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Mineral Rights

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I. LEGISLATION—1994 REGULAR SESSION

A. Act 2—Severance Tax Incentives

Act 2 of 1994 enacts and reenacts portions of Louisiana Revised Statutes 47:633(7),[1] enacts 47:648.1 through :648.4,[2] and repeals 47:646.1 through :646.5.[3] This act provides severance tax incentives for certain types of production and drilling of oil and gas wells. The tax is suspended on crude oil production from certified stripper wells in a month in which the average posted price for a thirty-day period is less than $20 per barrel. Severance tax is suspended for twenty-four months or until payout on horizontally drilled wells. There is a five-year severance tax exemption on wells returned to service after having been inactive for more than two years or having had less than thirty-one days of production during the past two years. Certified new discovery wells, defined as wildcat wells spudded after September 30, 1994, have severance taxes suspended for twenty-four months or until payout. The severance tax exemptions for new oil or gas fields[4] are repealed.[5]

B. Act 35—Natural Gas Franchise Tax

Act 35 of 1994 amends and reenacts Louisiana Revised Statutes 47:1031 through :1034.[6] This act pertains to the natural gas franchise tax on pipelines transporting gas in Louisiana. The tax is equal to one percent of the gross receipts from the pipeline's operations in the state. The amendments provide additional definitions and a new basis for the calculation of the taxes owed.

C. House Concurrent Resolution No. 35—Stripper Wells Transfer Fee

Noting that the imposition of a fee by the state for the transfer of ownership of stripper wells effectively takes them out of commerce because of the inability of the owner to recover his costs from the marginal production, the Louisiana Legislature, in House Concurrent Resolution No. 35,[7] authorized and directed

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1. 1994 La. Acts No. 2, § 1.
2. *Id.* § 2.
3. *Id.* § 3.
4. La. R.S. 47:646.1, .5 (1990).
5. 1994 La. Acts No. 2, § 3.
6. 1994 La. Acts No. 35, § 1.
7. H.R. Con. Res. 35, Reg. Sess. (1994).

the Department of Natural Resources, Office of Conservation, to not impose or charge a fee for the transfer of ownership of stripper wells.

II. CONTRACT INTERPRETATION

A. *Joint Operating Agreement*

In *Martin Exploration Co. v. Amoco Production Co.*,[8] plaintiff, Martin Exploration Company (MECO), brought suit against Amoco Production Co. (Amoco) claiming a contribution of acreage under a joint operating agreement. Gulf Oil had farmed out certain acreage to Amoco on March 10, 1980, in return for Amoco drilling a well. MECO and Amoco had entered into a letter agreement pertaining to the same area. Amoco drilled a well (the Ravenswood well) on the Gulf Oil farmout acreage. In August, 1980, MECO agreed to participate in the cost of the drilling of the Ravenswood well and to execute a mutually satisfactory operating agreement. In October, 1980, Amoco sent MECO a proposed operating agreement, the AAPL Form 610-1977, to be effective as of October 21, 1980. MECO executed the agreement, with revision, on January 23, 1981, and changed the effective date to January 1, 1980, a fact Amoco noted but did not change when it executed the agreement. The well was successful. MECO asserted that, under Article VIII.C (the Contribution Clause) of the joint operating agreement, Amoco was required to assign a portion of the Gulf Oil farmout acreage to MECO. Amoco asserted Article III.B of the operating agreement provided that the interests of the parties in costs, liabilities, and production of the Ravenswood well would be in accordance with Exhibit A to the agreement.[9] The trial court agreed with Amoco and the appeals court affirmed. Exhibit A reflected that the Gulf Oil farmout acreage was attributable to Amoco's interest. Amoco had the right to all production from the farmout acreage until payout; if Gulf Oil backed in for a working interest after payout, Gulf Oil's share was to be deducted entirely from Amoco's interest. Amoco was bearing the costs of production for the well for its own lease acreage and for the farmout acreage. No undue advantage was obtained by Amoco.[10]

B. *Gas Purchase Contract*

The plaintiff natural gas producer in *DeNovo Oil & Gas, Inc. v. Louisiana Intrastate Gas Corp.*[11] brought suit against the purchaser under a gas purchase contract for failure of the purchaser to reimburse the producer for construction of a pipeline used to deliver gas to the purchaser. The purchaser claimed it had

8. 637 So. 2d 1202 (La. App. 1st Cir. 1994). The author should disclose he gave testimony in this proceeding. He is in no way related to or associated with the named plaintiff.
9. *Id.* at 1203-05.
10. *Id.* at 1207-08.
11. 638 So. 2d 358 (La. App. 4th Cir. 1994).

