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MINERAL CODE ARTICLE 206 LIABILITY AFTER *GLORIA'S RANCH*: RIGHTS, REMEDIES, REVOLUTION

Andrew D. Martin

INTRODUCTION

For Louisiana oil and gas attorneys, the biggest summer blockbuster of 2017 did not come at the box office. The Second Circuit released its opinion in *Gloria's Ranch L.L.C. v. Tauren Exploration, Inc., et al*¹ on June 2, 2017, and the immense significance of the decision was apparent on impact. One aspect of the decision particularly raised eyebrows: the court's determination that a mortgagee of a mineral lease could be held liable for a failure to acknowledge the extinction of the lease.² The liability allegedly arose via Louisiana Mineral Code article 206, which requires former owners of a mineral right to provide an act evidencing the extinction of that right upon written demand by the party in whose favor the right has extinguished.³

As of January of 2018, the case is pending before the Louisiana Supreme Court, which granted writs in December of 2017. As such, this article is intended less as a summary of a specific result, and more of an exploration of the legal questions related to Mineral Code article 206 liability implicated by the Second Circuit's decision. Broadly, the article addresses the right of a landowner to receive a recordable act evidencing extinction of a mineral right after demand, the remedies available to that

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Attorney, Davidson Summers, APLC. The author is indebted to the following for their perspicacious commentary on the substance of this article: Randall S. Davidson, Grant E. Summers, J. Davis Powell, and Wm. Lake Hearne, Jr., of Davidson Summers APLC, and Ian E. Roberts of Baker Botts, LLP. On a personal level, the author is grateful for the boundless love, indefatigable patience, and irrational confidence of his wife, Heidi Kemple Martin, Esq., and his parents, Prof. Patrick and Dr. Ann Martin, without whom this article certainly would not have been possible.

1. *Gloria's Ranch, L.L.C. v. Tauren Expl., Inc.*, 223 So. 3d 1202 (La. Ct. App. 2017).

2. This article limits itself to a discussion of the Article 206 liability issue, but the remaining issues are certainly interesting and the author concurs with the Court's decisions on those matters.

3. LA. REV. STAT. § 31:206 (1982).

landowner if the former owner of the right fails to comply, and the revolution of the *Gloria's Ranch* court finding a former mortgagee liable under article 206.

Part I of this comment will provide a brief summary of the factual and proceeding history of the case. Part II will give an overview of the relevant statutory law. Part III will analyze the nature of the article 206 obligation and scrutinize the Second Circuit's application of the law to the facts of the *Gloria's Ranch* case. Part IV will explore how the liability for a breach of an article 206 obligation should be shared, and will be followed by a short conclusion.

I. CASE SUMMARY

A. Factual Background

The plaintiffs in *Gloria's Ranch* own over one thousand mineral acres in southern Caddo Parish, spreading across Sections 9, 10, 15, 16, and 21 of Township 15 North, Range 15 West.⁴ Though this area would eventually become a hot spot of Haynesville Shale activity, it was mostly regarded as a staid Cotton Valley area in the early years of the new millennium.⁵ The plaintiffs leased the mineral rights to Tauren Exploration, Inc.⁶ in September of 2004.⁷ The lease was a simple one: a Bath Form, paid up lease with a single page addendum, concerned largely with surface operations and restrictions.⁸ The lease had a three-year primary term, contained a Pugh Clause, and provided for a 3/16th royalty.⁹ Other than the large geographical area leased, it was an unremarkable contract.

4. The acreage covered by the lease at issue in *Gloria's Ranch* totals 1,390.25 acres. *Gloria's Ranch*, 223 So. 3d at 1207.

5. The Haynesville Shale is an upper Jurassic-age shale lying directly beneath the Cotton Valley group. Andrew M. Heacock, *The Frac-As over Property Taxation of Louisiana Oil and Gas Wells*, 1 LSU J. ENERGY L. & RES. 179, 209 (2013); Thomas E. Kurth, Michael J. Mazzone, Mary S. Mendoza & Chris S. Kulander, *The States' Legal Framework: Texas/Louisiana Region American Law and Jurisprudence on Fracing* 14 (2011), <https://perma.cc/C86Q-FBLP>. See also *Peironnet v. Matador Res. Co.*, 144 So. 3d 791 (La. 2013) for another case involving southern Caddo Parish and the transition between Cotton Valley development and Haynesville exploration.

6. *Gloria's Ranch*, 223 So. 3d at 1207.

7. The "Lease." *Id.*

8. Oil, Gas and Mineral Lease, Book 3712, Page 236, Reg. No. 1941789, Caddo Parish Conveyance Records.

9. *Id.*

A year and a half after taking the lease, Tauren assigned an undivided forty-nine percent interest in it to Cubic Energy, Inc.¹⁰ On March 5, 2007, still within the primary term, Tauren and Cubic executed separate credit agreements with Wells Fargo Energy Capital, Inc., a subsidiary of Wells Fargo & Company.¹¹ Wells Fargo Energy primarily operates as a capital provider to all sectors within the energy industry.¹² In this case, Wells Fargo provided Cubic with a revolving credit facility, with no more than \$20 million to be outstanding at any time.¹³ Wells Fargo secured its advances by taking a mortgage on Cubic's interest in the lease. Notably, Cubic's mortgage contained a provision prohibiting Cubic from releasing the lease without the prior written consent of Wells Fargo.¹⁴

Tauren, through a contract operator, drilled Cotton Valley¹⁵ wells on the plaintiff's property in Sections 9, 10, and 16 in 2007.¹⁶ In 2008, Gloria's Ranch's property in Sections 15 and 21 was included in producing Haynesville units operated by Chesapeake Operating, Inc.¹⁷ The Cotton Valley wells in Sections 9, 10, and 16 produced natural gas at fairly low

10. "Cubic" hereafter; *see Gloria's Ranch*, 223 So. 3d at 1207.

11. *Id.* at 1207-08. *See also* Wells Fargo Energy Group, IPAA Private Capital Conference 7-9 (Jan. 22, 2016), <https://perma.cc/C8BC-QFBK>, for Wells Fargo's own description of Wells Fargo Energy Capital, which will be referred to hereafter simply as "Wells Fargo." Tauren's credit agreement and mortgage were not included in the record.

12. *Id.*

13. *Gloria's Ranch*, 223 So. 3d at 1207-08; John T. Bradford, *Damn the Torpedoes: Continuing to Finance U.S. Oil and Gas Operations in Tumultuous Times*, 55 ROCKY MTN. MIN. L. INST. § 22.05 (2009):

Revolving credit facilities . . . are committed facilities providing a maximum amount of capital, which the borrower can borrow, repay, and re-borrow as needed over the life of the loan. The borrower is typically entitled to specify the benchmark interest rate and interest period for each specific borrowing under the facility as amounts are advanced.

14. *Gloria's Ranch*, 223 So. 3d at 1208. This provision will be referred to as the "Consent to Release Clause."

15. The Cotton Valley formation is "a tight gas play in Northeast Texas and Northwest Louisiana located just above the Haynesville/Bossier Shale. It is Upper Jurassic and Lower Cretaceous in origin and consists of sandstone, limestone, and shale. The depth of the Cotton Valley formation is roughly 7,800 to 10,000 feet. Although it is mainly a natural gas play, some oil has been produced in parts of the Cotton Valley." *Cotton Valley Tight Gas*, Oil & Gas Journal, <https://perma.cc/E9GE-VF4Z> (last visited Jan. 26, 2018).

