra* note 1, at 3-37 n. 165.

article setting out a conceptual approach to resolving division order disputes, suggests that the lessor should be eliminated from the marketing transaction. He suggests drafting the oil and gas lease to vest title in the lessee to all production with the authority to sell it to others and the duty to account to the lessor based upon express and implied terms of the lease.¹³⁰ Thus, careful attention to drafting the terms of the lease can be a solution to any potential problem posed by division orders.

Another solution for the royalty owner is to carefully review all submitted division orders and delete any offending clauses. Many mineral owners send their attorneys division orders for review prior to their execution. Attorneys routinely strike through those clauses which purport to amend the lease to the disadvantage of the lessor. While occasionally a purchaser will object to deletions from its standard form division order, most purchasers are willing to work with the royalty owners and are agreeable to reasonable changes in their standard form. Few, if any, purchasers refuse to allow any alteration of their standard form division order. Also, as previously suggested, the lessor should insist on inserting an express provision in the division order that while the purchaser is authorized to buy the oil, the execution of the division order will in no manner affect any of the terms of the lease or the lessor's rights in real property in general.¹³¹

Legislation is another possible solution to the problems of royalty owners as sellers of production. Royalty owners are increasingly better organized and are beginning to have statutes enacted which affect royalty payment procedures. As previously discussed, statutes which require the purchasers to disburse payments within a certain period of time and make them liable for interest on funds not timely disbursed have been enacted by several states in recent years.¹³² Several states have recently passed payment information statutes which require the first purchaser to provide certain accounting information on the check stubs in a uniform manner so royalty owners can tell precisely what interest they are being paid and what deductions are being made from their interest. Louisiana, Montana, North Dakota, Oklahoma, and Texas all have statutes of this nature.¹³³

A statute passed in the 1989 session of the Wyoming Legislature provides that a division order may not alter or amend the terms of an oil

130. *Pierce, supra* note 1, at 3-49 to -51.

131. *Rain, supra* note 1, at 82.

132. *See supra* note 120.

133. *See Lear, supra* note 1, at 17-53 to -54 & n.209.

and gas lease or other contractual agreement.¹³⁴ The statute states that a division order that attempts to so alter a lease or contract is invalid to such extent, and that the terms of the lease or other contractual agreement will control. This statute also provides penalties for any working interest owner or agent who fails to provide royalty information in a proper and timely manner.¹³⁵ A similar bill was passed in Oklahoma to amend existing statutes to define a division order and to preclude a division order from relieving the lessee of any liabilities or obligations under an oil and gas lease.¹³⁶

An effort is also being made by the National Association of Royalty Owners and others to develop a Model Division Order Form. Working interest owners have enjoyed the benefit of a Model Form Operating Agreement for over thirty years. The Model Form Operating Agreement has changed periodically to reflect experiences of operators and is often amended by the parties. However, the basic model forms have facilitated harmonious operation of jointly owned properties. Although there is currently no standard division order, many division order provisions are common and not objectionable to royalty owners. Development of a Model Form Division Order could help allay many fears that royalty owners have. It is too early to tell how successful this effort will be.

VIII. CONCLUSION

Division order cases are the "Am. Jur." of oil and gas law. Quotations can be found in the various cases to support almost any proposition. Few generalizations can be made about the effects of "division orders" because many different instruments masquerade under this label. Execution of a division order or even the refusal to do so may adversely affect a royalty owner's rights. However, from a royalty owner's vantage point, not all division orders are bad. Division orders may, in fact, provide royalty owners with benefits under favorable gas contracts to which they otherwise would not be entitled. Division orders can also be useful in specifying royalty payment procedures that may only be vaguely set out in a lease. In executing division orders, royalty owners should observe the three R's. *Read* the division order before you *write* your name to it and make sure the *arithmetic* adds up to the interest you claim.

134. WYO. STAT. 30-5-305(a) (Supp. 1989).

135. WYO. STAT. 30-5-303 (Supp. 1989).

136. OKLA. STAT. tit. 52, § 540(B) (Supp. 1989).