CURRENT ISSUES UNDER THE LOUISIANA LAW OF OIL AND GAS

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Patrick S. Ottinger
OTTINGER HEBERT, L.L.C.
P. O. Drawer 52606
1313 West Pinhook Road (70503)
Lafayette, Louisiana 70505-2606
(337) 232-2606
e-mail: psottinger@ohllc.com

Member, Louisiana and Texas Bars

Adjunct Professor of Law, Paul M. Hebert Law Center
Louisiana State University
Baton Rouge, Louisiana

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"The meek shall inherit the Earth, but not its mineral rights."[1]

I. Introduction

"Current Issues Under the Louisiana Law of Oil and Gas." Now, that's a bit of an ambiguous (or is it ambitious?) title. The only thing on today's agenda that is more pervasive or amorphous is "Lunch."

The issues identified herein could as easily be called today's "Hot Topics in Louisiana Mineral Rights," and, on occasion, your presenter will so characterize them in the pages that follow.

First, a bit of context and background. As used in the jargon of the industry in Louisiana, the term "mineral rights" is usually understood to mean distinctly a mineral servitude, properly speaking.[2] Hence, it is

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[1] J. Paul Getty (1892-1976).

[2] "A mineral servitude is the right of enjoyment of land belonging to another for the purpose of exploring for and producing minerals and reducing them to possession and ownership." LA. REV. STAT. ANN. § 31:21. *See also* PATRICK S. OTTINGER, *Mineral Servitudes*, Louisiana Mineral Law Treatise, § 404 (Martin, ed., Claitor's Law Books & Publishing Division, Inc., 2012) (hereinafter cited as "Ottinger, *Mineral Servitude Treatise*").

often said that the “vendor reserved his mineral rights,” when it is actually envisioned that a mineral *servitude* was reserved by that seller of land.

For example, the Supreme Court in one case noted that, “[o]n March 15, 1926, the Louisiana Central Lumber Company, . . ., transferred the whole 80,000 acres to the Brown Paper Mill Company, reserving . . . all of the *mineral rights* in the land transferred.”[3]

In another case, the court referred to the dispute before it as involving a party’s “reserved *mineral rights*,” in which the plaintiffs were “seeking a declaratory judgment that the *servitude created by reservations* in the sale included only the right to explore for and exploit oil, gas and kindred minerals and not the right to explore for or strip mine for solid minerals such as lignite.”[4]

Finally, another court examined the precursor statute to article 149 of the Louisiana Mineral Code,[5] describing it as having been “enacted . . . to make imprescriptible mineral servitudes that were created when landowners *reserved mineral rights* in a sale of land to school boards and other named agencies of the state.”[6]

With the adoption of the Louisiana Mineral Code, effective January 1, 1975,[7] the term “mineral rights” now embraces three distinct real rights that are classified as incorporeal immovables.[8] In this regard, article 16 of the Mineral Code provides that the “basic mineral rights that may be created by a landowner are the mineral servitude, the mineral royalty, and the mineral lease.”[9]

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[3] *Lenard v. Shell Oil Co.*, 29 So. 2d 844, 845 (La. 1947). (Emphasis added.).

[4] *Continental Group, Inc. v. Allison*, 404 So. 2d 428, 430 (La. 1981), *writ den’d* 456 U. S. 906 (1982). (Emphasis added.).

[5] LA. REV. STAT. ANN. § 31:149.

[6] *Anadarko Production Co. v. Caddo Parish School Board*, 455 So. 2d 699, 700 (La. App. Ct. 2d), *writ den’d* 460 So. 2d 610 (La. 1984). (Emphasis added.).

[7] Act No. 50, 1974 La. Acts Vol. III, effective January 1, 1975.

[8] “Rights and actions that apply to immovable things are incorporeal immovables. Immovables of this kind are such as personal servitudes established on immovables, predial servitudes, mineral rights, and petitory or possessory actions.” LA. CIV. CODE ANN. art. 470.

[9] LA. REV. STAT. ANN. § 31:16.

There is yet another mineral right, albeit not characterized by the Code as being "basic," making it somewhat akin to the "Uncola," or the "other white meat" of oil and gas, both of Madison Avenue fame. That is the "executive right," defined in article 105 of the Code as "the exclusive right to grant mineral leases of specified land or mineral rights."[10]

Mineral Code article 106 explicitly characterizes the executive right as a mineral right, thus invoking the attributes specified in article 16 for those interests as being "real rights [that] are subject either to the prescription of nonuse for ten years or to special rules of law governing the term of their existence."[11] Article 18 provides the further characterization of the executive right as being an incorporeal immovable that is alienable and heritable.[12]

Hence, in view of the foregoing, an unnecessarily longer title to this presentation might be "Current Issues in Louisiana Mineral Servitudes, Mineral Royalties, Mineral Leases, and Executive Rights," but let's agree to simply stick with the shorter moniker, and just call it *potpourri*.[13]

II. Current Issues Involving Mineral Servitudes

A. Altering a Mineral Servitude's Duration: Fixed Term, or Shortening of Prescription?

Louisiana is a civil law system, in contrast to Texas and the remaining states that are based in the common law.[14] Accordingly, in Louisiana, it is not possible to own or hold a so-called "mineral estate," as such is incompatible with fundamental principles of the civil law of property, which tend toward certainty, and disfavor the dismemberment or

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[10] *Id*. at § 31:105. *See* PATRICK S. OTTINGER, *Louisiana Mineral Leases: A Treatise*, Ch. 7 (Claitor's Law Books & Publishing Division, Inc., 2016) (hereinafter cited as "Ottinger, *Mineral Lease Treatise*").

[11] LA. REV. STAT. ANN. § 31:16.

[12] *Id*. at § 31:18.

[13] "A mixture of things, especially a musical or literary medley."

[14] For excellent commentary on the fundamental differences between the two systems of law, *see* Patrick H. Martin and J. Lanier Yeates, *Louisiana and Texas Oil & Gas Law: An Overview of the Differences*, 52 LA. L. REV. 769 (March 1992).

fractionalization of title.[15] Indeed, as long ago as 1853, our Supreme Court resisted the introduction or recognition of different regimes of ownership of land, saying, as follows:

> The general idea of property under the Roman Law, and under our system, in that of simple, uniform and absolute dominion. The subordinate exceptions of use, usufruct and servitudes are abundantly sufficient to meet all the wants of civilization, and there is no warrant of law, no reason of policy, for the introduction of any other.[16]

Rather, what one might own is a "mineral servitude"[17] that is subject to being extinguished if not "used" for a period of ten years.[18] Utilizing a common law notion of "forever," a mineral servitude might actually exist in perpetuity (a term that does not appear in the Louisiana Civil Code), unless ten years elapse without a "use."[19]

In one of the few opportunities afforded contracting parties to modify the attributes of a mineral servitude, article 74 of the Louisiana Mineral Code provides:

> Parties may fix the term of a mineral servitude or shorten the applicable period of prescription

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[15] *Wemple v. Nabors Oil & Gas Co.*, 97 So. 666 (La. 1923) ("And we therefore conclude that there is in this state no such estate in lands as a corporeal 'mineral estate,' distinct from and independent of the surface estate; that the so-called 'mineral estate' by whatever term described, or however, acquired or reserved, is a mere servitude upon the land in which the minerals lie, giving only the right to extract such minerals and appropriate them."). *Id*. at 669.

[16] *State v. McDonogh's Ex'rs*, 8 La. Ann. 171, 251 (La. 1853).

[17] *See supra* note 2.

[18] "A mineral servitude is extinguished by: (1) prescription resulting from nonuse for ten years; . . .." LA. REV. STAT. ANN. § 31:27(1). *See* Ottinger, *Mineral Servitude Treatise*, § 408(1). Louisiana's regime of prescription of nonuse is akin to a sort of statute of limitations, resulting in the termination or extinguishment of rights if no "use" is made of the mineral servitude for the pertinent period of time.

[19] A "use" of a mineral servitude is the drilling of a well or production. A dry hole can constitute a "use" if it meets the standards for a "good faith operation." *See* Part II.B hereof.

> of nonuse or both. If a period of prescription greater than ten years is stipulated, the period is reduced to ten years.[20]

If parties "fix the term," the mineral servitude comes to an end upon the accrual of that stated term, even if there then exists an activity that would otherwise perpetuate the servitude.

If, instead, parties merely "shorten the applicable period," the mineral servitude can still be perpetuated by a use accomplished within that shorter period, and so on, but it will thereafter extinguish if the truncated time period accrues without a use.

A few cases in recent years have taken up the issue of whether parties, in availing themselves of this right of "freedom of contract," intended to "fix the term" of the mineral servitude, or to merely "shorten the applicable period of prescription of nonuse."[21]

The case of *St. Mary Operating Co. v. Champagne*[22] was a concursus proceeding that was filed to determine the ownership of proceeds of production allocable to a mineral servitude that had been created "for a period of ten years."[23] As stated by the court, the issue was, as follows:

> Under the Louisiana Mineral Code, does the phrase in a cash sale document, "for a period of 10 years," create a fixed, ten-year term, not subject to prescription, or is this phrase a reaffirmation of the parties' adoption of the regular ten-year prescriptive period, making it subject to interruption?[24]

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20 LA. REV. STAT. ANN. § 31:74. *See* Ottinger, *Mineral Servitude Treatise*, § 415.

21 *See* Ottinger, *Mineral Lease Treatise*, § 3-08(b).

22 945 So. 2d 846 (La. App. Ct. 3d 2006), *writ den'd* 954 So. 2d 140 (La. 2007).

23 A "concursus proceeding" is essentially an interpleader, brought by a stakeholder to judicially resolve competing claims to money or property. *See* Ottinger, *Mineral Lease Treatise*, § 13-45.

24 945 So. 2d at 848.

The trial court held that "the reservation clause in the cash sale deed reserved a servitude for a fixed term that was not subject to the rules of prescription."[25] "Therefore, it could not be perpetuated beyond ten years by the good-faith exploration for minerals within the ten-year period beginning on the date the servitude was established."[26]

The mineral servitude owners appealed, and the judgment of the trial court was reversed. The appellate court held that "[t]he phrase 'for a period of ten years' was a restatement of the default prescriptive period assumed into all mineral rights created in the State of Louisiana because the parties did not specifically state otherwise."[27]

The court further held, as follows:

> The mineral servitude reserved to them in the cash sale deed is still active and valid because the ten-year prescriptive period was interrupted when mining activities began in March of 2003, within ten years of its creation on June 22, 1993. Accordingly, the mineral servitude will continue to exist until there is a ten-year lapse in the use of the servitude.[28]

At dispute in *Moffett v. Barnes*,[29] was whether a mineral servitude was subject to a 10-year term that was "fixed."

The plaintiffs owned two tracts of land that they purchased from the defendants. The act of sale stated, "Vendor retains all oil, gas and other mineral rights in the land herein conveyed for ten (10) years."[30]

The defendants granted mineral leases covering the tracts, and the lessees drilled and established production on each tract before the tenth anniversary of the plaintiffs' purchase of the land.