16. *Id.*

17. *Id.*; additionally, Gloria's Ranch executed a top lease to Chesapeake for the Section 21 property.

volumes after the expiration of the lease's primary term in the fall of 2007.¹⁸

In November of 2009, Tauren assigned its interests in the lease below the Cotton Valley formation to EXCO USA Asset, Inc. for \$18,000.00 an acre.¹⁹ Tauren maintained its fifty-one percent interest in the shallower depths.²⁰ In conjunction with this assignment, Cubic assigned an overriding royalty interest in the deep rights to Tauren, who then immediately assigned a portion of it to Wells Fargo.²¹ Tauren also assigned a ten percent net profits interest to Wells Fargo in exchange for a release of the mortgage on Tauren's deep rights interests.²²

In late 2009, Gloria's Ranch began to suspect the lease had expired for a failure to produce in paying quantities and requested information from Tauren, Cubic, EXCO, and Wells Fargo on the revenue and operating expenses of the Lease.²³ After an unsatisfactory response from Tauren, Gloria's Ranch sent a letter to all four parties demanding a recordable act evidencing the expiration of the lease, pursuant to Mineral Code article 206.²⁴ The act was not provided, and Gloria's Ranch filed suit on June 14, 2010.²⁵

B. Suit and Trial Court

The plaintiff's petition claimed that the lease expired at some unspecified point for a failure to produce in paying quantities and that, pursuant to article 207 of the Louisiana Mineral Code, the defendants owed damages as a result of their failure to provide a recordable act stating

18. *Id.* For example, according to the data available on SONRIS, the Gloria's Ranch LLC 9 well in Section 9 never exceeded 600 mcf of production for a single month after August of 2008. The Section 10 well, the Gloria's Ranch LLC 10 well, is even less impressive, having failed to break 300 mcf in a single month after September of 2008. Back-of-the-envelope math using the monthly natural gas wellhead prices listed indicates that the former well was only pulling in around \$1,000 in revenue a month after the summer of 2008. *Natural Gas*, U.S. ENERGY INFO. ADMIN. (Dec. 29, 2017), <https://perma.cc/9N3X-8U7Z>.

19. *Gloria's Ranch*, 223 So. 3d at 1208. EXCO USA Asset, Inc. will be referred to hereafter as "EXCO".

20. *Id.*

21. *Id.*

22. *Id.*

23. *Id.* at 1208-09.

24. *Id.* at 1209.

25. The Petition is available in the Caddo Parish suit records, under suit number 541,758. Petition, *Gloria's Ranch*, 223 So. 3d 1202 (No. 541,758).

as much.²⁶ These damages included “lost leasing opportunities” damages: the potential amounts of bonus payments, royalties, and rentals that the plaintiffs were unable to realize because of the defendants’ refusal to acknowledge the extinguishment of the lease.²⁷

EXCO entered into a settlement agreement with Gloria’s Ranch in August of 2014.²⁸ A trial on the claims against the remaining defendants was held in August of 2015.²⁹ At the conclusion of the trial, the trial court declared that the lease had expired due to a failure to produce minerals in paying quantities.³⁰ The court assessed damages of \$18,000.00 per acre (a total of \$22,806,000.00) against Cubic, Tauren, and Wells Fargo *in solido* for the plaintiff’s lost leasing opportunities.³¹ Further damages of \$726,087.78 were assessed against the same defendants for the failure to properly pay royalties due from the Section 15 production.³² Lastly, the court found that Gloria’s Ranch was entitled to nearly \$1,000,000.00 in attorneys’ fees.³³ In response to motions for new trial filed by the defendants, the trial court amended its judgment on November 23, 2015, to reduce the damages by twenty-five percent to account for the EXCO settlement.³⁴ All defendants appealed.

C. Appellate Decision and Current Status

The Second Circuit affirmed the trial court’s November 23, 2015 revised judgment on appeal. The appellate court agreed that the Lease had automatically terminated for a failure to produce in paying quantities and

26. Petition, ¶¶ 6, 10, *Gloria’s Ranch*, 223 So. 3d 1202; Mineral Code article 207 sets forth the damages due for a breach of an article 206 obligation and is discussed in Part III of this comment.

27. Petition, *Gloria’s Ranch*, 223 So. 3d 1202.

28. *Gloria’s Ranch*, 223 So. 3d at 1209.

29. *Id.*

30. *Id.*

31. *Id.*

32. *Id.* The court essentially awarded treble damages for this award, pursuant to LA. REV. STAT. § 31:140 (1975), the royalty due (\$242,029.26) plus two times that number. This calculation was hotly contested because Mineral Code article 140 does not, on its face, clearly authorize this tripling. However, a review of the history of the improper payment issue compels the conclusion that this is, indeed, what the legislature intended in enacting article 140, a fact recognized by the Gloria’s Ranch panel, and by other courts. *See Wegman v. Central Transmission Inc.*, 499 So. 2d 436, 451 (La. Ct. App. 1986), writ denied, 503 So. 2d 478 (La. 1987); *Samson Contour Energy E & P, L.L.C. v. Smith*, 175 So. 3d 967, 984 (La. Ct. App. 2014), on reh’ en banc (June 10, 2015).

33. *Gloria’s Ranch*, 223 So. 3d at 1209.

34. *Id.*

that all defendants were solidarily liable for the refusal to acknowledge this termination in response to the article 206 demand from Gloria's Ranch.³⁵ In doing so, the Second Circuit overruled a trial court finding that Wells Fargo had been assigned a portion of the working interest of the lease; instead, Wells Fargo qualified as a "former owner" of the lease due to the nature of the particular security devices in its financing contracts with Cubic.³⁶ The Second Circuit affirmed the trial court's judgment in every other respect, including the damages amounts.³⁷

The Second Circuit opinion barely survived applications for rehearing filed by the defendants: both new judges on the rehearing panel would have granted rehearing, while the original three members of the panel would not have.³⁸ Justice Bleich's dissenting opinion painted a bleak picture of the oil and gas industry's future in Louisiana if the majority's opinion was maintained.³⁹ All defendants subsequently filed applications for writ of certiorari, which are currently pending before the Louisiana Supreme Court, all of which were granted on December 5, 2017.⁴⁰

II. STATUTORY FRAMEWORK

Louisiana Mineral Code article 206 is titled "Obligation of owner of expired mineral right to furnish recordable act evidencing extinction or expiration of right; mineral lease" and reads, in pertinent part:

[W]hen a mineral right is extinguished by the accrual of liberative prescription, expiration of its term, or otherwise, the former owner shall, within thirty days after written demand by the person in whose favor the right has been extinguished or terminated, furnish him with a recordable act evidencing the extinction or expiration of the right.⁴¹

35. *Id.* at 1213-24; LA. CIV. CODE art. 1794 (2018) explains: "An obligation is solidary for the obligors when each obligor is liable for the whole performance. A performance rendered by one of the solidary obligors relieves the others of liability toward the obligee."

36. *Gloria's Ranch*, 223 So. 3d at 1221-24.

37. *Id.*

38. *Id.* at 1225-26.

39. *Id.*

40. News Release, Clerk of Sup. Ct. La., <https://perma.cc/NT5Q-5AY4> (last visited Jan. 26, 2018).

41. LA REV. STAT. § 31:206 (1982). The Second paragraph of Mineral Code article 206 concerns mineral leases that expire before the end of the primary term and is not discussed herein.

