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Mineral Rights

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MINERAL RIGHTS

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I. State Lands and Taxation

A. *Venue for Litigation Regarding Ownership of Waterbeds*

The court of appeal in *Texaco, Inc. v. Plaquemines Parish Government*[1] held that a suit for determination of the ownership of certain waterbeds and for interpretation of a lease in which a parish government was one of the defendants had to be filed before the district court of the judicial district in which the political subdivision is located or in the district court having jurisdiction in the parish in which the cause arises. In this case Texaco, Inc. filed action for declaratory judgment in East Baton Rouge Parish against various defendants, including the state of Louisiana, certain state agencies and Plaquemines Parish Government (a political subdivision of the state). The suit was for determination of the ownership of certain waterbeds and interpretation of a lease. Plaquemines Parish Government filed an exception of improper venue, contending that mandatory venue was in Plaquemines Parish. The trial court sustained this exception and transferred the action to Plaquemines Parish. Texaco and additional plaintiffs appealed. The appeals court affirmed. Under the venue statute,[2] all suits against a political subdivision of the state must be filed before the district court of the judicial district in which the political subdivision is located or in the district court having jurisdiction in the parish in which the cause arises. The political subdivision here is Plaquemines Parish Government, and thus Plaquemines Parish was the mandatory venue for the suit. Plaquemines Parish Government did not waive venue by requesting a document before the ruling on the exception.

B. *Donation of Land to State with Reservation of Mineral Servitude*

The plaintiffs in *Reilly v. State*[3] filed suit to revoke an onerous donation of approximately 15,000 acres of land given to the state in

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1. 527 So. 2d 1128 (La. App. 1st Cir.), writ denied, 533 So. 2d 359 (1988).
2. La. R.S. 13:5101, 5104(B) (Supp. 1989).
3. 533 So. 2d 1341 (La. App. 3d Cir. 1988), writ denied, 536 So. 2d 1219 (1989).

1911 as a wildlife refuge. They claimed that the state and its agencies had breached certain conditions established in the donation. The plaintiffs alleged that the terms of the donation were violated when the defendants authorized a "massive geological exploration" of the property between May, 1976 and March, 1977. Alternatively, the plaintiffs asserted that the 1911 donation created an imprescriptible mineral servitude in their favor. The trial court granted defendants' motion for partial summary judgment, ruling that the mineral servitude at issue had prescribed and that it was not revived by legislation enacted subsequent to the prescriptive date. The appeals court affirmed the partial summary judgment and remanded for further proceedings.[4]

The present lawsuit was instituted by plaintiffs in 1981. The plaintiffs sought an effectuation of their reversionary interest. They claimed the geological exploration operations on the property that the defendants authorized violated conditions in the donation prohibiting defendants from using the lands for "any other purposes other than a refuge or reserve for wildlife" or for "any species of business or manufacture or development" that would defeat the underlying reason for the donation. The plaintiffs also claimed the defendants breached other provisions of the donation that created an affirmative duty on the part of defendants to maintain the refuge in such a manner as to protect the wildlife and aid in their propagation.

There was no claim that the mineral servitude contained in the 1911 donation was maintained by any prior exploratory or developmental operations on the subject tract. This had already been decided adverse to plaintiffs in the earlier litigation. As to the plaintiffs' claim that the Louisiana Legislature abrogated the concept of prescriptible mineral servitudes when the State acquires land subject to a mineral reservation

4. This case was an outgrowth and continuation of an earlier case, State v. Ward, 314 So. 2d 383 (La. App. 3d Cir.), writ denied, 319 So. 2d 440 (1975), which was instituted by the State of Louisiana as a possessory action against the heirs of Edward Avery McIlhenny and Charles Willis Ward and certain corporations who claimed mineral interests in the property by virtue of mineral leases and interests granted by the heirs. The Ward-McIlhenny heirs converted the action into a petitory action, claiming ownership of the property. Additionally, the heirs claimed ownership of the mineral rights by virtue of a mineral reservation included in the donation. The Ward-McIlhenny group asserted the donation did not effect a transfer of ownership. In the alternative, the group argued that they were entitled to a rescission of the donation due to the State's failure to comply with certain resolutory conditions in the donation. The district court entered judgment in favor of the State after a trial on the merits. The judgment held that there was a donation, that the State had substantially complied with the conditions in the act of donation, and that the State owned the property and the mineral interests. Further, the judgment recognized that the heirs had a reversionary interest in the property which they could sue to enforce if the conditions in the donation were not complied with in the future. The trial court's judgment was affirmed by the third circuit court of appeal and writs were denied by the Louisiana Supreme Court.

in favor of the transferor,[5] the court accepted defendants' argument that the legislature never intended any of the acts to be applicable where a reserved mineral servitude had expired and where the retroactive application would impair vested rights acquired by the State. The mineral servitude reserved in the act of donation at issue was extinguished in 1921 by liberative prescription resulting from nonuse for ten years. Ownership of the minerals in the property vested in the State in 1921, seventeen years prior to the effective date of the earliest applicable statute (1938). Thus, the 1938 Act and later acts of the legislature could not affect defendants' vested ownership of the mineral rights. The court also noted there was a final, definitive judgment, rendered in 1975, by all three levels of the Louisiana courts holding that the mineral servitude reserved by the donation had prescribed. Implicit in this holding was that the mineral rights in the property were prescriptible.

