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# Royalty Division Orders

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it, parol evidence is admissible to locate the property. With respect to intervening rights of third parties, the problem is whether the description in the recorded act of sale sufficiently identifies the property to put third parties on notice of prior transactions involving the property. The identifying description required for this purpose must often be more specific than that required between the parties. The attributes of a written description which identifies the property sufficiently to meet each of these situations cannot be conclusively stated; the situation has apparently not changed since 1872 when the Supreme Court said: "We are not prepared to fix the line between valid and invalid or sufficient and insufficient descriptions, which shall serve as a guide in all future cases. Each case must depend on its own circumstances."[48]

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## ROYALTY DIVISION ORDERS

### INTRODUCTION[1]

Complex division in the ownership of petroleum production is the rule rather than the exception. The speculative value of undeveloped minerals; the prevalence of the oil and gas lease, with its provision for the lessor's royalty, as the means by which the developer acquires his interest; the use of the overriding royalty and the production payment as vehicles for profit in lease brokerage and as means of obtaining financing for development; all contribute to the difficult problem of apportioning the revenue from mineral production in the petroleum industry.[2] The instruments by which various parties have acquired their respective interests in the production should, of course, govern the apportionment of the revenues of production. But the un-

48. Consolidated Ass'n of Planters v. Mason, 24 La. Ann. 518, 520 (1872).

1. For purposes of this paper any party entitled to a share in production revenues is considered a royalty owner. "Seller" and "purchaser," unless otherwise indicated, refer to the royalty owner as seller and the pipeline owner as purchaser under the royalty division order. "Lessor" will be substituted for "seller" when referring to royalty payment rights under a lease.

2. *E.g.*, divided ownership may result from a lessor's 1/8 lease royalty (Cheek v. Metzer, 116 Tex. 356, 291 S.W. 860 (1927)), subsequent conveyances (Texas Co. v. Leach, 219 La. 613, 53 So. 2d 786 (1951)), or unitization (Dobbins v. Hodges, 208 La. 143, 23 So. 2d 26 (1945); Robinson v. Horton, 197 La. 919, 2 So. 2d 647 (1941)). One oil property in the Oklahoma City Field is reportedly shared by 750 royalty owners. GLASSMIRE, OIL AND GAS LEASES AND ROYALTIES 312, § 83 (2d ed. 1938).

certainties created by these instruments frequently discourage prospective purchasers of production. To remove these uncertainties and facilitate sale of production, the industry has developed a specialized contract for sale of production designed to afford protection to the purchaser by apportioning the price among the sellers, normally[3] in proportion with their respective interests in the minerals produced. This agreement, known as a royalty division order, is a contract to sell all production delivered to a transporting pipe line, stipulating to whom and in what proportions the purchase price is to be paid.[4] The royalty owner's freedom to contract for sale of produced oil may be limited either by the contract under which he holds or by industry conventions. For example, a mineral lessee's agency powers[5] or a working-interest owner's powers[6] may permit the operator to negotiate initially for all royalty owners in creating a purchase agreement with a pipe line owner as purchaser. After negotiations for the sale of the oil and a title examination, the purchaser normally requires execution of a royalty division order to assure proper distribution of royalty proceeds and to protect himself from multiplicity of claims. Although division orders are extensively utilized in Louisiana, there is little jurisprudence on the effects of Louisiana contract and sales law on them; these effects will be the subject of this Comment.

## General Provisions

Common law jurisdictions consider the division order a con-

3. In certain situations the proportion of the proceeds due may not be equivalent to the mineral ownership, as in the case where heirs of deceased grant surviving spouse with usufruct of property the right to the proceeds through the division order.

4. Wagner v. Sunray Mid-Continent Oil Co., 182 Kan. 81, 318 P.2d 1039 (1957); Stanolind Oil & Gas Co. v. Terrell, 183 S.W.2d 743 (Tex. Civ. App. 1944).

5. Leases usually provide for the lessee to deliver the royalty oil to the purchaser's pipeline and receive payments as agent for the lessor. Tremont Lumber Co. v. Louisiana Oil Ref. Corp., 187 La. 454, 175 So. 25 (1937). Even though the lease may not authorize the lessee to sell the lessor's royalty oil to a purchaser, if the lessor provides no storage facilities, the lessee is impliedly authorized to sell as agent. Wolfe v. Prairie Oil & Gas Co., 83 F.2d 434 (10th Cir. 1936); Wolfe v. Texas Co., 83 F.2d 425 (10th Cir. 1936); Sohio Petroleum Co. v. United States & P. R.R., 222 La. 383, 62 So. 2d 615 (1953). These provisions are found in the royalty clause of the lease. In addition to duties pertaining to delivery of the lessor's oil in kind, the royalty clause contains a provision that requires the lessee to account to the lessor for payment of the latter's 1/8 royalty. This provision forms the basis of substantial portions of subsequent discussion.