paid the sums due, amendments made to the contract eliminated the obligation to reimburse, and a clause of the contract limited claims that could be made for "undercharges" to those made within twenty-four months of the undercharge. An additional defense concerned application of the Natural Gas Policy Act of 1978 (NGPA)[12] and whether this issue should be resolved first by the Federal Energy Regulatory Commission (FERC). The court found reimbursement of pipeline construction costs were not part of the price of the natural gas.[13] The producer and purchaser both reasonably concluded that, under a FERC order, the reimbursement, in addition to the maximum lawful price for gas, could not be paid for a period of several years. It was not necessary, however, that payments made during that time as part of the maximum lawful price of the natural gas be considered as part of the reimbursement of the construction costs. Once the NGPA maximum lawful price was no longer an effective limiting factor on the gas price, the parties amended the gas purchase contract price by letter agreements. The court found these amendments were not intended to supersede the reimbursement clause of the contract.[14] The court ruled in favor of the purchaser on the application of the twenty-four month limitation contained in the contract, holding that, once it became possible to charge for the reimbursement of costs, the special limitation began to accrue.[15]

III. CONVEYANCING

A. *Partition Interpretation—The Missing Comma*

A conveyance arising as part of a partition was construed in *Doyal v. Pickett.*[16] In the succession of Aubrey Arnold, his widow was recognized as owner of one-half of Blackacre and their two daughters as naked owners of one-fourth each, with usufruct in favor of the widow. One of the daughters, plaintiff Doyal, sought to partition the property in 1969 but then executed a compromise deed in 1971 in exchange for a $10,000 payment. The deed's second clause provided that plaintiff transfer:

> All of her right, title and interest in and to all of the property that was property of the marital community of acquets and gains existing between her mother, Evelyn Allison Arnold Mason, and her late father, Aubrey Franklin Arnold, *except that she is to keep all sums and movable property heretofore received* and particularly including all of her right, title and interest in and to all of the following described

12. Pub. L. No. 95-621, 92 Stat. 3350 (codified as amended in scattered sections of 15 and 42 U.S.C.).
13. *Id.* at 363-64.
14. *Id.* at 365-66.
15. *Id.* at 366-67.
16. 628 So. 2d 184 (La. App. 2d Cir. 1993).

> property, to-wit: [the home place and other immovable property are specifically described].[17]

The third clause of the deed reserved her interest in minerals in the "hereinabove described lands."

The plaintiff claimed the compromise deed reserved to her an interest in the home place and other immovable property, while the defendant contended the deed transferred the plaintiff's interest. The court, holding for the defendant, interpreted the deed's second clause as though there were a comma after the word "received." Under such an interpretation, only "all sums and movable property heretofore received" were excepted from the transfer.[18] The plaintiff's interest in the home place and immovable property were thus conveyed. The court's interpretation was buttressed by the fact the $10,000 payment far exceeded the value of the other matters in the dispute and the fact it would have been rather pointless to have sought a partition so as to get out of co-ownership and then not resolve that point of contention. Moreover, the clear reservation of mineral rights in the third clause was inconsistent with the claim the second clause retained ownership in immovable property. Had the immovable property been "excepted" as plaintiff claimed, there would have been no reason to "reserve" minerals. The court's premise is dead-center accurate, and its reasoning cannot be faulted. An additional noteworthy element of the decision was the principle, applied by the court, that a deed will be construed against the seller and/or drafter of the instrument.[19]

B. Partition—Divided and Undivided Interests

The case of *Campbell v. Pasternack Holding Co.*[20] presented several significant issues concerning partition: (1) whether a co-owner with perfect ownership may partition by licitation property as to which another undivided interest has been bifurcated into usufructuary and naked interests; and (2) whether the same plaintiff co-owner, who has no attendant mineral rights, may partition by licitation only her "surface" interest in the land, where one or more of the defendant co-owners has full interests in the land, including mineral rights. The answer to both of these was in the affirmative. In so holding, the court overruled one case[21] and ruled that Louisiana Civil Code article 543, as amended in 1983, is to be applied to partitions of co-owned property, even when the interests were acquired under pre-existing law and jurisprudence.[22] This article was amended to provide as follows:

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17. *Id.* at 187.
18. *Id.* at 188.
19. *Id.* at 187.
20. 625 So. 2d 477 (La. 1993).
21. Cahn v. Cahn, 468 So. 2d 1176 (La. 1985).
22. *Campbell*, 625 So. 2d at 481-84.