Article 207 gives teeth to article 206 by imposing on the former owner liability for attorneys' fees and "all damages resulting" from his failure to provide the instrument demonstrating the extinction of the right.⁴² These damages are not available if there is a good faith dispute as to the extinction of any mineral right other than a mineral lease.⁴³ A mineral lease automatically terminates if it fails to produce in "paying quantities" after the primary term.⁴⁴ A lessee's article 206 obligation arises purely from the statute and is not a facet of the mineral lease itself because, after the expiration of the lease, the lessee has no continuing contractual duties to the lessor.⁴⁵

III. THE OBLIGATION

A. Mortgagee Liability

The Second Circuit's decisions on the paying quantities and damages issues, reinforcing prior jurisprudence, are important; its ruling on a lender's liability for a breach of an obligation owed by former mineral rights owners is paradigm-shifting. This ruling is incorrect and should be reversed.

Wells Fargo's legal relationships with the lessor and lessees existed solely through its role as a lender to the lessees. Oil and gas financing arrangements are often complex in practice, but the character of the devices providing for payment and securing the lender in the event of default are easily understood. Similarly, it is not difficult to see why an aggrieved lessor, like Gloria's Ranch, would have an incentive to pursue a lender through its relationship to the lessees.

1. Context: O&G Financing

There were essentially three points of contact between Wells Fargo and the Gloria's Ranch lease: (1) a net profits interest (NPI) in the lease,

42. LA. REV. STAT. § 31:207 (1982).

43. LA. REV. STAT. § 31:208 (1975).

44. LA. REV. STAT. § 31:124 (1976); *Noel Estate, Inc. v. Murray*, 65 So. 2d 886, 888 (La. 1953); *Middleton v. EP Energy E & P Co., L.P.*, 188 So. 3d 263, 265 (La. Ct. App. 2016).

45. *See Shanks v. Exxon Corp.*, 674 So. 2d 473, 478 (La. Ct. App.), writ denied, 679 So. 2d 436 (La. 1996). This does not, of course, absolve a lessee from obligations already incurred. *See Patrick S. Ottinger, What's in a Name? Assignments and Subleases of Mineral Leases Under Louisiana Law*, 58 ANN. INST. ON MIN. L. 283, 327 (2011).

(2) an overriding royalty interest (ORRI) in the lease, and (3) a mortgage over the lease.⁴⁶ In the world of oil and gas operations financing, there is nothing unusual about a lender having these types of ongoing interests in leases.

Oil and gas exploration and production operations are highly capital intensive.⁴⁷ Despite the many brilliant technical innovations in drilling over the last few decades,⁴⁸ the basic task remains expensive, difficult, and speculative: an operator is still punching holes in the ground that stretch thousands of feet vertically (and sometimes horizontally as well) and hoping to find and extract gasified or liquefied dinosaurs.⁴⁹ An average Haynesville well alone will cost an operator over nine million dollars to drill.⁵⁰ For many operators, financing is a necessity. The nature of the planned production operation will generally dictate the sort of lending arrangement between the financier and the operator.⁵¹ Smaller operators often have to rely on private equity financing or complex mezzanine

46. The “Mortgage” hereafter.

47. Bradford, *supra* note 13, § 22.02; Jeffery A. Zlotky, *Equity Financings – Selected Issues in Structuring and Negotiating Private Equity Investments in Oil and Gas Companies*, 52 ROCKY MTN. MIN. L. INST. (2006).

48. See Patrick H. Martin, *What the Frack? Judicial, Legislative, and Administrative Responses to A New Drilling Paradigm*, 68 ARK. L. REV. 321, 325 (2015) for a discussion of how new technology has helped to reduce the costs of drilling.

49. Benjamin Holliday, *New Oil and Old Laws: Problems in Allocation of Production to Owners of Non-Participating Royalty Interests in the Era of Horizontal Drilling*, 44 ST. MARY’S L.J. 771, 774-75 (2013):

[F]ixed costs of drilling alone are just a part of what makes exploration an expensive venture. On top of these significant capital outlays are those less-quantifiable, yet perhaps greater, potential expenses that spring from the persistent risks that accompany hydrocarbon development. These include dry holes and structural integrity failures of the wellbore. The weight of this risk increases significantly when utilizing new, and at times unproven, drilling methods.

Gary B. Conine, *Speculation, Prudent Operation, and the Economics of Oil and Gas Law*, 33 WASHBURN L.J. 670, 687 (1994). Horizontal wells in hard-to-exploit formations incur the additional expense of huge amounts of water, necessary for the fracking process used to “open up” the formation. Laura Springer, *Waterproofing the New Fracking Regulation: The Necessity of Defining Riparian Rights in Louisiana’s Water Law*, 72 LA. L. REV. 225, 227 (2011). Lastly, see *Our History*, LA. CHEMICAL ASS’N, <https://perma.cc/44XU-22GW> (last visited Jan. 4, 2018) (“Louisiana rests on the graves of dead dinosaurs, a Jurassic Park of oil and natural gas that was compressed into the bowels of the earth eons ago.”).

50. Ryan King, *We Need A Fracking Baseline*, 77 LA. L. REV. 545, 581 (2016).

51. Bradford, *supra* note 13.

arrangements.⁵² Financing exploratory wells in a field with unproven reserves will typically require equity capital, rather than debt capital, because of the lack of an assured cash flow to repay debt.⁵³ A known prospect, like the Cotton Valley play targeted by Tauren in *Gloria's Ranch*, allows a borrower a bit more latitude in the sort of capital obtained.⁵⁴

Cubic was able to secure an impressively-sized credit facility of twenty million dollars in 2007, a feat that likely would not have been possible just a year later. By late 2008, a credit crunch had begun to squeeze the oil and gas industry, one that followed the doldrums of the wider U.S. economy after the subprime crisis.⁵⁵ Commodity prices fell, the stock market plummeted, and many small operators were left with little to no access to capital for their operations.⁵⁶ These conditions led to a shift of financing arrangements in favor of lenders.⁵⁷ In times of either feast or famine, however, oil and gas lenders employ a variety of methods to secure their investments. For instance, the lender may require ongoing payments structured as Volumetric Production Payments or Pledged Production Payments.⁵⁸ In addition, the lender may receive equity “kickers” of some sort, providing a permanent interest in the specific leases at issue, either as non-operating interests (like overriding royalties or net profits interests) or sometimes, a portion of the working interest itself.⁵⁹ Lastly, a lender will almost always cover the borrower's interests with a dedicated security device to obtain direct control over these interests upon a default of the borrower's obligations. Conventionally, the execution of a mortgage covers all, or a portion of, the borrower's

52. Jeffrey S. Muñoz, *Financing of Oil and Gas Transactions*, 4 TEX. J. OIL GAS & ENERGY L. 223, 225-26 (2008); Reese B. Pinney, *Capital Sources for the Small Independent Oil and Gas Company*, 49 LA. B.J. 292. For a good overview of private equity investing in E&P companies and projects, see Zlotky, *supra* note 47. Mezzanine financing in the oil and gas financing arena typically refers to “the combination of a borrowing base revolver with the assignment by the borrower of an ‘equity kicker’ to the lender.” Bradford, *supra* note 13, § 22.05.

53. Bradford, *supra* note 13, § 22.03

54. *Id.* § 22.04.

55. Muñoz, *supra* note 52, at 225.

56. *Id.* David B. Spence & Robert Prentice, *The Transformation of American Energy Markets and the Problem of Market Power*, 53 B.C. L. REV. 131, 164 (2012).

57. Bradford, *supra* note 13, § 22.04.

58. *Id.* Muñoz, *supra* note 52, at 228.