6. In the case of royalty carved out of the working interest, the working interest owner, as result either of contract provision or industry convention, has power to act as agent in selling production until a purchasing agreement is perfected between the purchaser and the individual royalty owners.

tract to sell production runs.[7] Each owner of an interest entitled to a portion of production agrees to sell his designated portion of production, warranting the title thereto, in return for a stipulated price or consideration determined by the prevailing market price. Significantly, the division order is not a sale of accrued or unaccrued royalty,[8] but rather a contract to sell oil as produced and delivered to purchaser's pipeline; the sale is complete only upon delivery. The contract is usually held terminable at the will of either party unless the contrary is stipulated.[9]

The elements of the royalty division order requiring most intensive examination are: (a) provision that any dispute concerning the seller's title to the minerals authorizes the purchaser to withhold payment without interest until title is determined, unless the seller furnishes a satisfactory indemnity bond; (b) provision that the purchaser is not bound by any transfer of interest or change of ownership until he receives a transfer order and recorded instrument evidencing such transfer; (c) warranty by each seller that he is the legal owner of the proportion of production set forth opposite his name; (d) authorization of the purchaser to take all production, crediting each seller in proportion to the amount opposite his name.[10]

## WITHHOLDING PAYMENTS

Common law jurisdictions uphold judicially the provision permitting a purchaser to withhold payments without interest if any dispute regarding the seller's title to the royalty arises.[11]

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7. Wagner v. Sunray Mid-Continent Oil Co., 182 Kan. 81, 318 P.2d 1039 (1957); Simpson v. United States Pipe Line Co., 196 Miss. 356, 17 So. 2d 200 (1944).

8. Williams Adm'r v. Union Bank & Trust Co., 283 Ky. 644, 143 S.W.2d 297 (1940); Thompson v. Thompson, 149 Tex. 632, 236 S.W.2d 779 (1951); Hogg v. Magnolia Petroleum Co., 267 S.W. 482 (Tex. Civ. App. 1924). See 8 OIL & GAS REP. 377 (1957), 7 OIL & GAS REP. 41 (1956). *But cf.* Robbins v. Martin, 18 La. App. 223, 138 So. 132 (2d Cir. 1931) (division orders estopped seller from questioning prior partial conveyance).

9. Snider v. Snider, 208 Okla. 231, 255 P.2d 273 (1953); Marlarnee v. Pauline Oil & Gas Co., 133 Okla. 192, 271 Pac. 937 (1928); Welch v. Pauline Oil & Gas Co., 133 Okla. 122, 271 Pac. 651 (1928).

10. 3 SUMMERS, OIL AND GAS 137 (1957). Several other pertinent provisions excluded from this Comment, are: (e) provision for termination of the order on written notice by the seller (or, occasionally, by either party); (f) requirement that the seller notify the purchaser of suits affecting title to the minerals and indemnify the latter against all costs incurred defending such suits; (g) provision that production is to become the property of the purchaser on delivery.

11. Wolfe v. Prairie Oil & Gas Co., 83 F.2d 434 (10th Cir. 1936); Wolfe v. Texas Co., 83 F.2d 425 (10th Cir. 1936).

However, literal enforcement of the provision grants unfair advantage to unscrupulous third party claimants; since even a frivolous extra-judicial claim of title authorizes withholding royalty payments, the beleaguered royalty owner may be forced to accept an unjust settlement to escape harassment.[12]

Louisiana has apparently legislated with this possibility in mind. Revised Statutes 30:105-107[13] make unlawful withholding of required royalty payments to royalty owners unless a suit testing title to the interest has been filed, and provides for mandamus to compel payment of "rentals, royalties, or other sums due."[14] These statutes virtually eliminate the withholding provision as an instrument of third-party harassment, since a title claimant will rarely undertake the trouble and expense of litigation unless he has some reasonable basis for his claim.[15]

## TRANSFER OF OWNERSHIP

### *Public Records Doctrine*

Revised Statutes 30:106 further provides that the oil purchaser is "fully protected" by making payments under the division order to the last record owner.[16] There seems little doubt

12. GLASSMIRE, OIL AND GAS LEASES AND ROYALTIES 223, § 60 (2d ed. 1938).

13. LA. R.S. 30:105-107 (1950). See discussion in text accompanying notes 16-19 *infra*.

14. The right to such extraordinary relief has, however, been judicially limited. The Supreme Court has required that the "sums due" must be definite, fixed, and certain — liquidated or capable of liquidation by simple mathematical calculation. State *ex rel.* Superior Oil Co. v. Texas Gas Transmission Corp., 242 La. 315, 136 So. 2d 55 (1962); State *ex rel.* Brown v. United Gas Pub. Serv. Co., 197 La. 616, 2 So. 2d 41 (1941); State *ex rel.* Boykin v. Hope Producing Co., 167 So. 506 (La. App. 2d Cir. 1936). The *Superior* case held that mandamus was not available where there was no contract between claimant and defendant, because the requirement of definite price was not met. The court did not deny a remedy existed, but merely held that mandamus under LA. R.S. 30:107 (1950) was not the proper one. In *Brown* and *Boykin* it was held that mandamus was not the appropriate remedy where the lessor alleged royalties due in excess of those stipulated in the lease. See generally Comment, 4 LA. L. REV. 304 (1942); see Irion v. Standard Oil Co., 199 La. 363, 6 So. 2d 143 (1942).