> When property is held in indivision, a person having a share in full ownership may demand partition of the property in kind or by licitation, even though there may be other shares in naked ownership and usufruct.
>
> A person having a share in naked ownership only or in usufruct only does not have this right, unless a naked owner of an undivided share and a usufructuary of that share jointly demand partition in kind or by licitation, in which event their combined shares shall be deemed to constitute a share in full ownership.[23]

The result in this case is not an unreasonable application of Article 543. Yet it does not resolve a problem that developed after the decision in *Steele v. Denning*.[24] Even though *Pasternack* speaks only to partition by licitation, it does not make clear the relationship between the owner of a mineral right who was not a party to the partition and the owner of the land after the partition. Under one view, the mineral right is "unaffected" but can be exercised by the mineral owner; whereas before the partition, the mineral right owner could not have exercised it without consent of all co-owners.[25] The resolution of this issue would significantly affect the value of land involved in licitation.

IV. Lease Maintenance and Royalty Payments

A. *Putting in Default*

The 1984 revision of the law of obligations eliminated the active and passive breach distinction which existed when Article 135 of the Louisiana Mineral Code[26] was enacted. That article incorporates the standards of the Louisiana Civil Code. Prior jurisprudence held a lessee must be put in default of its implied lease obligations prior to commencement of a suit. In *Taussig v. Goldking Properties Co.*,[27] the trial court found the lessees had abandoned the leases because of their failure to undertake additional development and treated the abandonment as an active breach which obviated the need to put the lessee in default. The court of appeals, however, held a formal placing in default was required. The attorneys for the lessors had made demands for lease cancellation,

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23. The legislation was intended, apparently, to overrule the decision in Pasternack v. Samuels, 415 So. 2d 211 (La. 1982). *See generally* Andrew L. Gates, III, *Partition of Land and Mineral Rights*, 43 La. L. Rev. 1119 (1983); Jeanne M. Gravois, Comment, *The Revision of the Louisiana Co-Ownership Law*, 65 Tul. L. Rev. 1261 (1991); Christina Berthelot Peck, Note, *Civil Code Article 543 and the Problem of Partition by Licitation of Property Subject to a Usufruct*, 43 La. L. Rev. 787 (1983).

24. 456 So. 2d 992 (La. 1984).

25. *See* Patrick H. Martin, *Mineral Rights, Developments in the Law, 1989-1990*, 51 La. L. Rev. 335, 336-37 (1990); Patrick H. Martin, *Mineral Rights, Developments in the Law, 1984-1985*, 46 La. L. Rev. 569, 587-89 (1986).

26. La. R.S. 31:135 (1989).

27. 495 So. 2d 1008 (La. App. 3d Cir. 1986), *writ denied*, 502 So. 2d 111 (1987).

not for development. A demand for cancellation, the court held, is not a substitute for a placing in default.[28] Furthermore, the trial court's conclusion that a passive breach had been transformed into an active one, obviating the necessity of placing in default under the Louisiana Civil Code's standards, was in error. The court of appeals stated: "Since the duty to develop is an implied obligation, the jurisprudence has consistently held that a breach of this duty is passive, and a formal placing in default is required before judicial intervention may be sought."[29]

An unreported decision, *Fina Oil & Chemical Co. v. Pennzoil Exploration & Production Co.*,[30] held the law applicable to mineral leases was changed with the revision of the obligations articles. Comment (e) to Louisiana Civil Code article 1989 of the 1984 law of obligations revision indicates it was not the intention of the drafters to change the operation of the Louisiana Mineral Code. Strictly speaking, the approach of the *Fina* decision is not necessarily inconsistent with comment (e). There was no express provision in the Louisiana Mineral Code for putting in default for breach of the implied obligations of the lessee under the prudent operator standard of Article 122 of the Louisiana Mineral Code,[31] other than the provision in Article 136[32] regarding drainage.

The court in *Hunt v. Stacy*[33] came to a different conclusion from the *Fina* court on the effect of the 1984 law of obligations changes. The *Hunt* court held the Louisiana Mineral Code continues the active/passive breach distinction despite the change in the Louisiana Civil Code. The *Hunt* court quotes from the comment to Louisiana Mineral Code article 135,[34] which observes the active/passive breach distinction, and then concludes: "It thus appears that the legislature intended to retain the distinction between passive and active breaches, as well as the jurisprudence regarding these classifications, at least as to contracts involving oil, gas and other minerals. Accordingly, we conclude that passive breaches do still exist."[35] The problem with the court's approach is that the text of Article 135 does not attempt to incorporate a static approach to the Louisiana Civil Code. Moreover, it seems questionable to quote a 1974 comment on legislative intent to ascertain the intent of a 1984 legislative act. It also appears troublesome to have the comments to the Louisiana Mineral Code articles, in effect, freeze the Louisiana Civil Code to what it provided in 1974. This would seem to require the courts to recognize the continued existence of the older

28. *Id.* at 1015.