C. *Severance Tax*

A purchaser is liable for underpayment of severance taxes that result from the producers' failure to properly certify wells as stripper wells. This was the holding of *McNamara v. Scurlock Oil Company*.[6] In this case, Scurlock Oil Company (Scurlock) purchased oil from Louisiana producers and withheld severance taxes on the purchase price due the owners. The taxes were paid to the Department of Revenue and Taxation (Department) on a monthly basis. The amount of taxes depended on whether the oil was produced from a stripper well, which was eligible for reduced rates of 6 1/4% or 3 1/8% rather than the full rate of 12 1/2%.[7] Scurlock duly paid taxes based on the information furnished by its producers, but on occasion the producers had not complied with the requirements to attain stripper well status. When the Department assessed Scurlock for a deficiency in severance taxes, Scurlock paid $442,495.82 under protest and sought review from the Board of Tax Appeals, which ruled in favor of Scurlock. The trial court reversed the decision of the

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5. The plaintiffs claimed that the Louisiana legislature abrogated the concept of prescriptible mineral servitudes when the State acquires land subject to a mineral reservation in favor of the transferor. The various acts referred to by the plaintiffs were the following: 1938 La. Acts No. 68; 1938 La. Acts No. 151; 1940 La. Acts No. 315; La. R.S. 9:5806 (repealed in 1975); 1958 La. Acts No. 278; 1960 La. Acts No. 528; and La. R.S. 31:149 (1989). These acts, and the amendments by subsequent legislation, are now codified in sections 149 through 151 of the Louisiana Mineral Code. See La. R.S. 31:149-151 (1989). They provide in general that if in the act of acquisition minerals rights normally subject to prescription are reserved to the landowner, they become imprescriptible. See Wall, Imprescriptible Mineral Servitudes in Louisiana, 42 La. L. Rev. 123 (1981).

6. 545 So. 2d 1312 (La. App. 1st Cir. 1989).

7. La. R.S. 47:633(7) (prior to its amendment by 1987 La. Acts No. 755, § 2, and 1987 La. Acts No. 821, § 1).

Board of Tax Appeals. On Scurlock's appeal, the court of appeals affirmed the trial court.

The Louisiana Constitution authorizes the legislature to tax the severance of natural resources "to be paid proportionately by the owners thereof at the time of severance."[8] The producer is not required to withhold the severance tax where a purchaser purchases natural resources under a contract requiring the purchaser to directly pay the owners.[9] Under such circumstances, the purchaser is required to withhold the severance taxes from payments made to the owner and file the requisite reports and pay the taxes due.[10] Thus, because Scurlock had entered into a contract with the owner, Scurlock was required to deduct and remit the tax due to the Department.

The court rejected Scurlock's contention that the Department failed to perform a statutory duty—the proper determination of stripper well status—that caused underwithholding of the severance taxes. The Department's determination of stripper well status was based on certification and monthly reports furnished by the severer. The court found that noncompliance with the statutory requirements for certification was not the fault of the Department. A claim by Scurlock that res judicata applied was also rejected by the court because the prior case, though involving similar issues, involved different producers.

II. Take-or-Pay Litigation

Rights of Royalty Owners

The plaintiffs in *Frey v. Amoco Production Company*[11] were royalty owners who sought a share of take-or-pay payments made by the defendant pipeline to the defendant lessees. The plaintiffs further contended that they were entitled to royalty on benefits Amoco received from "overproduction" under certain balancing agreements and other "side deals." The court ruled that the plaintiffs' motion for summary judgment on "overproduction" issues was premature because facts were in dispute as to whether and to what extent there was "overproduction" or "side deals" in connection with the agreements. On the plaintiffs' claim for royalty on take-or-pay payments, the court ruled that there was no right to share in such payments.

It was undisputed that Amoco and Columbia had a take-or-pay gas purchase contract and that Columbia failed to make certain payments

8. La. Const. art. VII, § 4.
9. La. R.S. 47:637 (1970).
10. La. R.S. 47:638 (1970).
11. 708 F. Supp. 783 (E.D. La. 1989).

under the contract. In settling this litigation, Columbia paid Amoco $20,891,791.00 as a non-recoupable take-or-pay payment, that is, without the right to recoup the payment by later taking gas in excess of the contractually required take-or-pay quantities. Additionally, Columbia paid Amoco $45,633,076.00, retaining the right to recoup this second amount by taking more during a year than required by the take-or-pay provisions in the contract as amended. Amoco had paid royalties to the plaintiffs on all amounts received by Amoco from Columbia (and others) in payment for gas produced and sold from the leased premises, including gas taken by Columbia in recoupment of its recoupable take-or-pay settlement payment to Amoco.