15. This legislation seems part of a well-integrated system for protection of both royalty owner and oil purchaser in the event of title disputes. The seller is protected against economic pressure associated with unmeritorious claims to royalties. Concomitantly, the purchaser is protected in that he may withhold payments after suit has been filed.

16. LA. R.S. 30:106 (1950): "A person producing minerals under a lease granted by the last record owner and holding under an instrument sufficient in terms to transfer title to the land or mineral rights, shall be presumed to have derived his record from the true owner. A purchaser of minerals produced from a recorded lease . . . shall be fully protected in making payment to any party in interest under the lease unless and until . . . suit [between owner and claimant] should be filed and the purchaser receives notification of it by the usual postal registry receipt card. The purchaser shall not be entitled to this protection unless

that the legislature, through enactment of this provision, intended to extend the protection afforded by the public records doctrine to transfers of royalty division orders.[17] The extension seems justified because the division order, though a contract to sell movables, is closely related to immovables; protecting the division order supplements the protection afforded immovables[19] and lends stability to the titles of record owners of immovable property and to oil and gas industry marketing practices.

### *Transfer-of-Ownership Clause*

The transfer-of-ownership clause provides that the purchaser under a division order is not bound by transfer of interest or change of ownership until a transfer order and recorded instrument evidencing the transfer are received;[20] it complements the withholding provision. Since the withholding provision does not protect the oil purchaser against a transferee of the record owner who records the conveyance but does not give notice, the transfer-of-ownership clause is necessary.[21] The royalty owner's transferee takes subject to recorded restrictions, one of which is the division order, and thus it seems he cannot claim royalty payments until the proper notice is given.[22]

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he has recorded in the conveyance records of the parish in which the land is located, notice that the minerals have been and will be bought by him."

17. State *ex rel.* Brown v. United Gas Public Service Co., 197 La. 616, 2 So.2d 41 (1941); State *ex rel.* Bean v. Caddo Oil Purchasing Corp., 189 So. 333 (La. App. 2d Cir. 1939); State *ex rel.* Muslow v. Louisiana Oil Ref. Corp., 176 So. 686 (La. App. 2d Cir. 1937). *Bean* held that § 106 was passed in the interests of royalty owners, lessees *and the purchasers of oil,* and that upon filing of the requisite purchasing notice the purchaser would be protected against non-record ownership claimants for all proceeds paid to the record owner.

18. Division orders are the consequences of divided ownership of production, which in turn is the resultant of mineral servitudes, royalty sales, and leases — in this context immovable transactions. Mineral servitudes and mineral royalty are held real rights, thus subject to the rules applicable to immovable things, including the protection afforded by recordation. Vincent v. Bullock, 192 La. 1, 187 So. 35 (1939); Frost-Johnson Lumber Co. v. Salling's Heirs, 150 La. 756, 91 So. 207 (1922). LA. R.S. 9:2721 (1950) has spelled out the public records doctrine protection applicable to mineral leases.

19. See, *e.g.,* LA. R.S. 9:2721, 2722, 1105, 4811, 5101, 5102 (1950).

20. Such provisions usually delay the effectiveness of a royalty transfer until notice of it is received by the purchaser. Standard Oil Co. v. Craig, 202 Ark. 168, 150 S.W.2d 744 (1941); Amerada Petroleum Corp. v. Melton, 139 Okla. 119, 281 Pac. 591 (1929); Tide Water Associated Oil Co. v. Hammer, 163 S.W.2d 232 (Tex. Civ. App. 1942); Sun Pipe Line Co. v. Wood, 129 S.W.2d 704 (Tex. Civ. App. 1939). However, if the purchaser does not heed the notice of change of ownership, no subsequent protection is afforded by the provision. Shell Petroleum Corp. v. Royal Petroleum Corp., 135 Tex. 12, 137 S.W.2d 753 (1940); McLean v. Texas Co., 103 F.2d 989 (5th Cir. 1939).

21. LA. R.S. 30:105-107 (1950) require payment to the last record owner.

22. It is arguable that such transferee becomes a record owner and is thereby entitled to claim royalty from the oil purchaser who, under LA. R.S. 30:105-107

WARRANTY

Under the warranty clause[23] each seller warrants title to his stipulated share of production runs. The function of this clause is evident; the purchaser of oil and gas from a person not entitled to them may be subject to damages for unlawful taking.[24] Under the sales articles of the Louisiana Civil Code, a seller warrants the purchaser's peaceable possession of the thing sold, unless the contrary is stipulated.[25] If the buyer is then evicted, the seller is liable to restore the price, return the fruits and revenues returned to the evictor by the buyer, and pay all costs occasioned by the suit. Additionally, "damages . . . besides the price . . . paid" are recoverable.[26] Upon suit against the purchaser by a third person, the purchaser may "bring in any person . . . who is his warrantor" as a party to the action.[27] Delivery of production pursuant to the division order results in a sale governed by these sales provisions. Therefore, a purchaser attacked by a third person claiming ownership of his share of production runs should be entitled to call his vendor in warranty to defend the action.[28]

CO-SIGNERS' RELATIONSHIP

In common law jurisdictions each co-signer of a royalty division order contracts to sell, and warrantys title to, only his own

(1950), is only protected when making payment to the last record owner. If this position should prevail, the transfer-of-ownership clause might assume the character of an indemnity agreement permitting the oil purchaser to require indemnification of the transferor.