29. *Id.* at 1014 (citing Trinidad Petroleum v. Pioneer Natural Gas, 416 So. 2d 290 (La. App. 3d Cir.), *writ denied*, 422 So. 2d 154 (1982)).

30. No. 95891 (La. Dist. Terrebonne Parish Apr. 2), *writ denied*, No. CW90-0846 (La. App. 1st Cir.), *writ denied*, 568 So. 2d 1086 (1990).

31. La. R.S. 31:122 (1989).

32. La. R.S. 31:136 (1989).

33. 632 So. 2d 872 (La. App. 2d Cir. 1994).

34. La. R.S. 31:135 cmt. (1989).

35. *Id.* at 875.

version of the Louisiana Civil Code in relation to mineral leases and to continue to develop a jurisprudence of active/passive breaches without a current Louisiana Civil Code basis for this. Clearly, the Louisiana Civil Code is to apply where it is not expressly or implicitly in conflict with the Louisiana Mineral Code.[36] There is nothing in the text of the Louisiana Mineral Code that conflicts with the 1984 Louisiana Civil Code revisions, except for Articles 137-140[37] dealing with royalty payment. It is, however, desirable to require written notice to lessees.[38]

B. Production in Paying Quantities

Virtually all mineral leases provide they will continue beyond the primary term for as long as there is production. If production ceases, the lease terminates automatically, unless saved by some other provision of the lease. The term "production" has been interpreted to mean "production in paying quantities."[39] The Louisiana Mineral Code, in Article 124,[40] codifies the judicial interpretation of this requirement. What constitutes production in paying quantities has been the subject of repeated litigation. In *Lege v. Lea Exploration Co.*,[41] the plaintiff lessors contended the lease had ceased because there was no longer production in paying quantities. The question of paying quantities turned on the accounting treatment of expenditures by the lessee for disposal of salt water. The lessee had installed a saltwater disposal system at substantial expense. The plaintiffs contended the expenses were greater than the value of the production. The lessee contended the system costs were in the nature of capital expenditures that should be amortized over a period of years. If the lessee's capitalization of these costs was correct, then the lease did produce in paying quantities in the relevant period. To this the plaintiffs responded the costs should be immediately expensed because the disposal system substituted for trucking the salt water away for disposal, and such lifting and trucking of salt water would have been properly treated as a current expense.[42]

The court agreed with the lessee that capitalization was the correct approach. Ruling for the lessee was clearly consistent with the standard of the Louisiana Mineral Code. The Louisiana Mineral Code provides the production in paying quantities standard looks to whether the lessee is acting as a prudent operator in

36. *See* Article 2 of the Louisiana Mineral Code, La. R.S. 31:2 (1989).

37. La. R.S. 31:137-:140 (1989 & Supp. 1995).

38. It may be noted both cases discussed here would have come out the same way on alternative grounds cited by the courts. The *Fina* court held if notice and demand for performance were required, the plaintiff had provided adequate notice. The *Hunt* court held the leases in question required notice of breach and a sixty day opportunity to comply with the demand for performance. Such demand for performance was not made and the suit was premature by virtue of the lease requirement.

39. *See, e.g.*, Coyle v. North Am. Oil Consol., 201 La. 99, 115, 9 So. 2d 473, 479 (1942).

40. La. R.S. 31:124 (1989).

41. 631 So. 2d 716 (La. App. 3d Cir.), *writ denied*, 635 So. 2d 1112 (1994).

42. *Id.* at 718.

seeking to make a profit or minimize losses and is not merely continuing production for speculative purposes.[43] The court declared "we are unable to accept the premise of plaintiff's position, that the nature of a lessee's cost is determined strictly by the substitution accomplished."[44] Nor was the matter of whether it was a pre- or post-production expense a determining factor. The lessee clearly was not acting for speculative purposes, and a prudent operator would continue to produce under the circumstances. The decision is undoubtedly correct.