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25 *Id*.

26 *Id*.

27 *Id*. at 851.

28 *Id*.

29 149 So. 3d 475 (La. App. Ct. 2d 2014).

30 *Id*.

The plaintiffs argued that the act of sale's statement that the defendants retained mineral rights "for ten (10) years" established a 10-year fixed term. Accordingly, the plaintiffs posited that the mineral servitudes terminated on the tenth anniversary of the act of sale, regardless of the existence of production.[31]

The trial court disagreed, ruling that the servitudes were not subject to a fixed term, and that prescription had been interrupted by drilling operations conducted, and production obtained, by the defendants' lessees.

Affirming, the appellate court stated that the act of sale's reservation "merely confirm[ed] the normal 10-year limit for a servitude, and does not reject or renounce the normal operation of nonuse and interruption provided by the law."[32]

The court rejected the plaintiffs' contention that they should have been allowed to present evidence regarding the intent of the parties, stating that the act of sale was unambiguous, and therefore evidence of intent was not appropriate.[33]

Taylor v. Morris[34] is a case with facts very similar to those presented in *Moffett*. However, it was decided by a different panel of the same appellate court.

This panel similarly held that an act of sale referring to a "period of ten (10) years" did not establish a fixed term, but instead merely referred to the law's default prescriptive period.[35]

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[31] "A mineral servitude is extinguished by: (4) expiration of the time for which the servitude was granted; . . .." LA. REV. STAT. ANN. § 31:27(4). *See* Ottinger, *Mineral Servitude Treatise*, § 408(4).

[32] 149 So. 3d at 478.

[33] *See* Ottinger, *Mineral Lease Treatise*, § 1-16, for a thorough discussion of the "parol evidence exclusionary rule."

[34] 150 So. 3d 952 (La. App. Ct. 2d 2014).

[35] *See supra* note 18.

Notably, one judge submitted a concurring opinion stating that, under the court's decision, "the literal words for a term period of years are being avoided and effectively interpreted out of the contract,"[36] but that such a result was justified "[i]n this unusual setting."[37]

The concurring judge identified two conceivable interpretations in cases under article 74, one being the "Prescription Construction" ("the presumption that the parties were only referring in their contract to such normal prescription"),[38] and the other being the "Literal Construction" ("words as literally expressing a term that could extinguish the servitude.").[39] He ordained the former as the "priority construction," saying, as follows:

> However, in the absence of such clarifying extrinsic evidence, I would hold that the near absurdity of a fixed-term mineral servitude on land, undeveloped for oil and gas, should make the Prescription Construction the priority interpretation which a court should apply.[40]

While this approach would certainly be workable, it is discordant with case law that suggests that, in case of two possible constructions, the court should adopt that interpretation that tends to unburden the land.[41] In a close case, the rule of interpretation is that "[d]oubt as to the *existence, extent, or manner of exercise* of a predial servitude shall be resolved in favor of the servient estate."[42]

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36 150 So. 3d at 959.

37 *Id*.

38 *Id*. at 960.

39 *Id*.

40 *Id*. at 961.

41 *See*, *e.g.*, *Whitehall Oil Co. v. Heard*, 197 So. 2d 672, 678 (La. App. Ct. 3d), *writ den'd* 199 So. 2d 923 (La. 1967) ("Ultimately, we conclude that, where the instrument could as reasonably be interpreted either way, the proper interpretation is that which least restricts the ownership of the land conveyed, as in the case of mineral servitudes.").

42 LA. CIV. CODE ANN. art. 730 (emphasis in original), made applicable to the mineral servitude by LA. REV. STAT. ANN. § 31:2.

Moral of the Story — Lessons to be Learned

If a party avails itself of one of the limited opportunities in the Mineral Code to contractually alter the intrinsic features of a mineral servitude, the scrivener should take care to express clearly the intention of the parties—that is, to expressly state whether the servitude is being subjected to a strict, fixed term, or that the prescription period is being shortened (remaining subject to the usual rules of use).[43]

If, for example, parties to a mineral servitude wish to use a six-year period rather than the default period of ten years, this could be accomplished by including language as simple as one or the other of the following alternative constructs, *viz*.:

> It is the intention of the parties that the prescriptive period is shortened to six years, but is otherwise subject to the usual rules of nonuse.
>
> OR
>
> It is the intention of the parties that the reserved mineral servitude is subject to a fixed term of six years.

The principal consequence of the fixing of a term is that any mineral lease granted by such servitude owner would concomitantly come to an end, regardless of the existence of a well situated on the servitude tract. This is an illustration of the doctrine of "conditional title."[44]

B. Interruption of Prescription by Good Faith Operations: Is the Test, Objective or Subjective?

Article 29 of the Mineral Code specifies that a "dry hole" may interrupt prescription if it meets the following requirements for a "good faith operation," to-wit:

> The prescription of nonuse running against a mineral servitude is interrupted by good faith

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[43] *See* Ottinger, *Mineral Servitude Treatise*, § 415.

[44] "A mineral lease may be granted by the owner of an executive interest whose title is extinguished at a particular time or upon the occurrence of a certain condition, but it terminates at the specified time or on occurrence of the condition divesting the title." LA. REV. STAT. ANN. § 31:117.

> operations for the discovery and production of minerals. By good faith is meant that the operations must be
>
> (1) commenced with reasonable expectation of discovering and producing minerals in paying quantities at a particular point or depth,
>
> (2) continued at the site chosen to that point or depth, and
>
> (3) conducted in such a manner that they constitute a single operation although actual drilling or mining is not conducted at all times.[45]

To be noted is that the requisites for "good faith" are expressed in the conjunctive, such that each distinct element must be satisfied. While elements (2) and (3) are essentially "mechanical," and are easily discerned as having been met (or not), element (1) is different in character in that it requires an evaluation of the *reasonableness* of the *expectation* of the party using the servitude.[46]

Concerning the element of "reasonable expectation" on the part of the party drilling the well, is this to be adjudged on an "objective" or a "subjective" basis?

A recent case considered, but did not resolve, this issue.

In *Indigo Minerals, LLC v. Pardee Minerals, LLC*,[47] a mineral servitude was created on 8,000 acres in December 1971; only four sections were at issue in the suit.

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45 *Id*. at § 31:29.

46 "Except as provided in Articles 44 through 52, use of a mineral servitude must be by the owner of the servitude, his representative or employee, or some other person acting on his behalf." *Id*. at § 31:42. *See* Ottinger, *Mineral Servitude Treatise*, § 411.

47 37 So. 3d 1122 (La. App. Ct. 2d), *writ den'd* 46 So. 3d 1274 (La. 2010). In the interest of full disclosure, your presenter represented the plaintiff in this suit. *See* Ottinger, *Mineral Servitude Treatise*, § 409(3).

Wells were drilled on the lands burdened by the servitude in 1980, 1989, and 1998. While all of the wells were dry holes, of particular relevance was the Famcor Well that was spud on December 4, 1998; drilled to a total depth of 3,586', and plugged and abandoned as a dry hole on December 15, 1998.

The surface owner, and the owner of a servitude that it later created in 2006, challenged the continued viability of the 1971 mineral servitude.

In particular, the plaintiffs contested whether certain of the dry holes, albeit timely commenced, constituted "good faith operations," as contemplated by article 29 of the Mineral Code.

Defendants offered expert testimony that the wells in question were drilled with a "reasonable expectation," based essentially on a geological evaluation from distant or remote fields in which production had been obtained—in other words, objective evidence. Defendants did not demonstrate that the wells in the remote fields (in some cases, several parishes distant from the tracts involved) were geologically relevant or correlative to the lands in dispute.

Plaintiffs presented deposition testimony and documentary evidence that the driller "had evidence and knowledge in its possession at the time of the drilling of its well which demonstrated that production in the more shallow formations was not expected."[48] That is to say, subjective evidence was presented in support of the parties challenging the continued existence of the mineral servitude.

After extensive discovery, cross motions for summary judgment were filed. The trial court granted the defendants' motion for summary judgment, and denied the motion by plaintiffs.

On appeal, the Second Circuit, Court of Appeal, reversed that motion for summary judgment, finding the existence of issues of fact that precluded its entry.[49]

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[48] 37 So. 3d at 1127.

[49] "As to both the Sutton Well and the Famcor Well, there are genuine issues of material fact as to the reasonable expectation, at the time the wells were commenced, of discovering and producing minerals in paying quantities at the levels to which the wells were drilled." *Id*. at 1132.

At issue was whether the "reasonable expectation" standard of article 29 is to be evaluated objectively or subjectively.

Moral of the Story — Lessons to be Learned

Writs having been denied by the Louisiana Supreme Court,[50] and because the case was a reversal of a summary judgment (and not a decision on the merits), the resolution of this important issue awaits another day.

Subsequent to this decision reversing a summary judgment, certain parties (including the named plaintiff) settled and were dismissed, but the case was ultimately tried by the remaining parties who did not settle. On February 1, 2017, the jury found that the Famcor Well (drilled in December 1998) was not "a good faith operation for the discovery and production of minerals." The jury having accepted the plaintiffs' evidence (subjective), the case is not authority for the proposition that objective evidence would never be considered. As of the date of this presentation, the case is not yet final.

Issues not completely resolved, given the procedural context of the case, are the following:

- Whether the "reasonable expectation" standard of article 29 is to be evaluated objectively or subjectively.

- Whether there is a presumption of good faith applicable to the activities of the servitude owner.[51]

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50 *Supra* note 47.

51 Early cases seem to suggest that the servitude owner who demonstrates the timely existence of a dry hole, is entitled to a "presumption of good faith." *Keebler v. Seubert*, 120 So. 591, 592 (La. 1929) ("There is nothing justifying the conclusion that the operations were not conducted in good faith."); *Lynn v. Harrington*, 192 So. 517, 519 (La. 1939) ("Taking all these things into consideration along with the legal presumption of good faith," . . .), and *Kellogg Bros., Inc. v. Singer Manufacturing Co.*, 131 So. 2d 578, 580 (La. App. Ct. 2d 1961) ("Without denying the existence of the presumption" of good faith, . . .). This presenter does not believe these cases remain authoritative for this proposition.

- Who has the burden of proof as to compliance with the standards of article 29?[52]

C. Liability of Servitude Owner for Damages to Land

Article 22 of the Mineral Code provides, as follows:

> The owner of a mineral servitude is under no obligation to exercise it. If he does, he is entitled to use only so much of the land as is reasonably necessary to conduct his operations. He is obligated, insofar as practicable, to restore the surface to its original condition at the earliest reasonable time.[53]

In *Dupree v. Oil, Gas & Other Minerals, Inc.*,[54] a suit for damages to growing crops, roads, and culverts was brought by the surface owner against the lessors of a mineral lease, and their lessee. After the lessee filed for bankruptcy, the lessee was dismissed by the plaintiff following the joinder of the owners of the mineral servitude.

The trial court granted motions for summary judgment filed by the servitude owners on the basis that, following the execution of a mineral lease, the lessee, as the only party entitled to explore for and produce minerals, is the only party that may be liable for surface damages.