59. Bradford, *supra* note 13, § 22.04.

leasehold interests.⁶⁰ Louisiana law expressly makes mineral leases susceptible to mortgage.⁶¹

In the *Gloria's Ranch* case, Wells Fargo had a combination of a borrowing base revolver with two kickers: the traditional ORRI and the NPI. Both of these interests are non-operating interests that are “carved out” of the working interest, but do not arise from true assignments of the working interest.⁶² Therefore, though Wells Fargo had “points of contact” to the lease through these interests, that contact did not reach the lessors. Wells Fargo also had the Mortgage on the leasehold interest, giving Wells Fargo the conditional right to seize and sell that interest upon a default. Given that there was no default, and Wells Fargo never seized the lease, Wells Fargo did not actually have any direct connection to the plaintiffs in this case at any point during the life of the lease. The “relationship” was only indirect through Wells Fargo’s financing contracts with the lessees.

Despite this attenuated connection, there is no great mystery as to why Gloria’s Ranch pursued Wells Fargo. Cubic and Tauren are both small

60. Muñoz, *supra* note 52, at 227 (“Banks usually secure the loans with a mortgage or deed of trust on the oil and gas properties that are being acquired or developed with the proceeds of the loan.”); Jason A. Schumacher, *E&P Lending: Due Diligence and Collateral Legal Issues in E&P Lending Deals for the Texas Law Man in Practice*, 1 TEX. A&M L. REV. 361, 365 (2013) (“The Credit Agreement will have a covenant that a certain percentage of the value of the properties in the borrowing base be under mortgage; it is normally a high percentage but not always 100%”). Additionally, in most states, if a lender has a security interest in the minerals prior to extraction, the Uniform Commercial Code creates a UCC interest in the produced minerals as as-extracted collateral. Louisiana provides for the same effect, provided that the act creating the security—usually a mortgage—specifies that the security attaches to the minerals upon their being reduced to possession. LA. REV. STAT. § 10:9-102(a)(6) (2015). This specification is in the form of a “pledge” of the minerals produced or the proceeds from the sale thereof. LA. REV. STAT. § 31:204(B) (1989).

61. LA. REV. STAT. § 31:203 (1992).

62. *Texas Independent Exploration, Ltd. v. People Energy Production-Texas L.P.*, 2009 WL 2767037, at *1 n.2 (Tex. App. – San Antonio 2009):

An “overriding royalty interest” is a non-participating interest in an oil and gas lease.An owner of an overriding royalty “has no right and thus no ability to go onto the underlying property and drill or otherwise take action to perpetuate a lease”Rather, such an owner is dependent on the lessee to preserve the lease.

PATRICK H. MARTIN & BRUCE M. KRAMER, WILLIAMS AND MEYERS, MANUAL OF OIL AND GAS TERMS 601 (14th ed. 2009):

Net Profits Interest: A share of gross production from a property, measured by net profits from operation of the property. It is carved out of the working interest.

operators who entered bankruptcy shortly after the trial.⁶³ Wells Fargo, as a dedicated provider of capital to exploration and production projects, should have pockets deep enough to satisfy any judgment.⁶⁴ Tauren and Cubic were essentially judgment-proof, leaving EXCO and Wells Fargo as the only solvent parties with any connection to the lease. As mentioned earlier, EXCO settled with the plaintiffs prior to trial. After that, it was only through Wells Fargo that the plaintiffs could hope to see some sort of substantial compensation for the harm they suffered.

2. Second Circuit's Grounds

Justice Bleich's dissent on the rehearing denial of *Gloria's Ranch* is overwhelmingly concerned with policy considerations and limits its legal analysis of the liability issue to a mere two sentences: "I believe this determination was legal error. Solidary liability is never presumed and arises only from a clear expression of the parties' intent or from law."⁶⁵

This latter statement is a correct statement of law—but was already noted in the original Second Circuit opinion.⁶⁶ The extensive discussion of the issue in that opinion should be sufficient to ward off any notion that the panel reached its decision by *presumption*. It is, by all appearances, a good faith attempt to determine the scope of liability for the breach of a legal obligation.

The Second Circuit accurately perceived that the obligee(s), under Mineral Code article 206, is only a "former owner" of an extinguished mineral right.⁶⁷ Therefore, the universe of parties who could be held liable for a failure to provide a recordable act declaring the extinguishment of a mineral right is confined solely to parties properly categorized as former

63. See Lilian Rizzo, *Cubic Energy Files for Chapter 11 Bankruptcy*, WALL STREET J., Dec. 14, 2015, <https://www.wsj.com/articles/cubic-energy-files-for-chapter-11-bankruptcy-1450104346>; Voluntary Petition for Non-Individuals Filing for Bankruptcy, In re Cubic Energy, Inc., No. 15-12500 (Bankr. D. Del. 2015).

64. Still, Wells Fargo's investments have exposed the company to risk. See Dan Freed, *Wells Fargo Energy Investment Unit Sought Risky Deals, Faces Losses*, REUTERS (Apr. 13, 2016), <https://perma.cc/ZNZ8-L57H>:

Wells Fargo Energy Capital had a \$2.1 billion portfolio as of January 2014 Many analysts expect the value to eventually be marked down. . . . [A]s the price of oil has reversed, Wells Fargo may be regretting its deep and wide involvement with the sector. The bank has already set aside \$1.2 billion in reserves for possible losses on energy loans. Barker estimates the bank will need to set aside another \$600 million.

65. *Gloria's Ranch*, 223 So. 3d at 1225.

66. *Id.* at 1219.

67. *Id.* at 1218.

owners of that right. The task was thus to determine which of the defendants qualified as a former “owner” of the lease, which was the mineral right at issue.

As noted by the Second Circuit, a lessee’s interest in a mineral lease is susceptible of co-ownership, such that many parties could simultaneously be partial owners of a lease.⁶⁸ For there to be co-ownership of a mineral lease, two or more mineral lessees must own undivided fractional interests in the same mineral lease.⁶⁹ The panel pointed out that ownership in the civil law conveys three rights to the owner of the thing: *usus*, or the right to use; *fructus*, or the right to the fruits; and *abusus*, or the right to alienate.⁷⁰ The court then determined that Wells Fargo, in fact, did have each of these rights in the lease through its relationships with the lessees. This determination was made despite the fact that the Second Circuit correctly overruled the trial court’s finding that the Mortgage contained an assignment of the lease’s working interest.⁷¹

The Second Circuit found that Wells Fargo had *fructus* of the lease because of an “assignment of proceeds” clause in the Mortgage and because of the existence of the overriding royalty and net profits interests.⁷² These provisions allegedly gave Wells Fargo the right to share in production from the lease.⁷³ Next, the Court determined that Wells Fargo was had *usus* because it purportedly exercised control over Cubic’s oil and gas operations, including holding the right to approve well locations and depths and actually directing Cubic to perform specific operations on other properties collateralized in the mortgage.⁷⁴ Lastly, the Second Circuit premised the finding of *abusus* on the notion that the Consent to Release Clause gave Wells Fargo control over Cubic’s ability

68. *Id.*

69. LA. REV. STAT. § 31:168 (1975).

70. *Gloria’s Ranch*, 223 So. 3d at 1223. *See* *Campbell v. Pasternack Holding Co.*, 625 So. 2d 477, 484 n.13 (La. 1993):

Ownership may be characterized by its elements: the right to use (*usus*), the right to enjoyment (*fructus*), and the right to alienate (*abusus*). Ownership is also characterized by its forms: perfect ownership, with the elements of *usus*, *fructus*, and *abusus*; usufruct, with *usus* and *fructus*; and naked ownership, with *abusus*. Under the Louisiana Civil Code and jurisprudence, holding in common means at least holding the same form of ownership in the same property.