C. *Assignment Clause*

The proper application of an assignment clause of a lease was at issue in *Hanks v. Wilson*.[45] In a series of transactions, Hanks acquired a fractional mineral servitude and the right to receive royalties to be paid under a lease affecting the mineral servitude subject to the occurrence of a condition. The right to receive royalty attributable to the mineral servitude had been purchased by the Wilsons, and they were to continue to receive the royalties until they had recouped their investment in purchasing the royalty together with interest. Hanks wrote a series of letters to the lessee notifying the lessee of the conveyances and of certain claims regarding the number of acres in the lease tract and the proper division interests of the royalty. The fourth letter by Hanks claimed the condition that gave him a present right to receive royalty had occurred. The Wilsons, however, claimed the condition had not yet occurred. In response to the differing claims, Amoco suspended payment of the share of royalty in dispute and invoked a concursus proceeding to determine the ownership of the mineral royalty.[46]

The trial court found that the condition had occurred prior to suspension of the royalty payments and that the Wilsons owed Hanks over $49,000, which they had been overpaid. The trial court further ruled the actions of Amoco in not paying Hanks on the basis of his fourth letter and in suspending the royalty payments pending the court action were reasonable and Amoco was not liable to Hanks for the money overpaid to the Wilsons.[47] On appeal, the first circuit affirmed. It ruled under paragraph 9 of the mineral lease that the lessee was relieved from the obligation to pay royalties to the assignee of the lessor's royalty rights, until the lessee had been provided with appropriate evidence of the change in royalty ownership.[48] From the information submitted, Amoco could

43. Article 124 of the Louisiana Mineral Code, La. R.S. 31:124 (1989).
44. *Lege*, 631 So. 2d at 719.
45. 633 So. 2d 1345 (La. App. 1st Cir. 1994).
46. *Id.* at 1345-47.
47. *Id.* at 1347.
48. *Id.* at 1350-51. The pertinent paragraph provides:

All provisions hereof shall inure to the benefit of and bind the successors and assigns (in whole or in part) of Lessor and Lessee, but regardless of any actual or constructive notice not determine the condition to which Hanks's interest was subject had in fact occurred. The lease clause protected Amoco from claims of improper royalty payment. This decision is consistent with prior cases applying similar or identical assignment clauses of mineral leases.[49]

D. Contra Non Valentem

The plaintiffs in *La Plaque Corp. v. Chevron U.S.A. Inc.*[50] were owners of an overriding royalty created out of a state-owned lease. The defendant was the lessee. Plaintiffs asserted the lessee had failed to pay proper royalty for many years and the lessee was therefore liable for underpayment from 1972 through 1989. A particular focus in the case was on a gas purchasing contract the lessee's predecessor, Gulf Oil Corporation (Gulf), had entered into in 1964 with Texas Eastern Transmission Corporation (Texas Eastern). The gas purchasing contract was a "warranty contract" pursuant to which the producer was required to provide a certain volume of gas at a fixed price (approved and limited by the Federal Power Commission), regardless of the source of the natural gas. The defendant asserted plaintiffs' claims had prescribed under the three-year prescriptive period set forth in Louisiana Civil Code article 3494, precluding all claims prior to June 5, 1987. The plaintiffs responded that prescription had not run because of the doctrine of contra non valentem; the defendant, they asserted, had not informed them of facts that would have enabled them to bring their claim earlier.[51]

The trial court concluded the doctrine of contra non was applicable and overruled the exception of prescription. The appeals court overturned the decision, finding the information on the market value of the gas was in the public records and available to the plaintiffs, and the plaintiffs had been advised, during various periods of the relevant time, by knowledgeable consultants. "A plaintiff," the court ruled, "will be deemed to know that which he could have

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thereof, no change in the ownership of the land or any interest therein or change in the capacity or status of Lessor or any other owner of rights hereunder, whether resulting from sale or other transfer, inheritance, interdiction, emancipation, attainment of majority or otherwise, shall impose any additional burden on Lessee, or be binding on Lessee for making any payments hereunder unless, at least forty-five (45) days before any such payment is due, the record owner of this lease shall have been furnished with certified copy of recorded instrument or judgment evidencing such sale, transfer or inheritance, or with evidence of such change in status or capacity of Lessor or other party owning rights hereunder. The furnishing of such evidence shall not affect the validity of payments theretofore made in advance.

Id. at 1350.

49. Lapeze v. Amoco Prod. Co., 842 F.2d 132 (5th Cir. 1988); Hibbert v. Mudd, 294 So. 2d 518 (La. 1974); Atlantic Refining Co. v. Shell Oil Co., 217 La. 576, 46 So. 2d 907 (1950).