If the change of title were not recorded but notice of title transfer were forwarded to the purchaser and the purchaser continues to pay the last record owner, there should be no charge of wrongful taking since the statutory provisions of payment to the last record owner have been met. However, the oil purchaser has breached the contract in failing to pay royalty to the vendee, for which damages should lie. However, such situations seem unlikely as a vendee of producing oil property is not apt to fail to give notice of his acquisition to the purchaser or to record his title.

23. The warranty clause is also referred to as the "their respective interest" clause. See note 32 *infra.*

24. Hughes v. United Pipe Lines, 119 N.Y. 423, 23 N.E. 1042 (1890).

25. LA. CIVIL CODE arts. 2475, 2476, 2500 (1870).

26. *Id.* art 2506.

27. LA. CODE OF CIVIL PROCEDURE art. 1111 (1960).

28. Though this remedy is available, its value may be curtailed by insolvency of the alleged royalty owners. This sometimes inadequate protection, the desire to do away with frivolous claims, and the important policy behind creation of stable market conditions for the Louisiana petroleum industry seem to have been instrumental in the high degree of protection given by LA. R.S. 30:106 (1950) to the purchaser who pays the last record owner. Though this warranty may provide little practical protection, reliance on the public records substantially protects the purchaser.

stipulated share of production runs.[29] No legal relationship is created between co-signers.[30] Under the first principle, no co-signer is responsible for a failure of another co-signer's title. Under the second, a co-signer is not precluded by signing an inaccurately apportioned division order from recovering against another co-signer unjustly enriched.

Both principles are probably valid in Louisiana. Dictum in *Ferrell v. Simms*[31] suggests Louisiana will view the contract as creating legal relationships only between each seller and the purchaser. In any event, the division order apparently negates the idea of solidary warranty as it provides that the parties warrant title only to "their respective interests."[32] The absence of contractual ties between co-signers should eliminate any preclusion that would hinder one co-signer's seeking restitution from another.

## INACCURATE APPORTIONMENT

### *General Provisions*

Occasionally, a division order will erroneously allocate to a seller a smaller proportion of production payments than his proportionate ownership of production runs, allocating the excess to another seller.[33] The injured seller might seek redress against

29. 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); Chicago Corp. v. Wall, 156 Tex. 217, 293 S.W.2d 844 (1956); Allen v. Creighton, 131 S.W.2d 47 (Tex. Civ. App. 1939).

30. Wagner v. Sunray Mid-Continent Oil Co., 182 Kan. 81, 318 P.2d 1039 (1957); Simpson v. United States Pipe Line Co., 196 Miss. 356, 17 So. 2d 200 (1944).

31. 209 La. 1072, 26 So. 2d 143 (1946). In attempting to invalidate a division order, plaintiff-seller contended that Ferguson, a co-signer, had not received the proportion due him under the order. After determining Ferguson had received the correct proportion, the court concluded that in any event the division of Ferguson's royalty interest did not affect the other landowners' rights.

32. Some lawyers preparing division orders strike or leave out the "their respective interests" portion of the warranty clause apparently with the intention of requiring each signer to warrant title to all production — not just to his stipulated interest. Neither Louisiana nor the common law jurisdictions have determined the effect of this deletion. However, in an analogous situation it has been suggested that the warranty would be binding where the owner of an undivided interest in fee executes a lease in which the lessee requires him to warrant title to all of the fee. WILLIAMS, OIL AND GAS LAW 573, § 503.3 (1959). Though it seems unlikely that a lessor would knowingly enter such an agreement, principles of freedom to contract seem to permit it. However, as warranting a more extensive title than that conveyed is unusual, it should be suspect, particularly so where the warranty results from a mere deletion or omission. Consequently, it is suggested that the attempted enlargement of the warranty protection should be effective only if the division order unequivocally states that each party is to warrant title to *all* mineral produced.

33. The discussion is limited to those inaccurate apportionments producing

the purchaser; against the lessee for breach of the obligation to pay under the royalty clause of the lease; or against the party receiving the overpayment under the inaccurately apportioned division order on a theory of unjust enrichment.

*Common Law.* — In common law jurisdictions a seller who signs an inaccurately apportioned division order is held estopped to claim the excess against the purchaser.[34] Further, a royalty owner, by signing the division order as seller, relieves his lessee of the duty to pay royalty under the lease, and accepts instead the obligation of the purchaser to pay under the terms of the division order.[35] However, the injured seller may recover from an unjustly enriched recipient the increment of production payments to which the injured seller was entitled.[36]

*Louisiana.* — Though the jurisprudence and legislation are insufficient to reach definitive conclusions, it seems Louisiana will follow these common law rules. *Brown v. Sugar Creek Syndicate*[37] apparently determined that estoppel by contract would be applicable to cases of inaccurate apportionment. By signing the division order the seller was held estopped to contest the accuracy of the apportionment in an action against the pur-

deficiencies in one royalty owner's proportionate ownership and a corresponding excess in another's — errors in curative and title work and certain types of clerical errors, *e.g.*, transposition. The type of clerical error normally complained of, though, results in a deficiency without corresponding excess, such that in effect the purchaser is the party unjustly enriched in not having disbursed one hundred per cent of the proceeds. It would seem the unjustly enriched purchaser would readily reform the contract according to the correct apportionment. Randazzo v. Ins. Co. of Pennsylvania, 196 La. 822, 200 So. 267 (1941); Giovanovich v. Breda's Heirs, 149 La. 402, 89 So. 251 (1921). For general survey of reformation of instruments in Louisiana, including reformation for clerical errors, see Comment, 30 TUL. L. REV. 486 (1956).