At issue on appeal was the liability of a mineral servitude holder to the surface owner for damages caused by the former's mineral lessee. The court of appeal refused to excuse the servitude owners from the statutory obligation to restore the surface imposed by article 22. The court reasoned that the servitude owners benefited from the lessee's activities, which interrupted the running of prescription on the servitude only several months before its extinguishment.

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52 *See* Ottinger, *Mineral Servitude Treatise*, § 411.

53 LA. REV. STAT. ANN. § 31:22.

54 731 So. 2d 1067 (La. App. Ct. 2d), *writ den'd* 749 So. 2d 635 (La. 1999).

Moreover, the court noted that the mineral lease expressly obligated the lessee to indemnify the lessors for claims by the landowner, and the court refused to allow the servitude owners to benefit from the interruption of prescription while avoiding the obligations of article 22 of the Mineral Code.

Reversing the summary judgment in favor of the servitude owners, the court of appeal held that an owner of a mineral servitude may be liable for damages to the surface of land burdened by a mineral servitude that were caused by its lessee.

Moral of the Story — Lessons to be Learned

As many mineral servitudes are held by parties who were formerly owners of the land, but who have sold the land and created a mineral servitude by reservation in the sale, the implications on the "servitude owner" could be quite extreme. In other words, a servitude owner is not always—perhaps is virtually never—a Fortune 500 company, but is an individual, a married couple, or (dare I say it), a voter in local judicial elections. He or she who is, at one moment, the owner of the land, becomes, after the closing of the transaction, the owner of a mineral servitude (and no longer a landowner), and probably is one who was not educated or informed by the closing lawyer as to the potential consequences or exposure to the owner of the surface.

A lawyer representing a vendor of land, in which a mineral servitude is created by reservation in favor of that lawyer's vendor-client, should advise the soon-to-be servitude owner of the potential for restoration liability.

When the servitude owner grants a mineral lease, it should endeavor to exercise its right of "freedom of contact" so as to create a contractual undertaking in its favor whereby the lessee expressly obligates itself to protect the lessor by assuming its obligations to the surface owner under article 22 of the Mineral Code, and indemnifying the lessor-servitude owner from any claims by the surface owner.[55]

Another "current" issue is the temporal meaning of "original condition" as used in the last sentence of article 22 of the Mineral Code, quoted above. That is to say, to what point in time is the land's condition

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[55] The important principle of "freedom of contract" is addressed in Part I of Chapter Two of Ottinger, *Mineral Lease Treatise*.

to be evaluated if E&P operations had occurred, and had been ongoing, for a period of time *prior* to the establishment of the mineral servitude?

A recent trial court ruling indicates that the servitude owner's responsibility "to restore the surface to its original condition" means the condition of the property at the creation of the servitude—and not the property's condition prior to the conduct of operations.

In *Sterling Sugars Inc. v. Amerada Hess Corp.*,[56] E&P operations on the subject property had been underway and occurring more than forty years before a mineral servitude was created in 1979. Clearly, the condition of the property in 1979 was significantly different than the land's condition prior to the first conduct of drilling operations on the burdened land decades before.

The plaintiff landowner sued the present mineral servitude owner in 2012, and argued that, under article 22, the servitude owner was required to restore the property to its "original condition" as of the 1930s—before the commencement of oil and gas operations.

The court rejected this argument, concluding that "the phrase 'original condition' in Article 22 is tied to the exercise of a servitude and means the condition in which it was originally found by the servitude owner immediately before the servitude is exercised."[57]

D. Imprescriptible Minerals Arising Out of Expropriation

On first blush, amendatory legislation in 2012[58] would not seem to have much relevance as a "current" issue in the Louisiana law of oil and gas, or mineral rights, in that it amends certain sections of Title 19 of the Revised Statutes, Expropriation, including (relevant for our immediate purposes) Section 2 that identifies the types of juridical persons enjoying the power of expropriation.[59]

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[56] Civil Docket No. 100,091, 17th Judicial District Court, Lafourche Parish, Louisiana.

[57] Amended Judgment, July 14, 2017.

[58] Act No. 702, 2012 La. Acts 2921.

[59] Expropriation in Louisiana-speak is condemnation or eminent domain in Texas jargon.

This Act made numerous procedural and other changes to the law of expropriation (including a change to the so-called "*St. Julien* Doctrine"),[60] but for our immediate purposes, your presenter deems it appropriate to highlight only one change made to the statute.

Signed by the Governor on June 11, 2012,[61] Act No. 702 amended Louisiana Revised Statutes section 19:2 so as to expand the "created for" standard of eligibility for the right to expropriate, in order to now include a legal entity that is "engaged in" certain specified activities.

We must first digress. Article 149 of the Louisiana Mineral Code deals with a mineral servitude that is not subject to the prescription of non-use. Basically, if land is acquired by an "acquiring authority," and the vendor reserves minerals in such transaction, the "prescription of the mineral right is interrupted as long as title to the land remains with the acquiring authority, or any successor that is also an acquiring authority."[62]

As stated, these are euphemistically called "imprescriptible minerals,"[63] and constitute a statutory innovation dating back to the acquisition of vast quantities of lands in the '30's and '40's in connection with public works projects. The statutes were intended to put Louisiana landowners on a par with their Texas counterparts who had the ability—not enjoyed in Louisiana—to create a perpetual mineral estate.

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[60] Taking its name from the decision in *St. Julien v. Morgan Louisiana & Texas Railroad Co.*, 35 La. Ann. 924 (La. 1883), this doctrine stands for the proposition that a landowner who acquiesces in the installation of facilities on its property by a party having the power of expropriation, forfeits the right to demand the removal of the facilities and is relegated to a claim for money damages. Later overruled by *Lake, Inc. v. Louisiana Power and Light Co.*, 330 So. 2d 914 (La. 1976), the doctrine is now codified in LA. REV. STAT. ANN. § 19:14.

[61] This legislation became effective on August 1, 2012.

[62] LA. REV. STAT. ANN. § 31:149B.

[63] One should note the inconsistent terminology employed in article 149. In one instance, reference is made to the servitude's "imprescriptibility" – that is, that it is *not* subject to prescription at all. *Id*. In another instance, it states that the "prescription of the mineral right is interrupted as long as title to the land remains with the acquiring authority, or any successor that is also an acquiring authority," a formulation suggestive of the notion that it is afflicted with pre-scription. *Id*.

As defined in article 149, an “acquiring authority” includes, in addition to the Federal and State governments (and certain political subdivisions thereof), “any legal entity with authority to expropriate or condemn, except an electric public utility acquiring land without expropriation.”[64]

Louisiana Revised Statutes section 19:2 specifies the types of “legal entity with authority to expropriate or condemn,” and, hence, clarifies which non-governmental legal entities would constitute an “acquiring authority” as envisioned by Mineral Code article 149.

Prior to this legislation in 2012, those juridical persons included certain entities that were “created for” certain specific purposes, *e.g.*, the construction of railroads, toll roads, or navigation canals; the construction and operation of street railways, urban railways, or interurban railways; the construction or operation of waterworks, filtration and treating plants, or sewerage plants to supply the public with water and sewerage; the piping and marketing of natural gas for the purpose of supplying the public with natural gas; the purpose of transmitting intelligence by telegraph or telephone; the purpose of generating, transmitting and distributing or for transmitting or distributing electricity and steam for power, lighting, heating, or other such uses, and piping and marketing of coal or lignite in whatever form or mixture convenient for transportation within a pipeline.

In view of the foregoing, prior to 2012, it was both necessary and sufficient to examine the organizational papers of a legal entity involved in such a transaction (a legal entity being a vendee in a sale of land wherein the vendor reserves a mineral servitude), in order to determine with certainty if the legal entity had been “created for” any of the purposes enumerated in Louisiana Revised Statutes section 19:2.

As noted, Act No. 702 of 2012 expanded the “created for” standard of eligibility for the right to expropriate, to now include a legal entity that is “engaged in” the specified activities.[65]

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64 *Id*. at § 31:149A(2).

65 Although LA. REV. STAT. ANN. § 19:2(11) listed, as an entity having the right to expropriate, “any domestic or foreign limited liability company *engaged in* any of the activities otherwise provided for in this Section,” this Subsection, by its explicit terms, does not reach or apply to corporations or partnerships.

Thus, if a corporation was created "for any lawful activity,"[66] or if a limited liability company was organized "for any lawful purpose,[67] (and, hence, was not "created for" one of the enumerated purposes), but is in fact "engaged in" certain specified activities, a reservation of a mineral servitude in a sale to such entity might be imprescriptible.

Here is where it gets difficult. When, prior to the adoption of Act No. 702 of 2012, the standard was simply whether the entity was "created for" a stated purpose, a title examiner had the actual ability to scrutinize the organizational articles,[68] and make a determination as to whether the vendee was an "acquiring authority,"[69] and, hence, to determine if the vendor's mineral servitude was (or was not) subject to prescription.

Now that the touchstone for the power of condemnation has been expanded to include an entity that is "engaged in" those specified activities (even if the entity is not explicitly "created for" such purpose), this gives rise to a factual matter *not* reflected by the public records, and would seemingly require an inquiry as to the activities in which the entity is or has been "engaged."

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[66] As stated in LA. REV. STAT. ANN. § 12:1-301A, "[e]very corporation incorporated under this Chapter has the purpose of engaging in any lawful business or activity unless a more limited purpose is set forth in the articles of incorporation."

[67] "A limited liability company may be organized under this Chapter and may conduct business for any lawful purpose, unless a more limited purpose is stated in its articles of organization." *Id*. at § 12:1302A.

[68] The Model Business Corporation Act, effective January 1, 2015, has eliminated the requirement (under prior law) that the articles be filed in "the office of the recorder of mortgages of the parish in which the registered office of the corporation is located," (former) LA. REV. STAT. ANN. § 12:25D, now repealed. However, the articles would be available in the office of the Secretary of State, *id*. at § 12:1-123B.

[69] *See Calcasieu & S. Ry. Co. v. Bel*, 69 So. 2d 40, 41 (La. 1953) ("The plaintiff *by its charter* is an organization constituted under the laws of this state for the construction of a railroad, and is thus a corporation to which this article gives the right of expropriation."); *Central Louisiana Electric Co., Inc. v. Pugh*, 96 So. 2d 523, 525-26 (La. App. Ct. 2d 1957), and *Texas Eastern Transmission Corp. v. Terzia*, 138 So. 2d 874, 875-76 (La. App. Ct. 2d 1962) (court rejected an argument that the plaintiff-corporation failed to prove it had right of expropriation, calling such argument "so technical and unreasonable as to hardly be worthy of consideration.").

And worse, the acquisition in question might be for purposes unrelated to the statutory activity, but if that entity is "engaged in" a prescribed activity in another parish or state (unrelated to the transaction at hand), is that sufficient to bring that transaction within the ambit of article 149 so as to make the reserved servitude imprescriptible? Nothing in the new formulation requires that the land purchase (with attendant reservation of a mineral servitude) actually be effectuated in connection with a qualifying activity in which the vendee is then "engaged."[70]

In other words, a corporation or LLC "created for" the generic purpose of engaging in "any lawful" activity or purpose might actually be "engaged in" a qualifying activity in Bossier Parish, and thereby might enjoy the power of expropriation in Terrebonne Parish, even though its activities in that latter parish (some 300 miles away) are unrelated to the conduct of (or "engagement in") the specified activity.