50. 638 So. 2d 354 (La. App. 4th Cir. 1994).

51. *Id.* at 354-55.

learned from reasonable diligence."[52] The court was evidently influenced in part by the fact the named plaintiff was a corporation set up specifically to pursue the claim of underpayment of royalty. Three shareholders, directors and officers of La Plaque Corporation, had been involved, in various capacities, in management of the royalty interests in litigation for many years prior to suit being filed. They had been intimately aware of the Gulf/Texas Eastern contract. The exception of prescription was thus sustained.

E. Class Action Denied

The litigation fallout from *Frey v. Amoco Production Co.*[53] concerning the liability of lessees for royalty on take-or-pay payments and settlements, continues and will no doubt result in reported cases for some years to come. An effort to bring a *Frey*-type claim as a class action was rejected in *Stoute v. Wagner & Brown*.[54] The plaintiffs sought to certify a class action, seeking to proceed as a class consisting of all mineral lessors and royalty owners in the Moore-Sams Field, against the defendant producers. The court found many different contracts were involved—mineral leases, gas purchase agreements and settlements—and accordingly, many different rights, remedies, and defenses were likewise involved. It would not, the court concluded, be more efficient to try these disputes in a class action.[55]

V. OIL WELL LIEN ACT[56]

The case of *Guichard Drilling Co. v. Alpine Energy Services, Inc.*,[57] raised the question whether a creditor, when executing on his oil well lien, can seize the ownership interests of parties who were not made defendants in the seizure proceedings. The court also had to resolve the issue whether seizure, pursuant to an oil well lien against one party who purportedly has an ownership interest in the encumbered property, prevents other owners who were not made defendants from raising the defense of peremption. The court held, while the Oil Well Lien Act creates a right in rem—a lien and privilege in favor of certain persons over certain property, fundamental due process requires the owner of the "rem" be afforded notice and the opportunity of a hearing.[58] Because the lienholder instituted legal proceedings against only defendant Alpine Energy Services, Inc. (Alpine), and not the intervenors, in attempting to enforce its lien,

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52. *Id.* at 358 (citing Matthews v. Sun Exploration & Prod. Co., 521 So. 2d 1192, 1197 (La. App. 2d Cir. 1988)).
53. 603 So. 2d 166 (La. 1992).
54. 637 So. 2d 1199 (La. App. 1st Cir. 1994).
55. *Id.* at 1200.
56. La. R.S. 4:4861-:4867 (1991 & Supp. 1995).
57. 635 So. 2d 1312 (La. App. 4th Cir.), *writ granted*, 642 So. 2d 1303 (1994).
58. *Id.* at 1315-16.

the lienholder's security interest, recognized in a default judgment against Alpine, could be recognized as encumbering only Alpine's ownership interests in the property encumbered. The court went on to rule the Oil Well Lien Act is a statute of peremption.[59] Peremption is a time limit for the existence of a right, and unless it is timely exercised, the right is extinguished. The suit against Alpine did not interrupt peremption against the intervenors in this litigation. Thus, the lienholder's lien rights had been extinguished by the passage of time.

VI. CONSERVATION REGULATION[60]

A. *Louisiana Well Cost Statute*

A complex issue of well costs was resolved in *Tex/Con Oil & Gas Co. v. Batchelor.*[61] This case arose from revisions of units in the South Lake Arthur Field. The revisions changed the ownership interests in the units as new acreage was brought in and some acreage was taken out. A dispute arose over the method of allocating well costs among the new and former owners of interests in the units. The commissioner applied the "dollar-for-dollar" method of depreciation. Under this approach, the actual reasonable well cost was reduced by the amount of monies received from the prior production on the original unit, less severance taxes. Because the money received from production exceeded the reasonable well costs for each well, the commissioner concluded the cost chargeable by the owners of the original units to the subsequent owners of the revised units was zero.[62]

The owners of the original units sought judicial review and won a temporary reversal. The trial court ruled Louisiana Revised Statutes 30:10(A)(2) and the custom and usage of the industry require the application of the unit of production depreciated well cost reduction method of accounting. Under this method, well costs are reduced by the percentage of depletion of the unit's total recoverable reserves caused by production prior to unit revision. The appellate court, however, reinstated the commissioner's order based on the "dollar-for-dollar" method and rejected the trial court's determination that as to certain owners the dollar-for-dollar method would constitute a taking of property by the state without just compensation. The court concluded the commissioner had properly applied the then-applicable version of the statute, which mandated the commissioner apply the dollar-for-dollar method of depreciation.[63] Louisiana Revised Statutes 30:10(A)(2)(d), as it then existed, dictated that well costs "be reduced