71. *Gloria’s Ranch*, 223 So. 3d at 1222: “Since the Cubic mortgage does not include the transfer of Cubic’s working interest in the lease, the mortgage did not include an assignment of the lease.”

72. *Id.* at 1223.

73. *Id.*

74. *Id.* at 1223-24.

to release the lease.⁷⁵ The court found it important that the vice president of Cubic informed the plaintiffs in 2008 that Cubic could not “release” the lease for a failure to produce in paying quantities because it was collateralized in Cubic’s credit facility with Wells Fargo. Based on these conclusions, the Second Circuit determined that Wells Fargo was a former “owner” of the lease.

3. Ownership of Mineral Lease

What is most jarring about the Second Circuit’s conclusion that Wells Fargo was a “former owner” of the lease is a number of correct determinations indicating the opposite, chief among them being that Wells Fargo never obtained a working interest in the lease.⁷⁶ Despite pointing out the various ways in which Wells Fargo was not a former owner of the lease, the Second Circuit still held it to be one, and therefore liable for an article 206 breach.⁷⁷ This was an error because Wells Fargo did not possess all three requisite elements of ownership – *fructus*, *usus*, and *abusus*.

a. *Fructus*

Wells Fargo enjoyed the fruits of the lease by way of the ORRI and NPI; through these interests, it was entitled to a portion of the proceeds derived from the sale of production from the lease. However, a claim to the fruits of something is not indicative of “ownership” of that thing. As Professor Yiannopoulos explained:

According to traditional civilian ideas, maintained in modern codes, civil fruits accrue by virtue of an obligation; hence one entitled to civil fruits acquires a “claim” for the collection of civil fruits rather than “ownership” thereof. Accordingly, the mode of acquisition of civil fruits is ordinarily a matter governed by the agreement of the parties and the law of obligations.⁷⁸

75. *Id.*

76. Additionally, the Court noted that: the Mortgage did not contain an assignment of the lease to Wells Fargo; a mineral lease conveys the rights to explore and develop, to produce minerals, to reduce them to possession, and to assert title to a specified portion of the production; the right to receive a share of proceeds from a lease is distinct from a right to conduct operations on that lease; the Mineral Code declares that a mineral right is susceptible of mortgage. *Id.* at 1218-22.

77. *Id.* at 1224.

78. A.N. YIANNPOULOS, 2 LOUISIANA CIVIL LAW TREATISE, PROPERTY § 2:30, (5th ed. 2015); Ross v. Ross, 857 So. 2d 384, 389 (La. 2003).

The proper characterization of an overriding royalty and net profits interest is discussed in greater depth hereafter. For the purposes of the present section, however, it is enough to say that the holder of an overriding royalty is not thereby automatically the owner of a mineral lease.

The Second Circuit mistakenly took the presence of an “assignment of proceeds” clause in the Mortgage as evidence of Wells Fargo’s contemporaneous right to share in the production of the lease.⁷⁹ This clause did not actually give Wells Fargo any pre-default rights to enjoy those proceeds. Though an assignment of production provision sometimes appears, if read in isolation, to be an unconditional assignment, it is in reality simply a collateral device.⁸⁰ The assignment of proceeds clause operates to create a “pledge” of the produced minerals.⁸¹ A pledge is a security interest and nothing more.

b. Abusus

The conclusion that Wells Fargo had the right of alienation as to the lease appears to be founded entirely on the Consent to Release Clause. The Second Circuit apparently believed that Wells Fargo “controlled Cubic’s ability” to alienate by way of this provision, and thus Wells Fargo shared some of that alienation authority. This determination was ostensibly bolstered by the testimony of the manager of Gloria’s Ranch, Ron Lepow:

Lepow testified that he emailed [Cubic VP of Operations Jon] Ross in summer 2008 about releasing the lease for failure to produce in paying quantities. Ross responded to Lepow by stating, among other things, that he could not release Cubic’s interest in the lease because it was collateralized in Cubic’s credit facility with Wells Fargo. . . . *Wells Fargo . . . controlled Cubic’s ability to release the lease for failure to produce in paying quantities.*⁸²

This reasoning is flawed on two fronts: Wells Fargo had no legal control over Cubic’s ability to provide any sort of release, and no “release” was at

79. *Gloria’s Ranch*, 223 So. 3d at 1223.

80. “An assignment of production provision is a common feature of oil and gas mortgages. Even though some assignment of production provisions, if read by themselves, appear to be unconditional assignments of the right to production proceeds, *they are collateral devices and do not approach ‘true sale’ status.*” Terry I. Cross & Jason T. Barnes, *Oil and Gas Liens & Foreclosures – A Multi-State Perspective*, 51 OKLA. L. REV. 175, 181 (1998) (emphasis added).

81. See *supra* text accompanying note 59.

82. *Gloria’s Ranch*, 223 So. 3d at 1223-24 (emphasis added).

issue in the lessee's failure to provide a recordable act evidencing the extinction of the lease.

Mineral Code article 206 does not contemplate the "release" of a mineral lease at all. When a lease fails to produce in paying quantities, it automatically expires, and there is no longer anything to release.⁸³ Article 206 demands a written instrument acknowledging that the lease has expired. At the time of the demand from Gloria's Ranch, there was no longer any mineral lease to alienate. Consequently, *no one* had the right of *abusus* for the lease at that point; it simply no longer existed. As such, Cubic had a statutory obligation to provide a recordable instrument reflecting that expiration.⁸⁴ Cubic was not bound by the terms of its contract with Wells Fargo to withhold the furnishing of that recordable instrument because the "Consent to Release" clause literally only applied to active leases.

This might appear to be a purely academic distinction, as it is easy to imagine a situation where a former lessee furnishes the requested act of extinction, but the lessee's mortgagee incorrectly believes the lease is still in force and is therefore being released. Under this counterfactual, a mortgagee would likely consider the lessee in default and might attempt to foreclose on the property through the provisions of its mortgage, perhaps seizing and selling it. This would present problems for the lessor, as the foreclosure might procedurally skip ahead of a lease expiration suit and would, in any case, scare off potential new leasing activity. This hypothetical reveals nothing about a *right* to alienate, however, because it only illustrates an example of a mortgagee acting without a right, believing it has one. This potential unlawful exercise of power cannot aid in determining whether Wells Fargo ever had a lawful right to alienate.

83. There is no question that lawyers and courts often refer to the recordable act evidencing extinction as a "release." See *Chesapeake Operating, Inc. v. Richardson*, 884 So. 2d 1263, 1264 (La. Ct. App. 2004); *Gloria's Ranch*, 223 So. 3d at 1209; *Wood v. Axis Energy Corp.*, 899 So. 2d 138, 146 (La. Ct. App.), *writ denied*, 904 So. 2d 702 (La. 2005). That usage is easily understood in context. However, any release of an existing mineral lease tautologically can only occur while the lease is in existence. For instance, mineral leases sometimes specify that a lessee is obligated to release all portions of the lease the lessee is unwilling to develop. See *Wier v. Grubb*, 82 So. 2d 1, 4 (La. 1955). This constitutes a true release of a mineral lease, rather than an acknowledgment that the lease is expired. This is discussed further below.

84. Indeed, Cubic *only* had a statutory obligation at that point, as there are no ongoing obligations under a mineral lease that no longer exists. See *supra* text accompanying note 45.