The court held that royalties were only owed on gas which was actually produced and sold, looking to Louisiana law and to the lease royalty clause. The clause stated that royalties must be paid on the "amount realized at the well from such sales." The court said this language was not ambiguous and clearly required a sale of gas in connection with the payment of royalties. Gas could not be owned until actually severed from the formation harboring it and reduced to possession. Louisiana law established that a "sale" of gas could not occur absent physical production and severance of the gas. Therefore take-or-pay payments could not be part of the sale price of natural gas.

The court followed the reasoning set out in *Diamond Shamrock Exploration Corp. v. Hodel*[12] and declined to extend the "mutual benefits" article of the Mineral Code[13] to require royalty to be paid on take-or-pay. The plaintiffs received royalty on amounts realized from the sale of gas, and where there were no amounts realized from such sales, plaintiffs retained ownership of the natural gas in the ground.

III. Contract and Conveyance Interpretation

A. *Indemnification for Party's Own Negligence*

The Fifth Circuit in *Amoco Production Co. v. Forest Oil Corp.*[14] held that a letter agreement between a unit operator and the plaintiff oil company providing that operation of a running log by plaintiff oil company was to be "at the sole cost, risk and expense" of the unit did not contain clear and specific language plainly demonstrating a mutual intent to provide indemnification for damages to operational equipment arising from the sole negligence of the plaintiff oil company.

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12. 853 F.2d 1159 (5th Cir. 1988). The *Frey* court held there was no significant difference between the language employed in the leases in the two cases.
13. La. R.S. 31:122 (1989).
14. 844 F.2d 251 (5th Cir. 1988).

Under Louisiana law, which applied to this action on the Outer Continental Shelf, an indemnification agreement will not be construed to cover losses arising from the indemnitee's negligence unless a mutual intent to provide such indemnification is expressed in unequivocal terms.

Amoco Production Company (Amoco) and Forest Oil Corporation (Forest) were both parties to a field unit agreement for leases on the Outer Continental Shelf. Forest, the unit operator, operated one lease and Amoco operated another. Forest, as field unit operator, requested Amoco to run a log from its lease platform to test a certain sand. The parties entered into a letter agreement providing: "This specific operation shall be performed by Amoco for the account of the Eugene Island Block 273 Field Unit, Forest Oil Corporation, Operator, and at the sole cost, risk and expense of said unit." After running the log, an accident occurred through the sole negligence of an Amoco employee, damaging a crane and a wireline unit. Amoco brought suit under the letter agreement against Forest for these damages. Forest asserted that the agreement did not provide for liability for Amoco's negligence. The trial court ruled for defendant. Amoco appealed, and the Fifth Circuit affirmed. Under Louisiana law,[15] which applies to this action on the Outer Continental Shelf,[16] an indemnification agreement will not be construed to cover losses arising from the indemnitee's negligence unless a mutual intent to provide such indemnification is expressed in unequivocal terms. The court found that the letter agreement at issue here did not contain clear and specific language plainly demonstrating a mutual intent to provide indemnification for Amoco's negligence.

B. *Drilling Contract*

At issue in *Toce Oil Company, Inc. v. Great Southern Oil & Gas Company, Inc.*[17] was whether a turnkey drilling contract had been breached. Toce, an oil and gas exploration company, awarded Great Southern a contract for drilling a well on the basis of its bid. Toce needed the well drilled by the end of December, 1985, and the drilling contract was amended by a letter agreement to so provide. Near the end of December, Great Southern informed Toce that it would rather not drill the well. Toce then turned to another company (Pernie Bailey Drilling Company) to do the drilling. This company declared bankruptcy before completing the well. On January 10, 1986, Toce made demand upon Great Southern for $28,058.19. This represented the difference between the price of Toce's turnkey contract with Great Southern and

15. See Elmer v. Coplin, 485 So. 2d 171 (La. App. 2d Cir.), writ denied, 489 So. 2d 246 (1986); Diamond Crystal Salt Co. v. Thielman, 395 F.2d 62 (5th Cir. 1968).

16. 43 U.S.C. § 1333 (1982).

17. 545 So. 2d 1085 (La. App. 3d Cir. 1989).

the higher contract price which Toce had to pay to Pernie Bailey, the additional costs to modify the drilling site, and the costs for time expended finding a new contractor and negotiating the new turnkey contract. Great Southern refused to pay this sum, and Toce filed suit.