So, if one is examining title to land in that southern parish, and finds that the vendee purchased property in a deed in which the vendor reserved minerals, is the mineral servitude prescriptible or not? What inquiry must the title examiner make in order to ascertain the status or character of the reserved mineral servitude?[71]

Admittedly, the concern expressed herein might be assuaged somewhat by the requirement that the "instrument or judgment shall reflect the intent to reserve or exclude the mineral rights from the acquisition *and their imprescriptibility as authorized under the provisions of this Section* and shall be recorded in the conveyance records of the parish in which the land is located."[72]

If there is no reference in the deed to the minerals' "imprescriptibility as authorized under the provisions of this Section," the inquiry should end there. This conclusion is reinforced by the codal requirement that the "provisions of this Chapter shall not apply to: * * * [a] transfer in which the acquiring authority neither expressly reserves or excludes nor

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70 Seemingly, a large, multi-national, publicly traded corporation might be "engaged in" the piping of natural gas in North Dakota (what about Indonesia?), but not in Louisiana, and thereby qualify as an "acquiring authority" for purposes of article 149.

71 There are 64 parishes in Louisiana.

72 LA. REV. STAT. ANN. § 31:149B(2). (Emphasis added.).

conveys to the transferor a mineral right otherwise subject to prescription."[73]

However, even with compliance with this requirement, it is still necessary to inquire into the underlying facts so as to determine that the vendee is in fact an "acquiring authority" by reason of the circumstance that the vendee (while not "created for" a certain purpose) has "engaged in" a prescribed activity.

Said differently, merely stating, in the deed or judgment, that the reserved minerals are "imprescriptib[le] as authorized under the provisions of" article 149, does not make it so, unless it is actually so as a factual matter, compliant with the strictures of the relevant article. "Bootstrapping" is not allowed here.

This legislation creates an unnecessary burden on a title examiner and, thus, results in significant and unnecessary potential uncertainty in the law.

Moral of the Story — Lessons to be Learned

While important, the issue is admittedly academic until 2022 which is ten years after the 2012 amendment, followed by the creation of a qualifying servitude.

So mark your calendar for then!! It will be here before you know it.

If the mineral servitude has been used, the issue will still remain academic, but if the servitude is not used within ten years of its post-amendment creation (in a sales transaction confected after August 1, 2012), it would be necessary to ascertain if the servitude is imprescriptible, by reason of having been created in a sale of land to an "acquiring authority" that has been "engaged in" a qualifying activity.

E. Right of Servitude Owner Under Non-compliant Reservation

Article 11 of the Mineral Code was amended in 2006 to add Section B, requiring that language be included in a sale of land in which minerals are reserved, to essentially alert the vendee (as the new landowner subject to the vendor's reserved mineral servitude) of the rights of

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[73] *Id*. at § 31:149G(2).

the servitude owner to utilize the surface of the land.[74] This requirement only applies to a mineral servitude created by reservation, but does not control if the servitude is created by grant.[75]

As noted, article 11B makes no mention whatsoever of the consequences of a failure to comply with the article's new requirement. Does non-compliance with the textual requirements of the article mean that the reserved mineral servitude is not valid? Or might it mean that, while valid, no operations may be conducted on the surface of the land?

If the vendor-servitude owner may not, for that reason, conduct operations on the surface of the burdened tract, may its lessee do so? Must the servitude owner or its lessee seek consent of the landowner to conduct operations? That this might be a concern to the lessee of such vendor is supported by the observation that one may not grant greater rights to another than it itself owns.[76]

Moral of the Story — Lessons to be Learned

Any requirement that the servitude owner (or its lessee) must seek the permission or consent of the landowner to operate on the servitude tract, is totally contrary to the essential nature of a mineral servitude, which is that the servitude owner may conduct operations on the burdened land, *without the need to secure the consent of the landowner*.[77] Indeed, the servitude itself constitutes the authority to enter the land and drill a well, as that is its inherent purpose.

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[74] Act No. 446, 2006 La. Acts 1828. Article 11B(1) of the Mineral Code now provides, as follows:

> A reservation of mineral rights in an instrument transferring ownership of land must include mention of surface rights in the exercise of the mineral rights reserved, if not otherwise expressly provided by the parties.

[75] "A landowner may convey, reserve, or lease his right to explore and develop his land for production of minerals and to reduce them to possession." LA. REV. STAT. ANN. § 31:15.

[76] *See* Ottinger, *Mineral Lease Treatise*, § 2-09, for authority supporting the proposition that a party cannot grant, lease or convey any greater rights than it holds or owns.

[77] *See*, *e.g.*, *Peabody v. Weeks*, 129 F. 3d 608 (5th Cir. 1997) ("[T]he [trial] court found that Weeks had impermissibly interfered with the mineral owners' reasonable use of the land to reach their minerals, and that their actions were 'plainly contrary to the fundamental tenets of the Louisiana Mineral Code.'").

The 2006 amendment to article 11 was nothing more than "feel good" legislation. This presenter's personal preference would be to repeal and remove that amendment (restoring article 11 to its original verbiage), but if not, one should be mindful of the need to comply with this requirement in the preparation of a sale deed in which minerals are reserved.[78]

III. Current Issues Involving Mineral Royalties

A. "Royalty Acres"

"A mineral royalty is the right to participate in production of minerals from land owned by another or land subject to a mineral servitude owned by another."[79] A recurring, but regrettable, occurrence in connection with the sale of a mineral royalty is the use of the term "royalty acres." This typically reads:

> Grantor is hereby conveying 22 royalty acres.

In the event of production, the interest in production to which a royalty owner is due is calculated by the operator, and is customarily expressed in decimals.[80] The accepted formula to calculate a royalty interest (in decimals), if one knows the number of royalty acres and the total number of acres in a tract of land, is to divide the royalty acres by the total acreage, and multiply by one-eighth (1/8). However, if the number of acres is shown to be inaccurate by a later survey, the royalty interest will necessarily change, thus arguably not effectuating the intention of the parties.

Courts have recognized that "the term [royalty or] mineral acres has usage in the oil industry but does not have a simple definite meaning which is easily understood by a person who has little or no experience in the field of minerals."[81]

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78 *See* Ottinger, *Mineral Lease Treatise*, § 11-03.

79 LA. REV. STAT. ANN. § 31:80. *See* PATRICK S. OTTINGER, *Mineral Royalties*, Louisiana Mineral Law Treatise, Chapter Five (Martin, ed., Claitor's Law Publishing, 2012).

80 *See* Ottinger, *Mineral Lease Treatise*, § 3-10(a)(6).

81 *Light v. Crowson Well Service, Inc.*, 313 So. 2d 803, 806 (La. 1975).

The uncertainty of the meaning of this term often leads to conflict, in the event of production, and certainly to the need to undertake curative efforts or the institution of a concursus proceeding.

Moral of the Story — Lessons to be Learned

The term "royalty acres" is often used as a "rule of thumb" basis to calculate the purchase price for the mineral royalty, such as "$200 per royalty acre."

Even if understood, if it is determined that the tract involved is of a different size than the parties anticipated or believed it to be, problems may occur. Certainly, the expectation of one party or the other will not be achieved.

The phrase "royalty acres," or (while we are at it) "mineral acres," should be avoided.

B. Recent Legislation — Unsolicited Offers to Purchase Mineral Royalties (or Servitudes)

In 2016, the Legislature enacted the Sale of Mineral Rights by Mail Solicitation Act.[82]

Brought about by abuses (perceived or actual) in the Haynesville Shale in Northwest Louisiana, this legislation creates a remedy to a landowner who sells a mineral royalty (or even a mineral servitude) to a purchaser who makes an unsolicited contact with the seller by mail.

Experience indicates that certain companies would send out mass mailings to the parties identified on an Interested Party list used in connection with compulsory unitization applications.[83] Anecdotally, unsophisticated parties would receive these "fancy-looking papers" in the mail, and sign and return them, thinking that they were necessary in order to place their interest in line for payment. When the sellers would later inquire of the operator as to when they would be paid, they were informed that, by signing those "fancy-looking papers," they had divested themselves of their royalty (or worse, mineral) interest.

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[82] Act No. 179, 2016 La. Acts, now codified as Louisiana Revised Statutes sections 9:2991.1, *et seq*.

[83] LA. ADMIN. CODE tit. 43, pt. XIX, § 3907B.1.

These unsolicited offers were typically accompanied by a draft, and a proposed deed with onerous terms, including the following, to-wit:

- The right of the transferee to amend the legal descriptions or other terms.
- Mandatory arbitration in Texas.
- Choice of law in a foreign state.
- Duty on transferor to indemnify the transferee in certain respects.
- Making the transferee a mandatary for certain purposes.

Provisions of this type are now invalidated as being against public policy.[84]

The Act gives a right of rescission to the mail-solicited transferor, the duration of which depends on whether or not a certain disclosure is made by the transferee in the deed.[85] If the instrument of transfer contains the disclosure prescribed by law,[86] the transferor has 60 days within which it might rescind the transaction.[87] Otherwise, the transaction may be rescinded "within a preemptive period of three years."[88]

Moral of the Story — Lessons to be Learned

The Act was the result of a study committee by the Louisiana State Law Institute at the behest of the Louisiana State Senate.[89]

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84 "Persons may not by their juridical acts derogate from laws enacted for the protection of the public interest. Any act in derogation of such laws is an absolute nullity." LA. CIV. CODE ANN. art. 7.

85 LA. REV. STAT. ANN. § 9:2991.6.

86 *Id*. at § 9:2991.5.

87 *Id*. at § 9:2991.6A.

88 *Id*. at § 9:2991.6B.

89 Your presenter served on this committee of the Louisiana State Law Institute.

The statute explicitly excludes mineral leases as being within the ambit or scope of its features and protections.[90] This is an important consideration of security of title to a lessee who otherwise would be at risk in spending significant amounts of money to drill a well on lands covered by a mineral lease granted by a lessor who had been contacted merely by mail.

The legislation recognizes the need to protect third parties under the "Public Records Doctrine."[91]

Upon receipt of a timely notice of rescission, the transferee must return to the transferor any royalties or other payments received by the transferee.[92] Significant remedies are available to the transferor if the transferee does not comply with the transferor's written notice of rescission.[93] Included within the range of remedies is the potential for an enhanced recovery of royalties received by the transferee prior to rescission, but not restored to the transferor after a timely rescission of the transaction.[94]

IV. Current Issues Involving Mineral Leases

A. Production in "Paying Quantities"

If a mineral lease is maintained in force and effect by production, that production must be in "paying quantities."[95] This is so even if the mineral lease is silent in this regard.[96]

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[90] "As used in this Part, the term 'mineral rights' does not include a mineral lease." *Id*. at § 9:2991.2.