34. Dale v. Case, 217 Miss. 298, 64 So. 2d 344 (1953); Chicago Corp. v. Wall, 156 Tex. 217, 293 S.W.2d 844 (1956). Estoppel by contract prevents the party asserting a fact in the document from taking a position inconsistent therewith and detrimental to the other party. BIGELOW, ESTOPPEL 495 (6th ed. 1913). It should be noted that the seller may terminate the agreement at any time, and thus assert a claim to his proper share thereafter. See note 10 *supra*.

35. Amerada Petroleum Corp. v. Melton, 139 Okla. 119, 281 Pac. 591 (1929); Houston Lighting & Power Co. v. Liberty Pipe Line Co., 71 S.W.2d 393 (Tex. Civ. App. 1934); Texas Co. v. Beall, 3 S.W.2d 524 (Tex. Civ. App. 1927); 4 WILLIAMS, OIL AND GAS LAW § 705 (1962). *But see* Indian Territory Illuminating Oil Co. v. Killingsworth, 175 Okla. 78, 51 P.2d 505 (1935). This effect on the royalty clause appears to be an exception rather than the rule, as most lease provisions are unaffected by a royalty division order. 4 WILLIAMS, *id.* § 706. *E.g.*, Louisiana Live Stock & Planting Co. v. Kendall, 155 La. 122, 98 So. 862 (1923) (express drilling covenant).

36. 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); Chicago Corp. v. Wall, 156 Tex. 217, 293 S.W.2d 844 (1956); Allen v. Creighton, 131 S.W.2d 47 (Tex. Civ. App. 1939).

37. 195 La. 865, 197 So. 583 (1940).

chaser.[38] Recovery against the lessee also seems precluded in Louisiana, as in common law jurisdictions. Though no cases were found directly on point, it seems clear that a division order accomplishes a substitution of debtors, thus effecting a novation of that part of the lease providing for payment of royalties. Though a novation is not to be presumed[39] it may be effected by acts of a creditor that clearly evidence an intent to look no longer to the original debtor for payment.[40] Contractual substitution of one debtor for another — purchaser for lessee — seems adequate to show a clear intent no longer to look to the original debtor for payment.[41] Finally, recovery for unjust enrichment is available under Article 2301 of the Civil Code.[42]

### *Lessee-Purchaser*

*General Provisions.* — When a lessee is also the purchaser it may be necessary to distinguish his rights and duties in each capacity.[43] Suppose a lessee is obligated to pay 1/16 of produc-

38. The court's authority for its position came from decisions declaring that parties to an agreement are bound by the terms thereof. *E.g.*, Mims v. Sample, 191 La. 677, 186 So. 66 (1939); Sam George Fur Co. v. Arkansas-Louisiana Pipeline Co., 177 La. 284, 148 So. 51 (1933); Robbins v. Martin, 18 La. App. 223, 138 So. 132 (1931). Though none of the decisions dealt with royalty division orders the concept of contract estoppel seems equally applicable to all valid written contracts. As the agreement is terminable at the will of either party (see note 10 *supra*) the seller may effectively prevent a recurrence of inadequate payments by terminating the old and requiring a new agreement.

39. LA. CIVIL CODE arts. 2190, 2192 (1870); White Co. v. Hammond Stage Lines, 180 La. 962, 158 So. 353 (1934).

40. Strunk Chain Saws, Inc. v. Williams, 111 So. 2d 195 (La. App. 2d Cir. 1959) involved a substitution of debtors that the defendant contended worked a novation. In reply to the plaintiff's contention that novations are not to be presumed the court stated: "[O]ur courts have not adhered to the strict construction contended for . . . but have ruled a release or discharge can be evidenced by acts of a creditor clearly disclosing an intent to no longer look to the original debtor for payment." *Id.* at 197.

41. It may be argued that rather than a substitution of debtors the division order effects a change in the lessee's liability from primary to secondary. However, as uniformity in the area of mineral law between Louisiana and her surrounding common law states appears desirable, where conceptually permissive, an interpretation which would produce such uniformity should be favored.