59. *Id.* at 1316.
60. La. R.S. 30:10 (1989 & Supp. 1995).
61. 634 So. 2d 902 (La. App. 1st Cir. 1993), *writ denied,* 635 So. 2d 1102 (1994).
62. *Id.* at 904-05. *See also* Desormeaux v. Inexco Oil Co., 298 So. 2d 897 (La. App. 3d Cir.), *writ refused,* 302 So. 2d 37 (1974).
63. *Tex/Con Oil & Gas Co.*, 634 So. 2d at 908-09. The two methods are discussed in Robert T. Jorden, *Unit Well Cost Adjustment in Louisiana*, 38 La. Min. L. Inst. 82 (1992).

to account for monies received from prior production"; this phraseology contemplated use of the dollar-for-dollar method of determining well costs.

It should be noted Louisiana Revised Statutes 30:10(A)(2)(d) was amended by Act 595 of 1991. As the appellate court observed in this case,[64] the amendment changed the phrase "shall be reduced to account for monies received from prior production" to "shall be reduced in the same proportion as the recoverable reserves in the unitized pool have been recovered by prior production." This amendment evidences a clear change in the method of determining well costs to a unit of production well cost reduction method and provides further support for the court's conclusion that prior to the 1991 amendment, Louisiana Revised Statutes 30:10(A)(2)(d) mandated the use of the dollar-for-dollar method.

B. *Balancing of Natural Gas*

In *Hunt Oil Co. v. Batchelor*,[65] the litigation arose from revisions of units in the South Lake Arthur Field that changed the ownership interests in the units; new acreage was brought in and some acreage was taken out. The hearings were concluded on October 18, 1989, but the order was not issued until January 22, 1990. The order was effective as of October 18, 1989, but substantial production of natural gas took place between that date and the January 22, 1990 issuance of the order (the "critical period"). A dispute arose over how to account to new owners for the production that took place in this period. The overproduced parties contended there should be balancing-in-kind, allowing the underproduced parties to take a disproportionate share of the gas and sell it themselves to make up for the period for which they were underproduced. The underproduced parties sought a cash accounting based on what the overproduced parties actually realized from the sale of the gas during the critical period.[66] Applying the criteria of prior cases,[67] the court found cash balancing was necessary where the underproduced party could not have taken the gas at the time of production and an inordinate amount of time would have been required for balancing-in-kind to have been effected.[68] The court concluded "balancing in kind would be unfair and unjust in this case because plaintiffs would further lose the time value of money."[69] The Louisiana Supreme Court had granted a writ for review of this case at the time of this publication. Perhaps the supreme court court will consider the possibility of a reversal of circumstances in which the overproduced

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64. *Tex/Con Oil & Gas Co.*, 634 So. 2d at 908.

65. 633 So. 2d 259 (La. App. 1st Cir. 1993), *rev'd*, 644 So. 2d 191 (1994).

66. *Id.* at 260.

67. Amoco Prod. Co. v. Thompson, 566 So. 2d 138 (La. App. 1st Cir.), *writs denied*, 571 So. 2d 627, 628 (1990); Amoco Prod. Co. v. Thompson, 516 So. 2d 376 (La. App. 1st Cir. 1987), *writs denied*, 520 So. 2d 118, 118 (1988).

68. *Hunt Oil Co.*, 633 So. 2d at 262.

69. *Id.*

party insists on cash balancing in a time of rising gas prices, while the underproduced party seeks balancing-in-kind. A rule that favors balancing-in-kind is likely to be more fair overall than a rule that favors underproduced or overproduced parties.

C. Operator's Relationship to Nonoperator

Three interrelated cases[70] have resulted in several decisions holding the operator of a compulsory unit who sells unit production must account to unleased owners under a theory of quasi-contract rather than conversion. Because the plaintiffs were treated as unleased owners, the operator was obligated to account in money rather than through a balancing-in-kind. All three cases grew out of certain of the same facts reported in *Taylor v. Woodpecker Corp.*[71] The issue involved whether an unleased mineral interest owner has a right or cause of action against a purchaser of unit production to recover the value of his share. The unit involved in the litigation was a forty-acre unit established in 1942 by Order No. 24-D. In 1979 a well was drilled on acreage within the 1942 unit by E. C. Wentworth, and Ashland purchased production from the well. In 1986 the lessor-plaintiffs (Taylors) filed a lawsuit against their lessee, Woodpecker Corporation, and against Wentworth, the well operator, which led to the supreme court decision noted above.[72] This current phase of the litigation arose in 1991 when the plaintiffs filed suits against Wedon Smith and David New Operating Company, Inc., and a suit against E. C. Wentworth and Woodpecker Corporation that was transferred to a different district because of the naming of the state agency as a third party defendant. Common to all three reported decisions was the defendants' assertions that the plaintiffs' claims were governed by a one-year prescriptive period applicable to conversion. The appellate courts in all three cases held the obligation of the unit operator to a nonoperator under the pooling statute gives rise to an action in quasi contract.[73] Since the operator had the legal right to sell the production of the nonoperator, it would not be appropriate to apply the prescriptive period that governs wrongful taking or conversion. One of the courts further stated:

> We agree that LSA-R.S. 30:10 A(3) gives an unleased landowner a cause of action in quasi contract under these Civil Code articles. The unit operator acts as a *negotiorum gestor* or manager of the owner's business in selling the owner's proportionate share of oil and gas produced. In return for the right to sell the share of production of the

70. Taylor v. Woodpecker Corp., 633 So. 2d 1308 (La. App. 1st Cir. 1994); Taylor v. David New Operating Co., 619 So. 2d 1251 (La. App. 3d Cir.), *writ denied*, 625 So. 2d 1046 (1993); Taylor v. Smith, 619 So. 2d 881 (La. App. 3d Cir.), *writ denied*, 625 So. 2d 1038 (1993).

71. 562 So. 2d 888 (La. 1990).

72. *Id.* at 889-90.

73. *Woodpecker Corp.*, 633 So. 2d at 1313; *David New Operating Co.*, 619 So. 2d at 1255; *Smith*, 619 So. 2d at 888.

unleased landowner, the unit operator is obligated by law "without any agreement" to pay the unleased landowner his proportionate share of proceeds within 180 days of the sale of production. The "purely voluntary act" of assuming the position of unit operator, and thereby obtaining the right to sell the unleased interest owner's share of production, results in this obligation to account to the unleased interest owner pursuant to LSA-R.S. 30:10 A(3).[74]

D. Doctrine of Primary Jurisdiction Applied

Based on the decision in *Magnolia Coal Terminal v. Phillips Oil Co.*,[75] the United States Court of Appeals for the Fifth Circuit, in *Mills v. Davis Oil Co.*,[76] has ruled the doctrine of primary jurisdiction is followed in Louisiana as a matter of substantive law which the federal courts are bound to follow. The case grew out of a sheriff's sale of a tract of land, a portion of which had been included in a unit. The sale had the effect of extinguishing a lease. The former lessee was required to pay for the value of the production it had obtained, less the costs of production. Controversy arose over the proper costs, and the district court declined to exercise jurisdiction over Mills' well cost dispute and instead deferred the matter to the Commissioner of Conservation. Under Louisiana law,[77] such deference is a matter within the sound discretion of the trial court. The court held "Louisiana's doctrine of primary jurisdiction is substantive and it required the lower court to exercise its discretion as if it were a Louisiana state court."[78] The plaintiff claimed $11,735,000 in civil penalties under Louisiana Revised Statutes 30:10(A)(3). These were properly denied by the court, as those civil penalties were applicable to violations of the conservation statute.

The court's opinion reflects a matter of confusion in the minds and writings of some Louisiana attorneys. The court refers to "the Louisiana Mineral Code" when citing to a section of Title 30 of the Revised Statutes.[79] This is incorrect. The Louisiana Mineral Code is that body of articles found in Title 31 that were enacted initially in 1974.[80] The sections of Title 30 pertaining to the authority of the Commissioner of Conservation and to conservation regulation generally are more properly referred to as the "conservation statute" (though in fact a series of statutes are reflected therein).

74. *Woodpecker Corp.*, 633 So. 2d at 1313.

75. 576 So. 2d 475 (La. 1991).

76. 11 F.3d 1298 (5th Cir. 1994). See also La Plaque Corp. v. Chevron U.S.A. Inc., 638 So. 2d 354 (La. App. 4th Cir. 1994), discussed *supra* text accompanying notes 50-52 (applying the primary jurisdiction doctrine to an issue related to Federal Energy Regulatory Commission authority).

77. *See, e.g.*, *Magnolia Coal Terminal*, 576 So. 2d at 489 (denying application for rehearing).

78. *Mills*, 11 F.3d at 1304.

79. *Id.* at 1305.

80. Article 1 of the Louisiana Mineral Code, La. R.S. 31:1 (1989).