[91] *See* Ottinger, *Mineral Lease Treatise*, § 1-14.

[92] LA. REV. STAT. ANN. § 9:2991.9.

[93] *Id*.

[94] *Id*. at § 9:2991.9C. However, *see* Part IV.H hereof as to the statutory formulation by which this remedy is provided.

[95] *Id*. at § 31:124.

[96] *See* Patrick S. Ottinger, *Production in "Paying Quantities" – A Fresh Look*, 51 ANN. INST. ON MIN. LAW 24 (2004). Also published at 65 LA. L. REV. 635 (2005). *See also* Ottinger, *Mineral Lease Treatise*, § 3-15.

Developed jurisprudentially as a matter of public policy,[97] the contours of the requirement are now codified in article 124 of the Mineral Code that provides, as follows:

> When a mineral lease is being maintained by production of oil or gas, the production must be in paying quantities. It is considered to be in paying quantities when production allocable to the total original right of the lessee to share in production under the lease is sufficient to induce a reasonably prudent operator to continue production in an effort to secure a return on his investment or to minimize any loss.[98]

A production in "paying quantities" inquiry involves a comparison of revenue to expenses, and is usually very expert-intensive. But what revenue, and what expenses? And for what period of time is the evaluation to be made? These significant issues are at the heart of the case.

It is appropriate to note the conflicting interests of the lessor and the lessee.[99]

On the one hand, the lessor will want to consider as many items of expense as possible, so as to require a greater amount of production to meet or exceed that amount.[100] The lessor will also want to focus on the period of time when expenses were greater in comparison to revenue.

On the other hand, the lessee will want to eliminate those items of expense that are not recurring in nature, so as to require a lesser amount of production to meet or exceed that amount.

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97 The comments to article 124 indicate that "[t]he manner in which the test for production in paying quantities is stated in Article 124 is articulated well in the decision of the Texas Supreme Court in *Clifton v. Koontz*, 25 S.W.2d 684, 691 (1959)." LA. REV. STAT. ANN. § 31:124, cmt.

98 LA. REV. STAT. ANN. § 31:124.

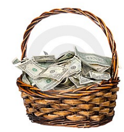
99 *See* Ottinger, *Mineral Lease Treatise*, § 3-15(c).

100 *See*, *e.g.*, *Lege v. Lea Exploration, Inc.*, 631 So. 2d 716 (La. App. Ct. 3d), *writ den'd* 635 So. 2d 1112 (La. 1994). In the interest of full disclosure, your presenter represented the defendant in this case.

The lessee will also want to make certain that the period of time that is studied by the court, will include periods of greater production relative to costs incurred.

The following diagram illustrates these features of the test for production in “paying quantities,” *viz.*:

A “PIPQ” Case Involves a Comparison of Two Baskets



A Basket of Bills ***versus*** **A Basket of Revenue**

The lessor will want this basket to be “full to the brim,” including every expense incurred.

This basket is always the revenue allocable to1.0 minus royalty under the mineral lease -- Article 124.

The lessee will want to limit this to “lifting expenses,” eliminating capital or extraordinary, non-recurring expenses.

Since this basket is a simple function of math, the battle in a “PIPQ” case essentially concerns the content of the other basket.

If the value of the basket of revenue exceeds the value of the basket of bills (even by a little), the lessee wins; the lease is producing in “paying quantities.”

A critical issue is the period of time during which the comparison is made; courts tend to view the matter in a longer time frame to avoid anomalies.

Moral of the Story — Lessons to be Learned

The “current issue” pertaining to the subject of production in “paying quantities,” is the impact of historically low commodity prices on this subject.

Courts continue to apply the traditional tenets of this subject, but remain mindful of the volatility of pricing for oil and gas as a relevant consideration.

One of the more recent cases in this regard is *Middleton v. EP Energy E&P Company, LP*,[101] where the court noted, as follows:

> In determining whether the Keatchie Well produced in paying quantities, the fact finder will need to consider all of the factors which would influence a reasonably prudent operator to continue production, *including the market price available*, the relative profitability of other nearby wells, the operating costs, the net income and the reasonableness of the expectation of profit.[102]

B. "Post-production Costs"

This is probably the hottest of "hot topics," due principally to the significant amounts of natural gas discovered and produced in the shale plays, particularly the Haynesville Shale in Northwest Louisiana.[103]

While the lessee is solely liable for all costs of exploration and production,[104] the issue presented is whether the lessor has any responsibility for "post-production costs."[105]

"Post-production costs" are those expenses incurred by the lessee-operator after the gas is brought to the surface of the earth, and "reduced to possession" (the wellhead being the point of production), and that are necessitated in order to render the product marketable.[106]

Relevant in this regard is article 7 of the Mineral Code that instructs that "[m]inerals are reduced to possession when they are under physical control that permits delivery to another."[107] This "reduction to possession" occurs at the wellhead.

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101 188 So. 3d 263 (La. App. Ct. 2d), *writ den'd* 192 So. 3d 774 (La. 2016). In the interest of full disclosure, your presenter represented a defendant in this suit.

102 *Id*. at 267. (Emphasis added.).

103 *See* Ottinger, *Mineral Lease Treatise*, § 4-25(d)(6).

104 *See id*., § 4-25(d)(6)(ii).

105 *See id*., § 4-25(d)(6)(iii).

106 *See id*., § 4-25(d)(6).

107 LA. REV. STAT. ANN. § 31:7.

The wellhead is a device that controls the pressure of the well, and allows the operator to control the flow of the oil and gas.

As to oil, it might be immediately directed to a tank battery.

With respect to gas, it will be channeled to a pipeline.

Regardless of the product, the wellhead is where the oil or gas is "reduced to possession."

Four things occur at the wellhead.[108]

First, the produced oil and gas ceases to be governed by the law of immovable property, and gains its status of mobility, becoming subject to the law of movable property.[109]

Secondly, under an "at the well" lease,[110] the royalty interest of the lessor attaches, and is fixed to the oil or gas, as produced.

Thirdly, the responsibility for severance taxes attaches at "severance," which occurs at the wellhead when the production is "reduced to possession."[111]

Finally, the royalty being fixed at that point, the "market value" "at the well" is applied or, if there is no value "at the well," is determined through a "net back," or "reconstruction," method of valuation, so as to "reverse determine" the "market value at the well."[112]

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108 *See* Ottinger, *Mineral Lease Treatise*, § 4-25(d)(6)(v).

109 *Southport Petroleum Co. of Delaware v. Fithian*, 13 So. 2d 382, 383 (La. 1943) ("It is well settled in this State that there is no title to oil so long as it remains in the earth; consequently, no lien could attach to it as the property of anyone until it is brought to the surface, and when brought to the earth, it is clearly no part of the well.").

110 "The reason why the division and delivery is made *at the well*, in cases where there is to be a division in kind, is that, there is where the parties come into ownership of the commodity, there is where title vests. The lessor and lessee are vested with title to the gas *at the well* or in the field in the same proportion as the oil is owned." *Wall v. United Gas Public Service Co.*, 152 So. 561, 563 (La. 1934) (Emphasis added.).

111 LA. REV. STAT. ANN. § 47:631.

112 *See* Ottinger, *Mineral Lease Treatise*, § 4-25(d)(6)(ix).

Moral of the Story — Lessons to be Learned

Legions could be written on this topic.

The default rule in Louisiana is that the lessor's royalty bears proportionately its share of "post-production costs," unless the parties have agreed otherwise.[113]

The lessor's responsibility for "post-production costs" is *in rem* only, never "out of pocket."[114]

In the exercise of "freedom of contract,"[115] parties might elect to include in their mineral lease a "No Deductions Clause," but provisions of this type have been the subject of significant litigation to interpret them.[116]

It is the experience of your presenter that many operators based in Texas, but operating in Louisiana, are surprised that the "default" rule of *Heritage Resources, Inc. v. NationsBank* does not prevail in Louisiana.[117]

C. Transfers — Assignment or Sublease?

When a mineral lease is transferred, the transfer document is either an assignment or a sublease.[118]

The name affixed to the instrument is immaterial; rather, its true character is discerned from document itself.[119]

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113 *Merritt v. Southwestern Electric Power Co.*, 499 So. 2d 210 (La. App. Ct. 2d 1986).

114 *See* Ottinger, *Mineral Lease Treatise*, § 4-25(d)(6)(vii).

115 *See* Ottinger, *Mineral Lease Treatise*, Chapter Two.

116 *See id*., § 5-14.

117 939 S.W. 2d 118 (Tex. 1996). *See also Chesapeake Exploration, L.L.C. v. Hyder*, 483 S.W. 3d 870 (Tex. 2016).

118 *See* Patrick S. Ottinger, *What's in a Name? Assignments and Subleases of Mineral Leases Under Louisiana Law*, 58 ANN. INST. ON MIN. LAW 283 (2011). *See also* Ottinger, *Mineral Lease Treatise*, § 10-07.

119 *See id*., § 10-06.

If the lessee conveys all of its interest in the lease, without a reservation of overriding royalty interest, or a consequential provision benefitting the transferor in terms of the future administration of the mineral lease, it is an assignment.[120]

If, however, the lessee reserves an economic interest—most usually an ORRI—or if the lessee imposes on the transferee a consequential duty, it is a sublease.[121]

"Every sublease is, in a sense, an assignment, but every assignment of a lease is not a sublease."[122]

In contrast to other oil and gas producing states, there are an array of significant consequences arising from the distinction between an assignment and a sublease.[123] These include (but are not limited to) the following, to-wit:

- Warranty of grantor.
- Authority of succession representative to grant.
- Ability to grant a complete release to a landowner.
- Remedy to the grantor if purchase price not paid.
- Duties owed by the grantee to the grantor.
- Prescriptive period applicable to claim for unpaid revenue due to the grantor.
- Divisibility of the mineral lease.

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120 *See id*., § 10-07(d).

121 *See id*.

122 *Smith v. Sun Oil Co., Inc.*, 116 So. 379, 380 (La. 1928).

123 *See* Ottinger, *Mineral Lease Treatise*, § 10-15.

Moral of the Story — Lessons to be Learned

Parties preparing instruments by which a mineral lease is to be transferred should be cognizant of the consequences that might arise if the transfer is structured as an assignment or a sublease. The next section discusses one particular consequence arising out of the distinction.

D. Division of Mineral Leases

One of the more significant "sleeper" issues arising out of the distinction between an assignment and a sublease is the potential that a mineral lease might be "divided" by a partial assignment (but not by a sublease),[124] if the mineral lease contains a "Division of Rental Clause."[125]

To "divide" a mineral lease is to turn one mineral lease into two (or more) leases, each standing alone and having separate lease maintenance obligations.[126]

A "Division of Rental Clause" provides, in essence, that, "[i]n the event of an assignment of the lease as to a segregated portion of the land, delay rentals shall be apportioned among the several leasehold owners according to the surface area of each, and default in payment by one shall not affect the rights of others."