42. LA. CIVIL CODE art. 2301 (1870). *Cf. id.* arts. 1965, 2292-2294. Article 2301 serves as foundation for any action to recover for unjust enrichment by providing that "he who receives what is not due to him, whether he receives it through error or knowingly, obliges himself to restore it to him from whom he has unduly received it." Application of this statute should allow recovery by the injured seller against the enriched seller for breach of a quasi-contractual obligation. See LA. CIVIL CODE arts. 2311, 1934 (1870). See also Greenfield Box Co. v. Independence Veneer & Box Mfg. Co., 163 La. 86, 111 So. 608 (1927); Standard Oil Co. v. Sugar Products Co., 160 La. 763, 107 So. 566 (1926); Crammer v. Fidelity & Cas. Co., 18 So. 2d 220 (La. App. 2d Cir. 1944).

43. *E.g.*, Stanolind Oil & Gas Co. v. Terrell, 183 S.W.2d 743 (Tex. Civ. App. 1944) (where lessee was also purchaser, provisions of division order limiting lessor's rights as provided in lease did not prevail; lessor entitled to royalty payments without tax deductions as per lease).

tion to lessor *A* and 1/16 to lessor *B* under the royalty clauses of separate leases, but the lessee is also purchaser under a signed division order allocating 1/32 of the proceeds of sale to *A* and 3/32 to *B*.

Common law courts have not differentiated between lessee-purchasers and third-party purchasers; the lessee is relieved of the royalty obligation in both situations.[44] Additionally, in his capacity as purchaser the lessee is protected by contract estoppel. No court appears to have considered the possibility that a lessee who prepares an erroneously apportioned division order should, on the basis of equitable estoppel, be held to his duty to pay under the lease, or, should, in his capacity as purchaser, equitably be denied the protection of contract estoppel. It seems, however, that in any case the doctrine of equitable estoppel is not applicable to the lessee-purchaser situation.[45] While novation seems clearly appropriate to relieve a Louisiana lessee from his royalty obligation in the third-party purchaser situation,[46] a strong argument can be made that a lessee-purchaser should not be similarly relieved.

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For ease of reference in this section the lessee-purchaser will be called the lessee, and in the lessor-seller will be called the lessor.

44. Amerada Petroleum Corp. v. Melton, 139 Okla. 119, 281 Pac. 591 (1929). However, if the lessee is the party enriched, he is protected neither by the substitution of debtors nor the doctrine of estoppel. Stanolind Oil & Gas Co. v. Terrell, 183 S.W.2d 743 (Tex. Civ. App. 1944). See also 7 OIL & GAS REP. 69, 71 (1957), 1 OIL & GAS REP. 1175 (1952). It should be remembered that since the order is revocable the lessor may reimpose an obligation upon the lessee in this respect by revoking the order.

45. If the lessee has misled the lessor to the latter's detriment, the lessee may be estopped to deny his duty to pay under the lease. However, for equitable estoppel to be successfully asserted there must exist either false representation or concealment of material facts, made with actual or constructive knowledge of the facts; the party to whom it was made must have been without knowledge of, or the means of knowing, the real facts; it must have been made with the intention that it be acted upon; and, the party to whom it was made must have relied or acted upon it to his prejudice. BIGELOW, ESTOPPEL c. XVIII, § 1 (6th ed. 1913); 31 C.J.S. *Estoppel* § 122 (1942). For the Louisiana position on estoppel by conduct see Little v. Barbe, 195 La. 1071, 198 So. 368 (1940); Parker v. Ohio Oil Co., 191 La. 896, 186 So. 604 (1939); Succession of Valdes, 44 So. 2d 151 (La. App. Orl. Cir. 1950); Jones v. Alford, 172 So. 213 (La. App. 2d Cir. 1937). See generally Note, 15 LA. L. REV. 855 (1955). Normally the lessor could not successfully contend he had no knowledge of the facts as he had in his possession both the division order and the lease and could easily have compared the royalty fractions apportioned to him by each. Furthermore, the lessee-purchaser generally has not intentionally misrepresented the facts as this apparently requires a state of mind akin to fraud. BIGELOW, ESTOPPEL 648 (6th ed. 1913). Finally, no estoppel arises where the representation or conduct of the party sought to be estopped results from ignorance founded upon an innocent mistake, usually the case in a division order dispute. 31 C.J.S. *Estoppel* § 128 (1942). Thus in the normal situation the requisites of equitable estoppel will not be present.

46. See text at note 39 *supra*.

*Mistake in the Principal Cause.* — As previously indicated, a lessee's duty to pay lease royalty in Louisiana is displaced, on the principle of novation, by the payment provisions of the division order.[47] Termination of the division order, which can be accomplished unilaterally, revives the lease royalty obligation.[48] Nullity of the division order should retroactively reinstate the lessee's obligation to pay royalty under the lease.[49] It is submitted that an inaccurately apportioned division order is null for mistake in the principal cause in the lessee-purchaser situation, though not in the third-party purchaser situation.

Mistake concerning the principal cause for contracting is a vice of consent permitting invalidation of the agreement by the party suffering under the vice,[50] if "the other party was apprised that it was the principal cause of the agreement, or unless from the nature of the transaction it must be presumed that he knew it."[51] The seller's principal cause in contracting a sale is receipt of the price. Obviously a lessor signing a division order intends to receive the price of his full share of production as provided by the lease. This is his principal cause.[52] Therefore the critical issue is whether the lessee-purchaser who signs a division order as purchaser should be held to know that the lessor's principal cause for signing the division order is to receive the undelivered price of the lease.