The principal dispute in the litigation was over a paragraph of the amending letter agreement which provided as follows: "Finally, Toce's acceptance is predicated on Great Southern timely providing a rig to drill the subject well during the early part of December so that drilling operations are completed before the end of the year." Great Southern contended that the paragraph was an "escape clause" for Toce's benefit. Great Southern argued the clause meant that if Great Southern did not commence drilling the well in time to complete it by the end of 1985, Toce would no longer be bound by the contract; Toce could then contract with another party to drill the well. Great Southern attempted to characterize the paragraph as a resolutory condition rather than as a counteroffer to Great Southern's proposed original contract. The court rejected Great Southern's reading of the provision and concluded that Great Southern was bound to drill the well and was accordingly liable for damages for failure to drill. The court said that to accept Great Southern's interpretation of the contract would render the contract meaningless. Further, even if this provision had been a resolutory condition, Great Southern had a rig available which it did not use when it had the opportunity, instead placing the rig at another well site for a later contracting party. The court of appeal further stated it was not error for the trial court to admit evidence from Toce attempting to establish this point.

The court also ruled that Toce was a proper party to bring suit; it was the operator for other parties. The contract was with Toce, not with the investors, and those investors would not have been able to bring suit against Great Southern. The court rejected also Great Southern's claim that Toce had suffered loss because it should not have prepaid Pernie Bailey for drilling. The trial court correctly appraised the moral obligation of a bankrupt company as worthless and calculated Toce's damages accordingly. While an injured party has a duty to mitigate damages by exercising reasonable diligence and ordinary care in attempting to minimize his damages after an injury has been inflicted, this principle will not be applied to restrict an injured party's recovery when the injured party is required to make substantial expenditures of his own funds or incurs substantial risks in order to avoid the consequences of a breach of contract.

C. *Conveyance of All Minerals*

The case of *West v. Godair*[18] presented a question of whether sand, gravel, topsoil, and pit run were minerals under mineral reservations in three separate cash sales made in 1982 in which the seller reserved "an undivided one-half (1/2) interest in and to all of the minerals of every nature or kind situated in, on and under the hereinabove described property." A year later the buyers entered into agreements allowing for the exploration and mining of pit run, field dirt, wash gravel, topsoil, and sand on the property purchased from the Wests. In 1986 the Wests made written demand on the Godairs for an accounting in connection with all pit run, field run, field dirt, wash gravel, top soil, and sand mined or removed from the property the Godairs acquired. The defendants contended the mining of these items did not fall within the scope of the mineral reservations contained in the deeds.

The trial court ruled that the substances in question were reserved by the sellers. The court of appeal reversed, ruling that the addition of the words "of every nature or kind situated in, on and under the hereinabove described property," did not suffice to remove the inherent ambiguity found in the term "all mineral rights." The parties had not specifically negotiated the language of the reservations. Considering the fact that the usual and customary reservation of minerals is meant to apply to oil and gas, and that sand and gravel excavation has a serious detrimental effect upon the use and development of the surface, the court applied the interpretation which least restricted ownership of the land conveyed. The Louisiana Supreme Court reversed and reinstated the trial court judgment without rendering an opinion.

This case should serve as a warning to all practitioners against allowing a purchaser of land to agree to a reservation of "all minerals." The owner of a small farm or a house on a modest tract of land may wake up one day to the sound of gravel trucks going onto his or her property. It will be to no avail for the owner to say "I was thinking this meant oil or gas and there was little likelihood of drilling." The value and use of the land may be effectively destroyed by that reservation of "all minerals." Lawyers and land purchasers should be on notice that the Louisiana Supreme Court is likely to treat a reservation of "all minerals" in an expansive manner.[19] The appropriate response to avoid the consequence of this is to limit reservations to "oil and gas" and to put surface use restrictions on the mineral servitude rights.

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18. 538 So. 2d 322 (La. App. 3d Cir.), rev'd, 542 So. 2d 1386 (1989).
19. See also Continental Group, Inc. v. Allison, 404 So. 2d 428 (La. 1981).

IV. Oil Well Lien Act

Furnisher of a Furnisher

In *Baker Chemicals, Inc. v. Arkla Exploration Company*[20] a supplier of mud drilling equipment sought recognition of a lien and privilege on an oil and gas well and appurtenant structures. Baker, the supplier, had entered a warehouse agreement with Drilling Chemicals Inc. ("DCI"). DCI had a man named Willis operating the warehouse. DCI paid him to deliver materials from the warehouse to the well locations. Baker also contracted with Willis to maintain its inventory at the warehouse and to act as its agent in sales to DCI. Willis delivered Baker's materials to Arkla's well. DCI's bills to Arkla were paid in full, but DCI failed to pay Baker $6,578.73. Baker sought recovery of this from Arkla, asserting the existence of a lien based on the Louisiana Oil, Gas and Water Well Lien Statute.[21]