Particularly in connection with the purchase and sale of producing mineral leases, the purchaser, in conducting its due diligence, should be mindful of this possibility, and investigate the leasehold history of the leases in order to discern if any prior partial assignment in the chain of title has resulted in lease division.[127]

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124 *See id.*, § 4-28(d)(3). This clause is also called an "Apportionment of Rental Clause."

125 *See id.*, § 4-28.

126 "The unarticulated premise of these cases is that in the absence of such provisions the lease would be indivisible in the sense that a partial assignment would not have the effect of creating two leases where but one existed before." LA. REV. STAT. ANN. § 31:130, cmt.

127 *See* Patrick S. Ottinger, *Closing the Deal in the Bayou State: The Purchase and Sale of Producing Oil and Gas Properties*, 76 LA. L. REV. 691, 738 (2016).

In the seminal case on this subject,[128] the court relied upon the "Division of Rental Clause" as giving rise to a division of the lease in case of a partial assignment.

This presenter questions the court's reliance on this provision to find a division, since the principal purpose of this clause is of a different focus, *viz.*, the apportionment of delay rentals among two or more assignees of a segregated portion of the leased premises, and the consequences of default in payment by one such assignee.

The Second Circuit, Court of Appeal, in *Hoover Tree Farm, L.L.C. v. Goodrich Petroleum Co., L.L.C.*,[129] seems to have embraced this observation when it noted, as follows:

> While the contractual provision itself [*i.e.*, the "Division of Rental Clause"] contemplated only a type of limited lease division upon the non-payment of a portion of the lease rentals during the primary term, both Sun Oil and Roberson without explanation interpreted the clause broadly and by implication ruled that a lease containing such provision would be divided for all purposes into two leases upon the transfer of the entirety of the leasehold rights to a specific geographical portion. Such broad interpretation therefore moved the clause beyond merely the subject of rental payment default to effect a stringent modification of the typical habendum clause principle for maintenance of the entire lease beyond the primary term by the operations and production of one well.[130]

In *Roberson v. Pioneer Gas Co.*,[131] the court again considered the issue of whether a certain transfer was an assignment or a sublease. It articulated the following distinction between the two types of transfer, to-wit:

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[128] *Swope v. Holmes*, 124 So. 131 (La. 1929).

[129] 63 So. 3d 159 (La. App. Ct. 2d), *writ den'd* 69 So. 3d 1161-62 (La. 2011).

[130] *Id*. at 174.

[131] 137 So. 46 (La. 1931).

> The distinction between an *assignment of a lease* and a *sublease* is that, in an assignment, the assignor transfers his entire interest in the lease in so far as it affects the property on which the lease is assigned; whereas, in a sub-lease, the original lessee, or sublessor, retains an interest in the lease in so far as it affects the property subleased -- by imposing some obligation upon the sublessee in favor of the sub-lessor, such as an obligation to pay additional rent to the sublessor.[132]

The mineral lease covered 125 acres, and the lessee assigned the lease as to 25 acres, with no reservation sufficient to render the transaction a "sublease."

The mineral lease contained a "Division of Rental Clause." The court noted that such a clause "made the lease a divisible one," citing *Swope v. Holmes*.[133] Thus, the partial assignment divided the lease, and the drilling of a well on one portion of the lease did not have any effect as to the other portion of the lease.

In *Noel Estate, Inc. v. Murray*,[134] the plaintiff-lessor sought cancellation of mineral lease on the whole of 60 acres. The lessee had obtained production on 10 acres, and then later assigned the lease on the other 50 acres. No production was secured on the 50-acre tract. The court canceled the lease as to the 50-acre tract, but not as to the 10-acre tract on which a well was located. Both parties appealed.

The mineral lease contained a clause that "recited that the rights of either party thereunder could be assigned in whole or in part."[135]

By assigning the lease on the 50-acre tract, the court held that the lessee "divided a divisible lease, creating in favor of Smith an in-

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[132] *Id*. at 48. (Emphasis supplied by court.).

[133] *Supra* note 128.

[134] 65 So. 2d 886 (La. 1953).

[135] *Id*. at 887. The clause in the instant mineral lease differs from the clause in *Swope v. Holmes*, *supra* note 128.

dependent lease on the north 10 acres."[136] Production never having been obtained on 50 acres, the lease as to that tract was properly canceled.

Moral of the Story — Lessons to be Learned

One should be aware of the potential of lease division, and of the consequences on lease maintenance. While article 130 of the Louisiana Mineral Code provides that a "partial assignment or partial sublease does not divide a mineral lease,"[137] that is not a statement of public policy that cannot be modified in the exercise of "freedom of contract."

This is particularly so in the Haynesville Shale in Northwest Louisiana, in which many old leases are HBP from shallow production, and have been subject to numerous instruments of transfer at various subsurface depths over many years. The potential that the rule would be held applicable to a horizontal transfer could lead to significant consequences, in that shallow production might not hold deeper rights, or *vice versa*.[138]

E. Rights Under the Well Cost Reporting Statute

Louisiana law is well established that an unleased mineral owner (a "UMO") is not entitled to share in production from a compulsory unit until the operator has been reimbursed the costs of drilling, testing, completing, equipping, and operating the unit well, out of production.[139] This point of time is called "payout."

The dilemma of the UMO is that—lacking both the staff and sophistication of an E&P company--it has no way of ascertaining when "payout" occurs for this purpose. It is often at the mercy of the operator in this regard.

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[136] *Id*. at 888.

[137] LA. REV. STAT. ANN. § 31:130.

[138] *See*, *e.g.*, *Guy v. Empress, L.L.C.*, 193 So. 3d 177 (La. App. Ct. 2d 2016), in which a horizontal division of a mineral lease was sought, but denied by the court.

[139] *See* Patrick S. Ottinger, *After the Lessee Walks Away – The Rights and Obligations of the Unleased Mineral Owner in a Producing Unit*, 55 ANN. INST. ON MIN. LAW 59 (2008).

The Well Cost Reporting Statute, Louisiana Revised Statutes sections 30:103.1, *et seq.*, affords the UMO the opportunity to call upon the operator to certify as to the amount of costs being recouped, and to thereby permit it to track the status of "payout."

Should the operator fail to properly and timely report to the UMO, it would incur the penalty prescribed by Louisiana Revised Statutes section 30:103.2, reading, as follows:

> Whenever the operator or producer permits ninety calendar days to elapse from completion of the well and thirty additional calendar days to elapse from date of receipt of written notice by certified mail from *the owner or owners of* ***unleased*** *oil and gas interests* calling attention to failure to comply with the provisions of R.S. 30:103.1, such operator or producer shall forfeit his right to demand contribution from *the owner or owners of the* ***unleased*** *oil and gas interests* for the costs of the drilling operations of the well.[140]

What is meant by "the owner or owners of *unleased* oil and gas interests"? Recent litigation addresses the issue of whether the Well Cost Reporting Statute may be availed only by a UMO (one who is truly unleased to any party), or also by a mineral lessee of an interest not under lease to the operator. Recent decisions have considered this issue.

In *TDX Energy, LLC v. Chesapeake Operating, Inc.,*[141] the plaintiff sued the operator, saying that it had forfeited its rights to recover well costs by failing to provide well-cost information under the Well Cost Reporting Statute.

TDX was a mineral lessee, not "the owner . . . of unleased oil and gas interests." It was not a UMO, certainly not in the industry understanding of the term.

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140 LA. REV. STAT. ANN. § 30:103.2. (Emphasis added.).

141 2016 WL 1179206, Civil Action No. 13-1242, W.D. La. In the interest of full disclosure, your presenter represented the defendant-operator in this suit.

The court granted Chesapeake's motion for summary judgment, holding that the Well Cost Reporting Statute only inures to the owner of a truly unleased mineral interest, and may not be availed by a lessee under a mineral lease in which the operator owns no interest.

The Fifth Circuit, United States Court of Appeal, reversed,[142] adopting the view of a Louisiana appellate court in another case.[143]

In that state case, the court also held that a lessee under a mineral lease, who had no contractual relationship with the operator, and who did not agree to share in the cost, risk and expense of drilling the unit well, comes within the ambit of the phrase "the owner . . . of unleased oil and gas interests."

Additionally, the court held that the penalty to which the non-compliant operator was subject was not limited to "the costs of the drilling operations of the well," but also forfeited the right to recover (out of production) "the costs of 'drilling, completing, and equipping the unit well.'"[144]

Moral of the Story — Lessons to be Learned

It has been held that that the Well Cost Reporting Statute, being penal in nature, "should be construed strictly against the party seeking to impose the penalty."[145] This means, at a minimum, that, if two interpretations of the statute are available, the court should choose the narrow one, not an expansive interpretation. Yet the Fifth Circuit, United States Court of Appeal, in *TDX* elected to follow the *XXI* decision, which (as the court stated) "followed the latter, more expansive view."[146] This is clearly contrary to the rule of strict construction of a penal statute.

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142 857 F. 3d 253 (5th Cir. 2017).

143 *XXI Oil & Gas, LLC v. Hilcorp Energy Co.,* 124 So. 3d 530 (La. App. Ct. 3d 2016); 206 So.3d 885, *writ den'd* 216 So. 3d 814 (La. 2017). In the interest of full disclosure, your presenter represented the defendant-operator in this case to prepare and prosecute a writ application to the Louisiana Supreme Court, but did not represent the defendant at the trial or appellate level.

144 *Id*. at *6.

145 *Scurlock Oil Co. v. Getty Oil Co.*, 324 So. 2d 870, 877 (La. App. Ct. 3d 1975).

146 857 F. 3d at 259.

Until clarification by the Louisiana Supreme Court, if your operator-client receives a proper demand for well-cost information from a lessee, one needs to evaluate the risk of non-compliance.

F. Payment of Royalties Under Louisiana Risk Fee Act

The Louisiana Risk Fee Act, codified at Louisiana Revised Statutes section 30:10A(2)(a), permits a party intending to drill a unit well to call upon other lessees in the unit to make an election to participate, or not, in the cost, risk and expense of the well.[147]

If a party does not affirmatively elect to participate, its interest would be subject to the operator's right of recoupment of allocated expenses, *plus* a risk charge of 200% of certain costs (with exceptions).

Prior to 2012, while the operator was recouping its cost *plus* the risk charge, the non-participating lessee remained solely responsible for paying its royalties "out of pocket."[148]

This changed in 2012 when significant amendments were made to the Risk Fee Act.[149]

The most significant—and controversial—amendment is to now impose on the operator the duty to pay royalties to the lessor(s) of the non-participating party.

This radical amendment upset a century's worth of jurisprudence, and results in the diminution of the revenue stream to which the operator has historically been entitled. Worse than that, it represents a public policy that encourages, rather than discourages, a "free ride."

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[147] *See* Patrick S. Ottinger, *It's a Risky Business, but There's an Act for That: The Louisiana Risk Fee Act*, delivered to the 63rd Institute on Mineral Law, Paul M. Hebert Law Center, Louisiana State University, Baton Rouge, Louisiana, on March 31, 2016.