The Second Circuit in *Gloria's Ranch* conflated two distinct legal rights: (1) Wells Fargo's contractual right to consent to any release of the lease and (2) the right to release the lease. The first right exists and is a function of the contract between Cubic and Wells Fargo.⁸⁵ Had Cubic decided to release the lease while it was still in force, Wells Fargo would be entitled to proceed against Cubic alone for a breach of their agreement.⁸⁶ If such a release had occurred, Wells Fargo could proceed against Cubic, but would have no rights to the formerly leased property, as the lease would be dissolved.⁸⁷ The second right is inherent in any mineral lease,⁸⁸ but is clearly not referenced, much less assigned, in the financing contracts with Wells Fargo. Wells Fargo itself could not independently "release" the lease under the terms of the contract or under

85. Through the Consent to Release Clause.

86. See *Matter of Dibert, Bancroft & Ross Co., Ltd.*, 117 F.3d 160, 178 (5th Cir. 1997).

87. Though an unauthorized release would be a breach of the contract between Wells Fargo and Cubic, it would not enable Wells Fargo to seize and sell the mortgaged property, which was just the Lease. LA. CIV. CODE art. 3307 (2017) states:

A mortgage has the following effects:

- (1) Upon failure of the obligor to perform the obligation secured by the mortgage, the mortgagee may cause the mortgaged property to be seized and sold in the manner provided by law and have the proceeds applied toward the satisfaction of the obligation.
- (2) The mortgaged property may not be transferred or encumbered to the prejudice of the mortgage.

This would prevent an unauthorized *assignment* of the Lease by Cubic to a third party and would enable Wells Fargo to ignore the assignment and proceed against the property itself. See *Freedman v. Ratcliff*, 162 So. 783, 785 (La. 1935):

The pact de non alienando, in an act of mortgage, does not prevent the mortgagor from selling the property, subject to the mortgage, but gives the mortgagee the right to ignore a sale of the mortgaged property and to proceed only against the mortgagor.

But a released lease does not exist and is not "transferred or encumbered" by the release. This "property" no longer exists, and thus, cannot be seized.

88. As explained earlier, a true release occurs while a lease is still in existence. The lessee's authority to unilaterally release any acreage is explicit in almost every mineral lease. The *Gloria's Ranch* lease states, in Paragraph 10:

Lessee may at any time and from time to time execute and deliver to lessor or file for record a release or releases of this lease as to any part or all of said land or of any mineral or horizon thereunder and thereby be relieved of all obligations as to the released acreage or interest.

Furthermore, even if a lease were silent on this point, Louisiana law allows for the release of all or part of the lessee's interests. See *Ottinger*, *supra* note 45, at 326.

the law; had Wells Fargo declared to the plaintiffs that it was releasing the lease while the lease was alive, no legal effect would follow. Only the working interest owners could legally alienate their interests in the lease.

Because of the mortgage, Wells Fargo could sell the lease, provided it was still active, at a private sale *if* Cubic had defaulted on its payments to Wells Fargo. This would only occur in the event of a default—a default that did not occur during the life of the lease. As Wells Fargo noted on appeal, this is no different than a residential mortgagee selling a homeowner's house upon default and foreclosure.⁸⁹ The right to sell mortgaged property in the event of default is a function of the right of mortgage, not ownership.⁹⁰ Because of Louisiana's bar on self-help recourse, such a sale only occurs after the designated judicial procedures are followed.⁹¹ Any rights Wells Fargo might have had under the Consent to Release Clause were never triggered. In the event of a true default by Cubic and a subsequent seizure, Wells Fargo would qualify as a working interest owner and would thereafter be potentially liable for an article 206 breach. Under the facts presented in *Gloria's Ranch*, however, only Cubic, Tauren, and possibly EXCO ever had a right to alienate the Lease.

c. Usus

The primary flaw of the Second Circuit's ruling that Wells Fargo possessed the right of *usus* in the lease is identical to its error on *abusus*: the court mistook a conditional, accessory right as evidence of an actual, current right.⁹² The fact that Wells Fargo could, in the event of default and after a seizure through judicial means, assume operational control of the lease does not entail that Wells Fargo ever actually possessed the right to use the lease.⁹³ The post-default right to possession does not transmogrify a mortgagee into an owner *prior* to default. Wells Fargo's potential ability

89. Reply Brief for Defendant-Appellant, Wells Fargo Energy Capital, Inc., No. 51,077 (La. Ct. App. 2017) (citing *Matter of Dibert, Bancroft & Ross Co., Ltd.*, 117 F.3d 160 and *Freedman*, 162 So. 783).

90. *Id.* (citing LA. CIV. CODE art. 3279 (2017)).

91. LA. CIV. CODE art. 3279, cmt. (b) (2017) (“The requirement that the seizure and sale must be ‘in the manner provided by law’ emphasizes the long tradition in Louisiana of requiring recourse to judicial procedures and generally rejecting private sale or self-help as a method of execution.”).

92. See LA. CIV. CODE art. 3282, cmt. (a) (2017) (“Mortgage is accessory to the obligation that it secures.”). (“[T]he rights of the mortgagee may not be enforced until the principal obligation is due and unperformed ”) *Id.*

93. See LA. CIV. CODE art. 3278 (2017); (“Mortgage is a nonpossessory right created over property to secure the performance of an obligation.”).

to use the lease as a lessee was never triggered, and it therefore never had the right of *usus*.

The finding was not just that Wells Fargo had a right to take operational control in the event of default. Instead, the court affirmed the trial court's finding that Wells Fargo did, in fact, exercise that right.⁹⁴ Wells Fargo ostensibly "exercised control" over Cubic's right to conduct operations on the lease by retaining the right to approve of well locations, well depths, and operating agreements, directing Cubic to perform workovers on other properties collateralized in the mortgage, and by reviewing Cubic's financial statements.⁹⁵

The right of use granted in a mineral lease is the "right to explore for and produce minerals."⁹⁶ A lessee has these rights, as do any assignees of all or part of the lessee's working interest.⁹⁷ This right entails that its holder is entitled to the proceeds of production but also is required to pay the costs incurred in the use of the right. A lessee can, however, contract with third parties to perform some of the legwork required in exploration and production activities, a fact apparent even under the facts of *Gloria's Ranch*.⁹⁸ Tauren hired Fossil Operating Inc. as a contract operator in 2007, and Fossil actually drilled several wells on the lease. Fossil "used" the right to explore for and produce minerals, but this right was still one that belonged to Tauren. Had Tauren cancelled its contract with Fossil, the latter company would not be entitled to explore for or drill anything. Similarly, Fossil could not have been liable to the lessors for any breach of lease obligations. In the same manner, even if Wells Fargo actually participated in the execution of any of Cubic's exploration or production activities (a fact not apparent in the record), such participation was not evidence of any independent *right* of use.

Even more flawed is the notion that Wells Fargo's right to review the financial statements or well information of Cubic constitutes a right to "use" the rights granted under the lease. Reviewing paperwork is not equivalent to exploring for or producing minerals. If it were, then accounting firms who have performed audits on lessees have, in so doing,

94. *Gloria's Ranch*, 223 So. 3d at 1223.

95. *Id.*

96. LA. REV. STAT. § 31:114 (1975).

97. LA. REV. STAT. § 31:128 (1975) ("To the extent of the interest acquired, an assignee or sublessee acquires the rights and powers of the lessee and becomes responsible directly to the original lessor for the performance of the lessee's obligations.").