The court of appeal rejected Baker's claim. There was a completed sale from Baker to DCI before DCI ever sold and delivered the materials to Arkla. This transaction broke the link between Baker and Arkla. In effect, Baker furnished materials to DCI and DCI furnished them to Arkla, but Baker did not furnish them to Arkla as required by the statute. The court agreed that the presence of an intermediary sale or lease of material or equipment does not automatically destroy the supplier's right to assert the lien.[22] The general law of mechanic's liens requires that lien statutes must be narrowly construed. The statute does not define "furnish" and does not plainly extend or refuse lien rights to furnishers of furnishers.[23] The court ruled that a "furnisher of a furnisher" who does not actually deliver the materials to the site and does not look to the well for security has not established his right to assert the lien. The court reached its decision by looking to the supplier's expectation of security, following a rationale observed by the third circuit in another Well Lien Act case.[24] Oilfield suppliers know that the purpose

20. 545 So. 2d 709 (La. App. 2d Cir. 1989).

21. La. R.S. 9:4861-4867 (1983 & Supp. 1989).

22. "We stress that a 'furnisher of a furnisher' is not automatically excluded from the protection of R.S. 9:4861 just because he used a middleman or a lessee." 545 So. 2d at 712.

23. See Oil Well Supply Co. v. Independent Oil Co., 219 La. 936, 54 So. 2d 330 (1951), where the supreme court equated "furnishing" with "directly delivering." In Texas Pipe & Supply Co. v. Coon Ridge Pipeline Co., 506 So. 2d 1296 (La. App. 2d Cir. 1987), the second circuit noted that the supplier "delivered the pipe directly to the job site and thereby 'furnished' the identifiable pipe . . ." 506 So. 2d at 1299.

24. P&A Well Serv. v. Blackie's Power Swivels Inc., 507 So. 2d 280 (La. App. 3d Cir.), writ denied, 513 So. 2d 288 (1987).

of the law is to protect the furnisher of materials who supplies the materials directly to the construction site. If the party with whom such a furnisher contracted does not pay the furnisher, he is entitled to a lien against a site. The statute allows a furnisher of materials to take more of a risk in supplying than he ordinarily would, since he has another way to collect. Such is not the case when the supplier's involvement stops with a middleman, illustrated in this case. Baker's only obligation was to maintain an inventory with DCI, and it undertook this obligation looking only to DCI as obligor. Thus, Baker was insulated contractually and physically from the owners and operators who used the materials at the well sites; Baker did not actually deliver the materials to Arkla's wellsite or look directly to Arkla for payment.

V. Lease Maintenance

A. *Effect of Release of Lease*

In *Willis v. International Oil and Gas Corporation*[25] the plaintiffs were the owners of an acre of land that was subject to a servitude for one-half the minerals. The plaintiffs granted a lease for one-half the minerals, while the owner of the servitude had granted a lease to another lessee. The land was included in a unit created by the Commissioner of Conservation. The unit well that was drilled was a marginal producer which was not expected to pay back all of the costs of drilling and operation. The plaintiffs' lessee (sublessee of the original lessee) paid royalty to them for a time but then ceased. The plaintiffs brought suit for an accounting and for unpaid royalties from their lessee, as well as for damages, attorney fees and costs. They also asked that the operator withhold from production and pay them their share of the production. The lessee filed an answer and a third party demand against the unit operator. In the meantime, the plaintiffs' lessee released the lease.

The trial court gave judgment in favor of the plaintiffs against the lessee, requiring an accounting of royalties due for the period from February, 1983 through January, 1984, and also awarding damages of double the amount of unpaid royalties on the unit well for that same period, together with legal interest and attorney's fees. On appeal, this case presented two issues: (1) whether the plaintiffs' sublessee, while in default, could execute a valid release of the mineral lease, thereby avoiding the payment of future royalties; and (2) whether, pending recovery of the well costs, the operator could retain all proceeds from production.

25. 541 So. 2d 332 (La. App. 2d Cir. 1989).

The court of appeal ruled that the lessee's release effectively terminated all interests of the lessee in the lease; after the date of release the plaintiffs were to have the status of unleased owners with respect to the unit well. The lease contained a clause specifically allowing the lessee to release the lease at any time and be relieved of all obligations as to the acreage surrendered. The sublessee had the power to exercise this.

Turning to the second issue, the court found that the operator was entitled to retain 100 percent of the proceeds from the production of the unit well until such time as it recovered the full amount expended for drilling, completing and operating the well. To the extent that the plaintiffs were co-owners of the minerals, and had not participated in the expenses incurred in producing those minerals, they were not entitled to a proportionate share of the proceeds without paying a proportionate share of the expenses. The doctrine of correlative rights did not authorize the court to create a contract between the operator and the plaintiffs.