[148] *See*, *e.g.*, *Gulf Explorer, LLC v. Clayton Williams Energy, Inc.*, 964 So. 2d 1042, 1045 (La. App. Ct. 1st 2007) ("Clayton Williams has no contractual relationship with Gulf's lessors; under the facts presented herein, Clayton Williams has no obligation to pay Gulf's royalty and overriding royalty owners before it legally recoups its expenses from production pursuant to LSA-R.S. 30:10A(2)(b)(i).").

[149] Act No. 743, 2012 La. Acts 3030.

In 2016, a Senate Resolution was adopted that calls upon the Louisiana State Law Institute to study the 2012 amendments, and to make recommendations for possible repeal, amendment or clarification.[150]

Moral of the Story — Lessons to be Learned

Stay tuned to future amendments or clarifications of the Risk Fee Act, particularly the 2012 amendments that were so controversial.

If, in the meantime, your client is complying with its terms by paying the royalties for the benefit of the non-participating owner, one might evaluate the possibility of enforcing reimbursement from that lessee after payout is achieved. Although neither recognized nor disallowed by the amendments to the Risk Fee Act, theories of recoupment do exist, but have yet to be tested.

G. Does the Lessee Owe a Duty of Disclosure to its Lessor?

A recent case took up the issue of whether the lessee owed to its lessor a duty to disclose potential transactions with respect to the sale of its working interest.

In *McCarthy v. Evolution Petroleum Corp.*,[151] the lessee purchased its lessors' royalty interest for $42 thousand.

After it was publicly announced that the lessee then sold its working interest to Denbury for $50 million, the lessors sued to rescind the royalty sale based upon error or fraud.

The trial court sustained the defendants' peremptory exception raising the objection of no cause of action, but the Second Circuit, Court of Appeal, reversed.[152]

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[150] SR No. 31 of 2016 Second Extraordinary Session. Your presenter is serving as the Reporter for the Risk Fee Act Committee of the Louisiana State Law Institute, tasked with evaluating the legislation (particularly the 2012 amendments), and making legislative recommendations in connection therewith.

[151] 180 So. 3d 252 (La. 2015). In the interest of full disclosure, your presenter represented certain *amicus curiae* in support of the defendant's writ application in this suit.

[152] 111 So. 3d 446 (La. App. Ct. 2d 2013).

After the lessor amended its petition, in response to the appellate decision, the trial court again dismissed it, granting a second objection of no cause of action.

The Second Circuit, Court of Appeal, again reversed, expressing the view that the plaintiffs could allege facts supporting a "novel and untested cause of action by a mineral lessor that has never been specifically addressed and decided in our law."[153]

The Supreme Court granted the defendants' writ application (that was supported by numerous *amici* briefs), reversed the appellate court, and reinstated the trial court's dismissal of the (twice) amended petition. The court stated:

> Although . . . "[f]raud may . . . result from silence or inaction," in order "[t]o find fraud from silence or suppression of the truth, there must exist a duty to speak or to disclose information."[154]

Further, the court observed that a mineral lessee's duty ". . . to develop and operate as a reasonably prudent operator has no component of disclosing the information about which the plaintiffs complain . . .. Certainly, the information of the lessee gained through geological data and technical developments involving the lease premises remains proprietary information."[155]

Although *dicta*, the Supreme Court stated that a cause of action based on fraud by silence in a purchase of royalty rights by a lessee from its lessor might be sustainable if the mineral lease at issue required disclosure of pertinent information that was withheld.

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[153] 151 So. 3d 148, 160 (La. App. Ct. 2d 2014), *prior to reversal at* 180 So. 3d 252.

[154] 180 So. 3d at 258. As authority for this proposition, the Supreme Court cited to its earlier decision in *Greene v. Gulf Coast Bank*, 593 So. 2d 630 (La. 1992).

[155] 180 So. 3d at 259.

The last sentence of article 122 allows the parties to stipulate what shall constitute reasonably prudent conduct on the part of the lessee.[156] The Supreme Court noted that the lessor could expand on the lessee's duties so as to include a duty to disclose information, but it did not do so in this case.

Moral of the Story — Lessons to be Learned

It is often stated that "bad facts make bad law." The facts of this case come very close to embracing that tenet. Purchasing its lessor's royalty position is rarely a good idea on the part of the lessee.

Certainly, under all circumstances, the lessee must be truthful and candid with its lessor so as to avoid misunderstandings such as led to this litigation.

H. Authorized Damages for Unpaid Royalties.[157]

Several articles of the Louisiana Mineral Code provide authority for the award, in a suit for nonpayment of royalties, of "damages double the amount of royalties due . . .." In article 138.1, the award of "double damages" is mandatory ("the court shall award"), while, in all other articles, it is permissive ("the court may award").[158]

With respect to those articles stating that the court "may award" damages, the courts have recognized that the award of damages is discretionary, and not mandatory.[159]

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[156] "Parties may stipulate what shall constitute reasonably prudent conduct on the part of the lessee." LA. REV. STAT. ANN. § 31:122.

[157] The following is an adaptation of Ottinger, *Mineral Lease Treatise*, § 13-30(c).

[158] "The word 'shall' is mandatory and the word 'may' is permissive." LA. REV. STAT. ANN. § 1:3.

[159] *See*, *e.g.*, *Wegman v. Central Transmission, Inc.*, 499 So. 2d 436, 451 (La. App. Ct. 2d 1986), *writ den'd* 503 So. 2d 478 (La. 1987) ("Under R.S. 31:140 if the lessee fails to pay royalties due or fails to inform the lessor of a reasonable cause for failure to pay in response to the required notice, the court *may* award as damages double the amount of royalty due. Hence the award is discretionary."), and *Matthews v. Sun Exploration & Production Co.*, 521 So. 2d 1192, 1196 (La. App. Ct. 2d 1988) ("LSA-R.S. 31:140 provides the trial court with great discretion in awarding damages. It does not mandate that any award be given in excess of the royalties due.").

One court has stated that, "generally, such a maximum penalty should be reserved for the most blameworthy conduct."[160]

Where the award of double damages addresses itself to the discretion on the part of the court (as set forth in articles 139, 140 and 212.23 of the Mineral Code, each providing that the "court may award as damages double the amount of royalties due"), the court's discretion pertains to whether damages will be awarded at all, as well as to the amount of the award, which should be capped at double the amount due.

Unsettled is the issue of whether the Mineral Code envisions a maximum award of "double," or actually "treble," the amount of unpaid royalties as damages.

One school of thought is that the lessor is always entitled to its unpaid royalties, and the award of "double the amount of royalties due" is in addition to the royalties which are due, such that, in essence, the lessor might recover three times the royalties due.

While many courts have interpreted the codal provisions as authorizing, in essence, "treble" damages, Justice Knoll, in a dissenting opinion, expressed a contrary view.

Thus, in *Cimarex Energy Co. v. Mauboules*,[161] Justice Knoll offered the following view on this issue, to-wit:

> The trial court awarded Orange River unpaid royalties of approximately $3.2 million dollars, plus statutory damages of approximately $6.4 million dollars. The court held Mineral Code art. 212.23(B), which allows an award of "damages double the amount due," permits a court to award both the unpaid royalties and penalty damages in the amount of double the unpaid royalties, thereby effectively trebling the damages award. I would reverse the damages award as excessive.

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160 *Samson Contour Energy E & P, L.L.C. v. Smith,* 175 So. 3d 967, 981 (La. App. Ct. 2d 2015) (on rehearing).

161 40 So. 3d 931 (La. 2010).

> The far more natural reading of article 212.23(B) is to permit the plaintiff a total award of double the amount of unpaid royalties. As a simplified example, if the unpaid royalties total $100, the court has discretion to "double" the award by adding an additional $100 in statutory damages, for a total of $200.
>
> If the Legislature had intended article 212.23(B) to permit a treble damages award, it would have said so. Several Louisiana statutes unambiguously permit an award of treble damages. This is not one of them. Moreover, as Mineral Code article 212.23(B) is in the nature of a penal statute, it must be strictly construed in favor of the defendant. . . . I would remand for a recalculation of damages consistent with the statute.[162]

Justice Knoll gave numerous examples of "[s]everal Louisiana statutes [which] unambiguously permit an award of treble damages,"[163] to indicate that the Legislature is fully aware as to how to provide for such recovery, if that were its intention in adopting these provisions of the Louisiana Mineral Code.[164]

These comments, albeit assigned in dissent, make a compelling case for the proposition that the codal references to "damages double the amount of royalties due" should not be construed as authorizing the award of what is essentially "treble" damages.

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162 *Id*. at 952.

163 *Id*.

164 "La. Rev.Stat. § 3:4278.1 (Unlawful cutting of timber leads to damages "for three times the fair market value of the trees cut"); La. Rev.Stat. § 22:1023(F) (permitting "treble damages" for unlawful disclosure of private genetic information); La. Rev.Stat. § 30:2027 (Employee may recover "triple damages" for retaliatory termination for environmental whistleblowing); La. Rev.Stat. § 39:2163 (Employee may recover "treble damages" for retaliatory termination for uncovering employers' fraud in claiming hurricane relief monies); La. Rev.Stat. § 51:444 (Sales representative may recover "treble damages" for nonpayment of commissions). La. Rev.Stat. § 51:1409 (Permitting recovery of "three times the actual damages sustained" in unfair trade practice claim.)". 40 So. 3d at 952, n. 9.

The issue of the permissible amount of damages to be awarded under the regime of these articles was taken up by an appellate court, but admittedly in a unique procedural posture that does not provide clarity on this issue. In *Wegman v. Central Transmission, Inc.*,[165] the jury awarded double the amount of royalties due, rather than (in essence) triple such amount. The judge corrected this jury finding, and the defendant, on appeal, challenged the propriety of the judge making such correction when the plaintiff did not file a motion for JNOV. The situation was explained, as follows:

> Defendant contends that the trial judge erred in doubling the amount of the award (line 5) and then adding that figure to the actual damages (line 4) thereby giving plaintiff three times the amount of actual damages (line 6 vs. line 4). As previously noted, the jury awarded double the amount of damages instead of doubling the damages and adding that sum to the amount of royalties due. Defendant asserts that the different method of calculation used by the trial judge is not allowed because of the rules governing a motion for judgment notwithstanding the verdict and because the awarding of damages under LSA-R.S. 31:140 is discretionary. CTI does not claim that the award is more than authorized by statute.[166]

The appellate court upheld the actions of the trial court in constructing the judgment, explaining, as follows:

> We do not agree with defendant's characterization of this amendment to the jury award by the trial judge as a substantive change based on a fictional motion JNOV. The only reasonable inference possible is that the jury intended to award double damages but did not completely understand the proper method of calculation, especially in light of the specific jury finding that the remedy of damages was inadequate to

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165 *Supra* note 159.

166 499 So. 2d at 451.