98. For examples of contract operators, *see*: *Jardell v. Hillin Oil Co.*, 485 So. 2d 919, 921 (La. 1986); *Caskey v. Kelly Oil Co.*, 737 So. 2d 1257, 1260 (La. 1999); *Wood*, 899 So. 2d 138.

risked liability as “former owners” under article 206. This is simply not the case. Without access to this information, a secured lender would lack any significant ability to gauge his borrower’s ongoing ability to make payments.⁹⁹

d. Summary

Wells Fargo was never an owner of the lease in name or in fact. A mortgagee of an oil and gas lease holds only a conditional right in a lease. In *Gloria’s Ranch*, this conditional right never became anything more. A party cannot “own” a mineral lease without any working interest in that lease. Because Wells Fargo was never an owner of the lease, it was not a “former owner” when that lease expired. The rulings to the contrary by the trial court and the Second Circuit were in error.

B. Ownership of Other Mineral Rights

1. Overriding Royalty and Net Profits Interest

Wells Fargo was not a “former owner” of the lease and should not have been held liable for the failure to provide an act evidencing the extinction of that lease. Wells Fargo was the former owner of an overriding royalty interest and a net profits interest, both “carved out of” the lease. If these qualify as “mineral rights” under the Louisiana Mineral Code, then Wells Fargo was the former owner of those mineral rights. Might it then be proper to hold Wells Fargo liable for Wells Fargo’s failure to provide a recordable act evidencing the extinction of the ORRI and NPI?

The answer is certainly no. First, overriding royalty interests and net profits interest are not “mineral rights” as that term is used in the Mineral Code. Mineral Code article 16 states, in pertinent part: “The basic mineral rights that may be created by a landowner are the mineral servitude, the mineral royalty, and the mineral lease. This enumeration does not exclude the creation of other mineral rights by a landowner.”¹⁰⁰

Louisiana’s strong policy against dismemberments of ownership is implicit in the framework of the Mineral Code and in article 16 in particular; landowners are presumed to have all rights inherent in property ownership, including the right to explore for and produce minerals.¹⁰¹ All

99. This is an essential part of a lender’s ability to conduct ongoing due diligence on the borrower. *See* Schumacher, *supra* note 60, at 362.

100. LA. REV. STAT. § 31:16 (1975).

101. *See* LA. REV. STAT. §§ 31:6, 31:8 (1975); this policy is evident in the existence of Louisiana’s unique mineral servitude regime. *See* Cohort Energy

“mineral rights” are derivative of the landowner’s original right to explore and develop his property for the production of minerals;¹⁰² hence, the specification in article 16 that *landowners* create mineral rights, and that any rights in addition to the servitude, royalty, or lease must also be created by a landowner. The overriding royalty and net profits interests, on the other hand, are created out of the working interest by a working interest owner. Neither interest is a freestanding “mineral right” that exists on its own; both are mere *interests in* another mineral right. As a result, articles 206 and 207 do not apply to either.

This conclusion is in contradiction to decisions by the Louisiana First and Third Circuits. The former court stated, in *Terry v. Terry* that:

A mineral right is an incorporeal immovable. It is alienable and heritable. LSA–R.S. 31:18. The basic mineral rights are the mineral servitude, the mineral royalty, and the mineral lease. These mineral rights are classified as real rights. LSA–R.S. 31:16. Overriding royalties are, therefore, classified as real rights and incorporeal immovables.¹⁰³

The *Terry* court cited to the Third Circuit’s decision in *Duncan v. Paragon Res., Inc.*, which approvingly quoted the trial court for the proposition that “[a]n overriding royalty interest is a mineral right, and, as such, it is classified as a real right and an incorporeal immovable.”¹⁰⁴ Respectfully, these courts misunderstood the distinction between a mineral right and an interest in a mineral right. This split is clear in Mineral Code article 126 and its comment, which discuss interests “created out of the mineral lessee’s interest,” such as overriding royalties.¹⁰⁵ The mineral lease is the right, and the ORRI is an interest derived from that right, rather than a right itself. The lessee is the only *owner* of the right.¹⁰⁶

Co. v. Caddo-Bossier Pars. Port Comm'n, 852 So. 2d 1174, 1178 (La. Ct. App. 2003). The law of Louisiana regarding prescription of mineral interests reflects a historically strong policy against separate ownership of minerals and a policy of keeping land and minerals in commerce.

102. LA. REV. STAT. § 31:6 (1975).

103. *Terry v. Terry*, 565 So. 2d 997, 1000 (La. Ct. App. 1990).

104. *Duncan v. Paragon Res., Inc.*, 417 So. 2d 850, 854 (La. Ct. App.), *writ denied*, 421 So. 2d 908 (La. 1982).

105. LA. REV. STAT. § 31:12 (1975) & Comment.

106. For an exhaustive analysis of the nature of the ORRI, which also characterized that interest as a “mineral right,” see Randall S. Davidson, *The Overriding Royalty at the 27th Annual Louisiana Institute on Mineral Law* 38-109 (1980).

Second, even if Wells Fargo was the former owner of a mineral right, the plaintiffs may not have adequately demanded that Wells Fargo furnish an act evidencing the extinction of *that* mineral right. The plaintiff's demand letter reads, in full:

Gentlemen, Gloria's Ranch, L.L.C. reviewed the information provided by Mr. Canaday regarding the Gloria's Ranch 16 #1, 9 #1, and 10 #1 Wells. The above referenced mineral lease has expired because none of these wells are, or have been for some time, producing in paying quantities. Please furnish a recordable act evidencing the expiration of this mineral lease.¹⁰⁷

The only expired mineral right referenced here is the lease itself. Even if an ORRI or NPI represented a separate mineral right, Gloria's Ranch never actually demanded an act evidencing the extinction of either. Therefore, it would not seem that Wells Fargo would have a corresponding obligation to furnish an act relating to either. As a practical matter, whether ORRIs and NPIs are technically "mineral rights" or not, landowners are probably better off drafting all Mineral Code article 206 demand letters as broadly as possible. A demand for an act evidencing "*any and all* expired mineral rights formerly held" by the former owner might be safer for a landowner than more specific language.

Lastly, if the ORRI and NPI are considered distinct mineral rights, Wells Fargo would probably still not be liable for the same damages as the remaining defendants. The existence of a good faith dispute as to any expired mineral right other than a mineral lease precludes the landowner from collecting the damages detailed in article 207.¹⁰⁸ It seems unlikely that Wells Fargo was in bad faith under the facts presented in *Gloria's Ranch*.

2. Sublease

A more complicated "other mineral right" possibility is the sublease. Both Cubic and EXCO received partial "assignments" of the lease in *Gloria's Ranch*. Though Cubic never addressed the issue, EXCO argued vigorously that its transfer from Tauren constituted a sublease.¹⁰⁹ EXCO

107. Plaintiff's Trial Exhibit 112, *Gloria's Ranch*, 223 So. 3d 1202.

108. LA. REV. STAT. § 31:208 (1975).

109. EXCO's Memorandum in Support of Motion for Partial Summary Judgment, *Gloria's Ranch*, No. 541,768 (La. Ct. App. 2013).

claimed a sublessee bears no article 206 duty and therefore cannot be liable for article 207 damages.¹¹⁰

A true assignment of a mineral lease requires that the transferor assign all of his rights to a given portion of the lease to a third party.¹¹¹ As will be discussed later, this might occur through an assignment of a discrete portion of surface acreage or of a given subsurface horizon. A sublease, on the other hand, requires that the grant be of less than all of the transferor's interest in the assigned property. The sublease is said to be a new lease "engrafted upon" the original lease.¹¹² Louisiana has a long, complicated, and contradictory history on the sublease/assignment distinction, one that was not cleared up with the adoption of the Mineral Code.¹¹³ A true assignee will clearly be subject to the article 206 duty after the expiration of his portion of the lease, but a sublessee's responsibility is less obvious.