B. *Production in Paying Quantities*

In *Menoah Petroleum, Inc. v. Mckinney*[26] the plaintiff oil company had obtained a temporary restraining order to prevent the defendant from blocking the company's access to her property. When the hearing was held to determine if a permanent injunction should be issued, the defendant sought to establish that a right of ingress and egress had lapsed because of lease cessation. The issue turned on whether the lease had been maintained by production in paying quantities. The trial court dissolved the restraining order and awarded damages to the defendant. On appeal, the trial court was affirmed despite certain erroneous rulings. The trial court had improperly put the burden on the lessee to show the validity of lease. The general rule is that the party attacking the validity of a recorded mineral lease has the burden of proving the lease's invalidity. The defendant was able to prove that the lease had lapsed due to failure to produce in paying quantities. The lease acreage was in a fieldwide unit created in 1961 by the Commissioner of Conservation and dissolved in July, 1987. Although production of minerals from a unit is tantamount to production from all lands within the unit, production must be in paying quantities.[27] This means the lessee must show a profit.[28]

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26. 545 So. 2d 1216 (La. App. 2d Cir. 1989).

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

28. "[Production] is considered to be in paying quantities when the 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." Id.

The trial court found production revenue totaled only $69,849.59 in 1986, while the unit operation expenses totaled $118,185.74. Although the trial court made an error in the calculation, the court of appeal concluded that this did not alter the determination that the unit failed to produce in paying quantities in 1986.[29] The plaintiff's claim of lower costs which did not include administrative costs, was based on average oil prices rather than actual price received, and was not adjusted for severance taxes or marketing costs. The defendant's expense report (from the operator's report) was more accurate since it contained the actual charges billed by the operator in 1986. The court ruled that overhead should be considered when the unit is being operated by someone other than the lessee.[30] The court also said that ad valorem taxes should be considered when determining whether a reasonably prudent operator would continue to produce a well for the purpose of making a profit and was not merely holding a lease for speculation, since a prudent operator would consider the amount of past due taxes when deciding whether to continue to operate the lease or not. The award of damages for the wrongful issuance of a temporary restraining order was within the discretion of the trial court, and the court's action showed no abuse of discretion. The plaintiff had trespassed upon defendant's property utilizing the temporary restraining order, and damages were thus appropriate.

VI. Servitude Prescription

Confusion

The case of *Texas Gas Exploration Corporation v. Brian Investments, Ltd.*[31] was a concursus proceeding to determine rights to shut-in gas royalty payments. For simplication, the parties will be designated as *A*, *B*, *C*, and *D*. *A* conveyed to *B* some 32,000 acres of land in three parishes, reserving one-half the minerals. *B* executed a document purporting to create a $50,000,000 production payment to be satisfied out of 10% of 100% of the production from the property, specifying that payment of $32,500,000 was to be made to five assignees and $17,500,000 was to be made to *B*. *B* then conveyed the property to *C*, a corporation

29. The court of appeal's calculations showed 1986 expenses of $112,188.46 compared to 1986 revenue of $96,381.28; thus, there was a loss of over $15,000. 545 So. 2d at 1220-21.

30. "We recognize that generally overhead expenses should not be considered as operating expenses for the determination of whether a well is producing in paying quantities or not. This rule does not apply, however, in this case where the unit is being operated by a party other than the lessee." Id. at 1221.

31. 544 So. 2d 67 (La. App. 1st Cir. 1989).

50% of which was owned by *B* and 50% of which was owned by the five assignees; the conveyance was made "subject to" the production payment. There were subsequent assignments of interests from the production payment. *C* filed for bankruptcy, and *D* then acquired the land and 50% of the minerals. *D* also acquired 40% of the 50% of the interest in minerals held by *A*. *D* leased the land to Texas Gas which drilled a well. *B* and *B*'s assignees claimed a share of the shut-in gas royalty from a well on the land because of their interest in the production payment.

The trial court held that since *B* held title to the land that it attempted to burden by the creation of a production payment to itself, the production payment was extinguished by confusion. The appeals court affirmed this determination. A production payment is a limited royalty. *B*'s reservation of the $17,500,000 production payment was the creation of a separate mineral estate which was extinguished simultaneously with the acquisition of the mineral royalty by the original assignees. While *B* was the owner of the property and 50% of the mineral rights (excepting the portions of the production payment originally assigned), *B* could have reserved the mineral rights or a portion of the production payment for future assignment in the act of sale to *C*. But the conveyance to *C* did not do this. The language "subject to" in a conveyance generally does not operate to create new rights; it usually signifies the recognition of rights previously in existence. *B* did not expressly reserve any portion of its mineral rights (or create new mineral rights) in the act of sale. Since the $17,500,000 production payment was extinguished by confusion, the "subject to" language operated to recognize only that portion of the $50,000,000 production originally assigned on October 1, 1976. The documents were neither executed nor recorded simultaneously.[32] Under these facts and circumstances the instruments could not be considered as a single transaction.