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47. See text at note 40 *supra.*

48. The principle of contractual estoppel, said previously to prevent the lessor's contesting the agreement with the purchaser, requires that the agreement be a valid contract; if invalid, there can be no estoppel based on its terms. BIGELOW, ESTOPPEL 495 (6th ed. 1913). However, it does not seem that invalidation of the division order will expose the purchaser to liability for conversion. As the lessee's duties under the royalty clause are in a sense reactivated, so too are his agency powers. Thus, the lessee may sell oil to the purchaser *for the lessor.* The purchasing executed during the supposed existence of the division order may be valid under the agency powers, so that no conversion by the purchaser would result.

49. See first paragraph note 55 *infra.* This seems true unless it could be proved that the lessor intended receipt of the smaller amount under the division order to satisfy fully the existing debt under the lease, thus effecting a remission. Acceptance by the lessor of less than the full obligation due him may relieve the lessee of his full obligation, as a creditor may accept less than full payment as settlement for a debt. Jones v. Southern Natural Gas Co., 213 La. 1051, 36 So. 2d 34 (1948). However, remission of a debt is not presumed but must be expressed. LA. CIVIL CODE art. 2199 (1870) ; C. O. Black Inc. v. Swink, 197 So. 693 (La. App. 2d Cir. 1940). Thus, mistakenly accepting the smaller royalty will not satisfy the debt unless such is the lessor's intention. Jones v. Southern Natural Gas Co., *supra.*

50. LA. CIVIL CODE arts. 1819, 1823-1826 (1870).

51. LA. CIVIL CODE art. 1826 (1870).

52. It is frequently held that a mineral lessor's object in leasing, the consideration, is to receive the payments due under the lease. Davis v. Laster, 242 La. 735, 138 So. 2d 558 (1962) ; Melancon v. Texas Co., 230 La. 593, 89 So. 2d 135 (1956) ; Roberson v. Pioneer Gas Co., 173 La. 313, 137 So. 46 (1931) ; Saunders v. Busch-Everett Co., 138 La. 1049, 71 So. 153 (1914).

Pretermitting the issue of actual knowledge, it surely can be said of the lessee-purchaser that "from the nature of the transaction it must be presumed that he knew of it."[53] As lessee he knows the lessor's price for leasing includes the lease royalty. When he assumes the role of purchaser, he should still be held to have his lessee's knowledge that the full lease price is undelivered.[54] Should the lessee-purchaser be held apprised of the lessor-seller's principal cause, the remedy for this error in principal cause is rescission based upon the nullity of the division order. Lessee's fulfillment of the payment obligation under the lease should be required as though the division had never affected it.[55] Consequently, recovery for any loss previously sustained due to inaccurate apportionment should be available against the lessee.

53. LA. CIVIL CODE art. 1826 (1870).

54. This area may be further complicated by the problem of imputed corporate knowledge.

55. Pretermitting questions of equities of third persons relying on the division order, nullifying the division order necessarily nullifies all the sales thereunder, as between seller and purchaser, resulting in the purchaser having bought the oil without authority. On the theory that the lessee's duty to pay royalty is relieved by the purchaser's under the division order, nullifying the division order should nullify this substitution, particularly since the lessee cannot be considered a third party relying on the conduct and contracts of another. Consequently, the nullification, in effect, results in the lessee having sold the production runs to the purchaser but not having paid the proper price therefor. Under such situations, the lessee/purchaser's defenses of substitution of debtors and contract estoppel should be denied and liability imposed for the improper payment.

It should be noted that the above discussion concerning the effect of an error in recited apportionment presupposes that the recitation of each signer's interest in the division order represents the *price* of the contract — that the consideration for making the agreement is to receive, *e.g.*, 5% of the total sale price of all the oil produced by the well with this percentage represented by the interest figure found opposite each owner's name. An alternative presupposition is possible, but it presents novel problems. It is possible that the agreement simply declares that each signer grants the purchaser the right to take 5% of the oil from the area covered by the division order. This approach supposes that the "interest" represents *title*, *i.e.*, it is merely a descriptive designation, rather than a price. Such a result would require extensive application of Louisana property law rather than obligations law, with potential problems beyond the scope of this paper. To illustrate, however, one problem will be considered. Suppose the signer owns 7% royalty interest in a well, but signs a division order reciting only 5% interest opposite his name? He would contend that he in no way indicated that he owns only 5% interest, but rather he owns another 2% which the purchaser has been converting. Is this analogous to the situation which an owner of 7 acres of land sells 5, and the purchaser claims all 7? It is submitted that it is not and that such problems do not arise, as the interest recitation is in fact a stipulation of the entire price owed the seller by the purchaser. The division orders of the Tennessee Gas Transmission Company, which appear representative of the petroleum industry, state the purchaser is "hereby authorized to receive and sell all oil produced from the above described property and *to give credit for, in the proceeds*, as directed below." (Emphasis added.) In effect the seller declares that the purchaser is authorized to purchase *all* the oil taken from the well and delivered to him, and in consideration he must pay the seller a fraction of the total sale value of the oil. As this fraction is the total price requested by

It may be argued that cancellation for mistake in the principal cause is applicable to third party purchasers as well, on the following theory: during the title examination that precedes circulation of a division order the purchaser necessarily discovers the lease in question and is thereby constructively apprised that the lessor's principal cause for signing the division order is to receive the undelivered lease price. However, the writer feels it is better policy to limit cancellation for mistake in principal cause to the lessee-purchaser situation. As constructive notice depends on the "nature of the transaction," a meaningful distinction between the two purchaser situations is realized from their differing factual settings. It seems, therefore, that where the purchaser's only knowledge of the lease royalty comes from a lease discovered in a title search he should not be held to know of an error in the principal cause as he should be where he has also promised to pay the lease royalty.