> do justice and that the leases should be cancelled.[167]
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> *   *   *
>
> However, under the facts of this case, it is clear that the trial judge's calculation of plaintiff's award as royalties due, plus twice the amount of royalties due, as opposed to the jury's award of twice the amount of royalties due, was not a substantive change, but was done to correct an error in calculation under Art. 1951. The principal amount due the plaintiffs was not changed by this recalculation. Thus, the verdict was not reformed. Although the jury *may* award as damages any amount up to double the amount of royalties due, we do not believe that the jury would have failed to award the maximum amount of monetary damages when it also found that monetary damages were inadequate to provide a complete remedy. Furthermore, it is easily understood how the jury may have been confused about how to calculate damages as double the amount due.[168]

Clearly, because the issue of double versus treble damages was presented in the context of the procedure to modify a jury finding, the case is not compelling authority for the proposition. If the plaintiff had filed a motion for judgment notwithstanding the verdict, the examination of that issue by the court might have provided greater precedential guidance. Because the conduct of the lessee was found to be so egregious, the court had no sympathy for an argument--procedural or not--which sought to reduce the judgment cast against the defendant.

In Part III.B of this presentation, your presenter set forth a discussion of the recently-enacted Sale of Mineral Rights by Mail Solicitation Act. One of the remedies now provided to a transferor who avails itself of the right of rescission of a "sale of mineral rights by mail solicitation," is the recovery of royalties or other payments received by the transferee prior to the latter's receipt of a written notice of rescission. The

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167 *Id*. at 451-52.

168 *Id*. at 452.

formulation by which this special remedy is described is set forth in Louisiana Revised Statutes section 9:2991.9C, as follows:

> When an instrument evidencing a sale of mineral rights by mail solicitation does not contain the disclosure required by this Part, a transferee against whom the right to rescind is exercised shall be liable for attorney fees and court costs. In such a case, *in addition to restoring any royalties or other payments due to the transferor*, a court may further award as damages an amount up to twice the sum of royalties and other payments received by the transferee.[169]

One readily sees that this statutory formulation, in referring to the possible recovery of "twice the sum of royalties and other payments received by the transferee," as being "*in addition to* restoring any royalties or other payments due to the transferor," supports the proposition that, under the relevant articles of the Mineral Code, the lessor might only recover double, not treble, royalties. Concordant with the observation of Justice Knoll in the *Cimarex* case,[170] this new legislation demonstrates that the Legislature knows how to provide for a recovery of three times the royalties when it wishes to do so.

Moral of the Story — Lessons to be Learned

In a case involving a suit by a lessor against its lessee for damages for non-payment of royalty, one should be cognizant of the issue of whether the statutory scheme set forth in the Mineral Code contemplates a potential recovery of twice, or three times, the amount of royalties due. One should note the rationale advanced by Justice Knoll, quoted above, and also the arguments that might be based upon the recently-enacted remedy under the Sale of Mineral Rights by Mail Solicitation Act. The award of damages in this connection is discretionary in the first place,[171] but arguments exist to limit the upper or maximum limits of a recovery, if one is to be granted by the court.

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169 LA. REV. STAT. ANN. § 9:2991.9C. (Emphasis added.).

170 *Supra* note 161.

171 *See* cases, *supra* note 159.

I. Liability of Mortgagee-Bank for Faults of its Mortgagor-Borrower

The next "current" case is not, in the opinion of this presenter, merely a "Hot Topic." It is actually nuclear in that it is insupportable in law and has significant potential problems in the lending industry.

In *Gloria's Ranch v. Tauren Exploration, Inc.*,[172] the Second Circuit, Court of Appeal, affirmed a trial court's decision holding a mortgagee liable, on a solidary basis, with its lessee who had been cast for $23 million in damages, and "close to $1,000,000 in attorney fees."[173] The mineral lessee, Cubic Energy, Inc., was held liable for damages because it failed to timely release a mineral lease that the court held to have expired for failure to produce "in paying quantities."

Under article 207 of the Louisiana Mineral Code, if the "former owner of the . . . expired mineral [lease] fails to furnish the required act [evidencing the termination of the mineral lease] within thirty days of receipt of the demand . . ., he is liable to the person in whose favor the . . . lease has been . . . expired for *all damages resulting therefrom* and for a reasonable attorney's fee incurred in bringing suit."[174]

In this case, the mineral lease having been determined to have lapsed, the damages were based upon $18,000 per acre—the "going rate" in the Haynesville Shale in Northwest Louisiana at the time of lease termination—for "lost leasing opportunities."[175]

Whatever can be said about the propriety of the court's determination as to lease termination and the basis of damages "resulting from" the failure to release the lease, the most radical aspect of the decision is that the mortgagee-lender of the lessee was held liable along with the defaulting lessee.

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172 2017 WL 2391927 (La. App. Ct. 2d 2017).

173 *Id*. at *1.

174 LA. REV. STAT. ANN. § 31:207.

175 *See* Ottinger, *Mineral Lease Treatise*, § 1-25(e), for a discussion of volatility in bonus prices in the Haynesville Shale in Northwest Louisiana in the year 2008, documenting per acre bonus payments ranging from $150 (February 2008) to $25,000 (July and August 2008).

The trial court based its decision principally on the fact that the mortgagee, under its mortgage, had been "assigned" the mineral lease, seemingly making the mortgagee a working interest owner for purposes of having a duty to release an expired mineral lease that constituted its collateral.[176] The mortgage clause on which the trial court relied was an assignment *of proceeds*, commonly found in mortgages encumbering the working interest in the leases.[177]

The good news is that the appellate court reversed that particular finding as a basis of liability. The bad news is that the appellate court found that the various covenants in the recorded mortgage and unrecorded credit agreement—typical in "reserve based lending" transactions of this type—evidenced elements of "control" sufficient to impose liability on the mortgagee.

Most important to the court seemed to be a mortgage provision that required the bank's consent to the release by the lessee of an item of collateral, in this case, a mineral lease. As to this common clause, the court noted, as follows:

> Wells Fargo exercised control over Cubic's oil and gas operations on the lease, and controlled Cubic's ability to release the lease for failure to produce in paying quantities. As such, Wells Fargo shared coextensive liability with Cubic to provide a recordable act evidencing the release of its interest in the lease, and

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[176] The absurdity of this finding would be that the mortgage would have been extinguished by "confusion" (Louisiana's version of the doctrine of "merger").

[177] This typical mortgage provision read, thusly:

2.03 Assignment. To further secure the full and punctual payment and performance of all present and future Indebtedness, up to the maximum amount outstanding at any time. . . . Mortgagor does hereby absolutely, irrevocably and unconditionally pledge, pawn, assign, transfer and assign to Mortgagee all monies which accrue after 7:00 a.m. Central Time . . . to Mortgagor's interest in the Mineral Properties and all present and future rents therefrom . . . and all proceeds of the Hydrocarbons . . . and of the products obtained, produced or processed from or attributable to the Mineral Properties now or hereafter (which monies, rents and proceeds are referred herein as the "Proceeds of Runs"). Mortgagor hereby authorizes and directs all obligors of any Proceeds of Runs to pay and deliver to Mortgagee, upon request therefor by Mortgagee, all of the Proceeds of Runs . . . accruing to Mortgagor's interest[.]

> we discern no manifest error in the trial court finding Wells Fargo solidarily liable with the remaining defendants.[178]

The case is not final, and bears watching as it proceeds. Wells Fargo filed an application for rehearing which was denied on August 7, 2017, with two blistering dissents.

Moral of the Story — Lessons to be Learned

The court's analysis, if it can be said to exist at all, is thin, to say the very least. The decision does not articulate a rational basis on which the bank's liability was imposed. No prior case has turned a lending party into essentially a surety of its borrower. The various covenants on which the court relied to find the elements of "control" are typical in virtually every credit facility in the E&P lending space.

If this radical decision is correct (and your presenter does not believe it to be), banks should be concerned that the same result might attach if the borrower-mineral lessee is found liable for a "legacy lawsuit," damages for personal injury or death, failure of the operator to pay bills to contractors, or other fault or liability of the borrower-lessee.

To be sure, even beyond the energy lending space, a commercial lender in a sophisticated transaction typically enjoys an array of covenants that might be characterized as elements of control, potentially leading to unanticipated responsibility for a fault of its borrower.

V. Current Issues Involving Executive Rights

The Executive Right is a Mineral Right, With Attendant Consequences

Although article 16 states that the "basic" mineral rights are the mineral servitude, the mineral royalty, and the mineral lease, the executive right is explicitly stated in article 106 to be a "mineral right."[179]

An executive right is "the exclusive right to grant mineral leases of specified land or mineral rights."[180]

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178 *Id*. at *33.

179 *See* Ottinger, *Mineral Lease Treatise*, § 7-08.

180 LA. REV. STAT. ANN. § 31:105.

Being a mineral right, it is "alienable and heritable."[181]

Moral of the Story — Lessons to be Learned

The fact that the owner of an executive right is free to alienate it, or that the exclusive leasing right would be subject to the law of inheritance, ought to give concern to the party creating the right.

One who creates an executive right obviously has a degree of faith, confidence and trust in the person to whom this right is initially granted, but may not have the same level of faith, confidence or trust in a stranger to whom it might be alienated, or in the heirs or legatees of the executive right owner.

In order to obviate this possibility, the party creating the right should either negate the owner's ability to transfer it,[182] or make it personal to the original grantee,[183] and subject to termination at the death of the executive. One might consider language such as the following in order to achieve this objective, to-wit:

> Anything herein contained to the contrary notwithstanding, it is expressly understood and agreed that the rights conferred upon Grantee, as owner of the executive right herein [granted] [reserved], (i) are strictly personal to Grantee; (ii) shall not be conveyed, delegated or otherwise transferred by Grantee without the prior written consent of Grantor, and (iii) shall terminate upon the death or incapacity of Grantee; *provided*, *however*, that the termination under such circumstances shall be without prejudice

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181 *Id*. at § 31:18.

182 "Rights and obligations arising from a contract are heritable and assignable unless the law, the terms of the contract or its nature preclude such effects." LA. CIV. CODE ANN. art. 1984. *See Bryan v. Griggs*, 128 So. 3d 1255, 1264 (La. App. Ct. 2d 2013) ("Based upon the entire record in this case, it is clear that the obligations created by the letter agreement were strictly personal on the part of the obligor, Bryan, and required the special skills or qualifications that he represented that he possessed.").

183 "An obligation is strictly personal when its performance can be enforced only by the obligee, or only against the obligor." LA. CIV. CODE ANN. art. 1766.

to any lawful acts taken by Grantee pursuant to such executive right, prior to such event of termination.

VI. Conclusion

At any point in time, the question of what is a “current issue” in the law of oil and gas in the Bayou State is determined by either economic or market conditions in the industry. While it is difficult to quarrel with this truism, it is equally true that legislative or regulatory actions, or jurisprudential developments, can also give rise to issues with which industry participants and the practicing bar must be concerned.

It is obvious that any identification of these “hot topics” at any particular point in time is more subjective than objective, and reasonable minds can certainly disagree on the litany of these issues. Perhaps this is a case of beauty *vel non* being in the eyes of the beholder.

Nevertheless, it is the hope of this presenter that a review of the issues and matters examined herein will provoke thought as to pitfalls in legislation, as well as providing a glance into future issues that might be presented.