VII. Tort Claim

Oil Spill, Damages

The plaintiff in *Street v. Equitable Petroleum Corporation*[33] was the owner of a fishing camp. Oil spilled from an oil well production facility owned by defendants a half-mile from the camp. A current carried some of the oil to the plaintiff's camp area. The plaintiff filed suit against

32. The Assignment of Production Payment was executed on October 1, 1976, and recorded on October 15, 1976. The Act of Sale to *C* was executed on October 6, 1976, and recorded on October 18, 1976.

33. 532 So. 2d 887 (La. App. 5th Cir. 1988).

the defendants for damages she claimed to have sustained. A trial court judgment for the plaintiff was affirmed on appeal. The court held that a violation of Louisiana Civil Code article 667[34] does not require proof of negligence, because the fault of the defendant lies in the damage done to neighboring property. Relief under article 667 requires only proof of damage and causation, and the care and prudence exercised by the defendant is irrelevant in determining liability. The article does not only apply to ultrahazardous activities. The plaintiff's damages consisted of loss of ducks and geese, damage to boats, damages to other parts of the camp site and building and damages to personal effects. The trial court chose not to believe the spill was the result of an act of God through a lightning strike, and the judge was not clearly wrong in failing to relieve defendants of liability based on that defense. The defendants contended that even if the plaintiff suffered the damages she claimed, she had a duty to mitigate those damages. But the court concluded that the plaintiff acted in a reasonable manner, and she had no further duty to mitigate her damages. The trial judge awarded plaintiff $7,120 for her damages. Though the award was not itemized, the plaintiff's evidence showed the replacement cost for her ducks and geese amounted to $3,121.70, leaving $3,998.30 to account for the rest of her property damages and mental distress. The court of appeal concluded that this award did not constitute an abuse of the trial court's discretion.

VIII. CONSERVATION, POOLING AND UNITIZATION

A. *Joint Operating Agreement*

Summary judgment was inappropriate in a dispute over whether a joint operating agreement fixed the interests of the parties in participation from a well despite a subsequent unit order when the instrument in question was ambiguous and susceptible of different interpretations. This was the holding of the court in *Kaiser Aluminum Exploration Co. v. Celeron Oil and Gas Co.*[35]

In 1978 the Commissioner of Conservation created certain 640 acre units, one of which was for the Baxter well. Kaiser Aluminum Exploration Company (KAEC) and Celeron Oil and Gas Company (Celeron) entered into a joint operating agreement for this well and unit. The Commissioner subsequently entered new orders that had the effect of reducing the acreage owned by KAEC in the area to which production was attributed. KAEC filed suit for a declaration that the joint operating agreement fixed the percentage of participation of KAEC in the Baxter

34. La. Civ. Code art 667.
35. 526 So. 2d 374 (La. App. 4th Cir.), writ denied, 531 So. 2d 278 (1988).

well, notwithstanding the subsequent modification of the original unit formed by the Commissioner. The trial court granted summary judgment for KAEC, and Celeron appealed. The appeals court reversed and remanded. The court of appeals concluded that the agreement did not specifically state whether the parties' interests were or were not fixed for all time. The joint operating agreement was ambiguous and susceptible of different interpretations. There were genuine issues of material fact. Thus summary judgment was not appropriate, and the case was remanded for a trial on the merits.

The *Kaiser Aluminum* case reflects a somewhat common area of controversy—the effect of a pooling order upon a prior voluntary or declared unit. There are three possibilities for resolving the issue where a particular effect has not been provided for by the interested parties in their agreement. First, the court can take the position that the prior voluntary agreement takes precedence over the subsequent unit ordered by the state. Many such agreements will, however, have an express provision that they are made subject to laws and regulations of the state, and, in any event, contracts generally are made subject to the state's exercise of the police power. The second approach is that the unit ordered by the state supersedes the voluntary unit of the parties insofar as the compulsory unit sand or formation is concerned. Under this approach, the voluntary or declared unit has no force or effect in the allocation of production where the state has issued an order for a different allocation. The third approach attempts to harmonize the unit order and the voluntary agreement. Several Louisiana cases have dealt with the effect of a compulsory pooling order on a voluntary pooling agreement or an operating agreement.[36] Most of these are discussed in the court's opinion in *Kaiser Aluminum*.