*Termination of the Lease.* — It has been held that "failure to pay production royalties under an oil and gas lease, for any appreciable length of time, without justification, amounts to an active breach of such lease which entitles the lessor to cancellation thereof without necessity of placing the lessee in formal default."[56] Thus if a division order is annulled for mistake in the principal cause, the lessee would be chargeable with failure to pay full production royalties due under the lease during the order's duration and possibly subjected to cancellation. However, the court in *Jones v. Southern Natural Gas Co.*[57] held that failure to properly pay delay rentals, which was a consequence of an innocent mistake in accounting, amounted to "justification" and cancellation was refused. In light of the trend in recent jurisprudence apparently glossing over the distinctions between delay rentals and production royalty, drawing upon this merely analogous principle seems legally permissive and consistent.[58] It is suggested, therefore, that although an innocent

the seller, the principle of contractual estoppel is applicable to prevent a demand for a larger price. It seems clear then that the interest recitation is a designation of price rather than a description of property.

56. Bailey v. Meadows, 130 So. 2d 501, 508 (La. App. 2d Cir. 1961). Recently another appeal court reaffirmed the rule by permitting cancellation without putting in default for a failure to pay production royalties for seven months without justification. Pierce v. Atlantic Ref. Co., 140 So. 2d 19 (La. App. 3d Cir. 1962).

57. 213 La. 1051, 36 So. 2d 34 (1948) (assignee of lease paid lessor inadequate delay rentals due to mistake regarding total number of acres assigned; lessor's cancellation denied; held, payments delayed through accident or mistake do not justify cancellation).

58. Though there has historically been variant legal effect in decisions deal-

mistake in a division order may result in its nullity, the lease on the property which it covers should not be subject to termination for nonpayment of royalty while the division order was in force.

### *Non-Lessor Royalty Owner*

A non-lessor royalty owner is not entitled to the benefit of the covenants in the lease concerning payment of royalty unless he is a party to the agreement or is made a third party beneficiary.[59] Thus the royalty owner has no basis for asserting liability of the lessee. The purchaser will be protected against such an interest holder's claiming a larger interest by the doctrine of contractual estoppel,[60] for he is a party to the contract to sell contained in the division order. However, the injured royalty owner has recourse against the party unjustly enriched by the overpayment.[61]

*John J. Graham*

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ing with delay rentals, production royalty and shut-in payments, the net effect of recent court of appeal and Supreme Court decisions is to extenuate the distinctions between these lease payments. *E.g.*, Bailey v. Meadows, 130 So. 2d 501 (La. App. 2d Cir. 1961) and Pierce v. Atlantic Ref. Co., 140 So. 2d 19 (La. App. 3d Cir. 1962) allowed cancellation of mineral leases for failure to pay production royalties without requiring default, which is precisely the result reached in decisions cancelling leases for failure to pay delay rentals, though different reasoning was relied on. Davis v. Laster, 242 La. 735, 138 So. 2d 558 (1962), concerned with failure to pay shut-in gas payments, applied principles pronounced in a decision as applicable to delay rentals. Furthermore as the courts frequently consider royalty payments equivalent to rent, all three lease payments may apparently be considered rental payments. *E.g.*, Milling v. Collector of Revenue, 200 La. 773, 57 So. 2d 679 (1952); Roberson v. Pioneer Gas Co., 173 La. 313, 137 So. 46 (1931); Board of Commissioners of Caddo Levee District v. Pure Oil Co., 167 La. 801, 120 So. 373 (1928); Logan v. State Gravel Co., 158 La. 105, 103 So. 526 (1925).

59. Fry v. Farm Bureau Oil Co., 3 Ill. 2d 94, 119 N.E. 2d 749 (1954); Kile v. Amerada Petroleum Corp., 118 Okla. 176, 247 Pac. 681 (1925); Ebberts v. Carpenter Prod. Co., 256 S.W. 2d 601 (Tex. Civ. App. 1953), 2 OIL & GAS REP. 726, 740 (1953).

60. Dale v. Case, 217 Miss. 298, 64 So. 2d 344 (1953); Chicago Corp. v. Wall, 156 Tex. 217, 293 S.W. 2d 844 (1956).

61. 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); Chicago Corp. v. Wall, 156 Tex. 217, 293 S.W. 2d 844 (1956); Allen v. Creighton, 131 S.W. 2d 47 (Tex. Civ. App. 1939). See note 42 *supra*.