B. *Subsurface Trespass from Approved Injection*

In *Raymond v. Union Texas Petroleum Corp.*[37] a federal district court held that no legally actionable trespass occurs when salt water injected through a disposal well migrates onto the subsurface of adjacent property if the state conservation agency has approved the salt water disposal operation for conservation purposes in a producing oil and gas

36. These include Crow Drilling & Producing Co., Inc. v. H. L. Hunt, 254 La. 662, 226 So. 2d 487 (1969); Monsanto Chemical Co. v. Southern Nat'l Gas Co., 234 La. 939, 102 So. 2d 223 (1958); Texaco, Inc. v. Vermilion Parish School Bd., 244 La. 408, 152 So. 2d 541 (1963); Southwest Gas Producing Co. v. Creslenn Oil Co., 181 So. 2d 63 (La. App. 2d Cir. 1965), writ denied, 248 La. 797, 182 So. 2d 74 (1969); and Humble Oil & Refining Co. v. Jones, 157 So. 2d 110 (La. App. 3d Cir.), writ denied, 245 La. 568, 159 So. 2d 284 (1963). For discussion of these and related cases from other states see 1 B. Kramer & P. Martin, Pooling and Unitization § 13.08[1] (1989).

37. 697 F. Supp. 270 (E.D. La. 1988).

field. In this case the plaintiff landowners brought a claim against defendants for trespass, alleging that defendants injected salt water into a disposal well on neighboring property which migrated to the property (subsurface) of plaintiffs. The plaintiff's land and the land on which the injections took place were within a force-pooled unit established by the Commissioner of Conservation. However, the injections, which were permitted by the Commissioner of Conservation, were into a different formation than the one which was force-pooled, and some of the injected water was from other land not pooled with plaintiffs' land. Plaintiffs contended that the defendants were unlawfully using plaintiffs' subsurface property for disposal of salt water to the extent that the salt water was produced from lands not owned by the plaintiffs and not pooled with plaintiffs's land. Plaintiffs did not challenge the order of the commissioner permitting the salt water injection and did not seek to enjoin the injection; they sought rentals for the use of their subsurface.

The court held for the defendants. There was no legally actionable trespass. Applying *Nunez v. Wainoco Oil & Gas Co.*,[38] the court ruled that the invasion of salt water under plaintiffs' land was part of a disposal operation authorized by the Commissioner. As such, it was not unlawful and did not constitute a legally actionable trespass. While damages would be available upon a proper showing under the *Nunez* standard, there was no evidence here that the injection of the salt water caused harm.

The reported case actually goes somewhat beyond the case on which it relies, *Nunez v. Wainoco Oil & Gas Co.*[39] In *Nunez*, the plaintiff was the owner of land in a compulsory unit, and the unit well, drilled on the surface of an adjacent tract, had drifted onto his property at a point far beneath the surface. The plaintiff in *Nunez* was sharing in the well's production. The case reported here involved injections from land not unitized with plaintiffs (as well as commingled salt water from unitized land). The court nonetheless held that the commissioner's approval of the operation kept the injection from constituting a trespass. In holding this, the court follows the same approach as the Texas Supreme Court in *Railroad Commission v. Manziel*[40] without citing the case or mentioning the concept of the "negative rule of capture" which the Texas court accepted. Since the court recognized that damages would be available where injury is shown, the court did not reject the Oklahoma case of *Greyhound Leasing & Financial Corp. v. Joiner City Unit*,[41] which would apply a doctrine of nuisance to allow damages for un-

38. 488 So. 2d 955 (La. 1986).
39. Id.
40. 361 S.W.2d 560, 565 (Tex. 1962).
41. 444 F.2d 439 (10th Cir. 1971).

derground injections even when approved by the state conservation agency.[42] No Louisiana state court has expressly passed on the precise question ruled on by the federal court in *Raymond*, but the court's decision appears to be a proper application and extension of the principles followed in the *Nunez* decision.

C. *Retroactivity of Order*

A claim for retroactivity of a unit order was involved in *Burley v. Sunbelt Royalty, Inc.*[43] Burley, a landowner under lease, brought suit against his lessee and the purchaser of crude oil (ANCOA). The purchaser was dismissed on an exception, and the landowner appealed the dismissal. The third circuit affirmed the trial court's granting of the exception.

Burley was a party to a voluntary unit agreement. Four sands were involved in the agreement: the Miller, Turner, Artmann, and Nichols sands. A unit was created by the Commissioner of Conservation for the C-5 Sand, and Burley's land was not included in the unit. Approximately two years later, Burley filed a complaint, and the Office of Conservation reassessed the determination of what sands were productive. Based on a finding that the Turner sands were the actual producing sand, Burley's land was encompassed in a new unit that became effective on May 1, 1984. Burley's suit contended that ANCOA owed him back royalty payments from November 1, 1982, to May 1, 1984, since he did not receive any royalty payments within that period of time. He contended that the order of May 1, 1984, should be applied retroactively to November 1, 1982. Burley also argued that ANCOA breached an implied covenant to prevent waste; but, ANCOA, as the purchaser of oil, had no implied covenant obligations to Burley. Nor was the sale of the oil to ANCOA the sale of a thing not owned by the seller because oil is not subject to ownership by the owner of the land until reduced to possession.

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42. See generally, 2 B. Kramer and P. Martin, Pooling and Unitization § 23.03 (1989).

43. 534 So. 2d 101 (La. App. 3d Cir. 1988).