The considerations that render a holder of an overriding royalty something less than an "owner" of a mineral right are relevant to a determination of a sublessee's obligation, if any, under article 206. Like an overriding royalty, a sublease is carved out of the lessee's interest, rather than a landowner's interest. Unlike a third party's interest after a true assignment, a sublease is dependent on the continued existence of the transferor/sublessor's interest.¹¹⁴ In many respects, it is easy to view a sublease as a mere interest in the mineral right of another, rather than an independent "mineral right" that a party can own. If that is the case, EXCO was correct that a sublessee is not a former owner subject to the duty imposed by article 206.

On the other hand, as far as family resemblances go, a sublessee *looks* much more like an "owner" than a holder of an overriding royalty interest.¹¹⁵ A sublessee acquires *all* of the rights and powers of the lessee

110. *Id.*

111. Randall S. Davidson & Andrew D. Martin, *Mineral Lease Division Revisited-An Old Doctrine with New Applications*, 2 LSU J. ENERGY L. & RES. 1, 4 (2013).

112. *See Hoover Tree Farm, L.L.C. v. Goodrich Petroleum Co.*, 63 So. 3d 159, 180 (La. Ct. App. 2011).

113. *See Ottinger, supra* note 45; LA. REV. STAT. §§ 31:127-130 (1975) reference subleases and partial assignments but do not attempt to flesh out the distinction.

114. LA. REV. STAT. § 31:126 (1975).

115. On "family resemblances," *see*: LUDWIG WITTGENSTEIN, P.M.S. HACKER & JOACHIM SCHULTE, *PHILOSOPHICAL INVESTIGATIONS*, §§ 65-67 (4th ed. 2009), where the phrase is used to highlight the fact that we can meaningfully use the same word-concept across many contexts, even if no single trait is common to all

to the extent of the interest acquired.¹¹⁶ On the same note, the sublessee is directly responsible to the lessor for performance of the lessee's obligations.¹¹⁷ During the life of the lease, the sublessee looks and acts like a lessee for every practical purpose: he seems to possess and exercise *fructus, usus, and abusus*.¹¹⁸ It is true that the article 206 obligation is not an obligation of the former lessee *qua* lessee; it is a statutory obligation that applies to all former owners, rather than a contractual duty. It would be a curious asymmetry, however, for a sublessee to have all obligations of a lessee, both contractual and statutory, *during* the life of the lease but no statutory obligation *after* the expiration of the lease. This imbalance would be odd because it is seldom obvious whether a transferee is better classified as a sublessee or an assignee.

The trial court in *Gloria's Ranch* pretermitted discussion of the question of a sublessee's obligation because it found, as a factual matter, that EXCO was better classified as a partial assignee.¹¹⁹ The Second Circuit, despite its in-depth analysis of Wells Fargo's liability, did not touch this issue and reduced the total damage award by twenty-five percent to account for EXCO's assumed virile share. Given the amounts of money at stake, not to mention the implications for Cubic's liability, the question should have been considered by the appellate court.

C. The Policy Behind Article 206

The purpose of Louisiana Mineral Code articles 206 through 209 is to allow mineral owners an avenue to have their titles cleared easily, with penalties for recalcitrant parties who impede this process. The potential for an attempted foreclosure by a former lessee's mortgagee after the lessee furnishes the required act, as described in Section IV(A)(3), certainly opens the door for a serious headache for the former lessor. Such

usages. A lessee, a sublessee, and a mineral servitude owner may not have a single core characteristic in common, but there is a "criss-crossing network" of overlapping usages that makes reference to all three as "owners of a mineral right" sensible. That "network" is not apparent for the more limited ORRI or NPI interests.

116. LA. REV. STAT. § 31:128 (1975).

117. *Id.*

118. On *abusus*: the sublessee cannot independently "release" the prime lease. However, he can release his interest in the lease or sub-sublease that interest. *See Robinson v. N. Am. Royalties, Inc.*, 463 So. 2d 1384, 1388 (La. Ct. App.), *amended*, 470 So. 2d 112 (La. 1985).

119. Trial Court's Reasons for Judgment on Motion for Partial Summary Judgment by EXCO Operating, LP, *Gloria's Ranch*, 223 So. 3d 1202 (Apr. 19, 2013).

an action might diminish the plaintiff's ability to command top dollar on a future mineral lease.

Article 206 specifies that the obligation applies to former owners and former owners only, as does the liability for the resultant damages stated in article 207. Parties who never owned a mineral right can severely impact the marketability of landowners' property or cause them to incur substantial fees to clear their titles, but such parties are not implicated by the strict language of articles 206 or 207. Louisiana courts have previously construed articles 206 and 207 in this stringent manner. For example, in *Adams v. JPD Energy*, the Second Circuit denied attorneys' fees to a landowner who successfully had a lease declared null.¹²⁰ Because the lease was deemed to have never existed, it was not an extinguished mineral right, and the defendant was not a former mineral owner.¹²¹

The *Adams* holding probably belies the intent behind articles 206 and 207: it potentially imposes harsher penalties on good-faith former operators than on bad-faith parties with no connection to the property. It is likely that the legislature intended to cast a wider net, one that would catch parties whose actions clouded the public records, like the defendant in *Adams*. That defendant was eventually determined to not be a "former owner" but *appeared* to be the record owner of a lease for all purposes at the time of the demand by the landowner. The defendant's failure to furnish an act meant that the public records continued to incorrectly show that the landowner's minerals were out of commerce.¹²²

Similarly, a sublessee who does not provide the requested act has a recorded interest indicating continued rights in the landowner's property, clearly clouding the title of the landowner and reducing the marketability of his rights. The former sublessee might claim that his interest is entirely dependent on the prime lease, such that potential lessees will be concerned only with the actions of the lessee and sublessor. This argument appears persuasive at first glance and mirrors the reason why a former ORRI holder does not truly cloud title. It is, however, flawed as a practical matter. The sublease and assignment distinction is so murky that Louisiana's circuit courts cannot even remain internally consistent about

120. *Adams v. JPD Energy, Inc.*, 87 So. 3d 161, 164 (La. Ct. App.), *writ denied*, 89 So. 3d 1194 (La. 2012). Full disclosure: the author's law firm represented the landowner in this case. However, the case predates the author's employment with the firm.

121. *Id.*

122. Keeping property in commerce is, indeed, a public policy of this state. *Lumber Products, Inc. v. Crochet*, 156 So. 2d 438, 443 (La. 1963). The author would be remiss if he failed to acknowledge that Grant E. Summers made the *Adams* (87 So. 3d 161) policy arguments earlier and better.

the proper characterization of a given type of transfer.¹²³ Louisiana law should not demand that lay landowners and potential lessees answer a question that most courts apparently cannot, simply to determine if there is a competing ownership claim.

It is not apparent that the *Adams* or sublessee arguments hold for a former mortgagee of a former lessee, whose only claimed interest was a conditional one, never exercised. Though Wells Fargo's mortgage was a matter of public record, it is unlikely that this would have dissuaded any potential lessees from leasing the Gloria's Ranch property without an act of extinction in the *conveyance* records from Wells Fargo. Industry participants understand the accessory nature of a mortgagee's interest. The trial court in *Gloria's Ranch* accepted fact testimony to the contrary in that case, a finding affirmed by the Second Circuit.¹²⁴ But since both courts erroneously found that Wells Fargo was a "former owner" of the lease itself, this factual question was actually irrelevant to the holding.

There is no question that non-owners can cloud title to a landowner's mineral rights, like the defendant in *Adams*, the hypothetical foreclosing mortgagee sketched out above, or a former sublessee. If the Louisiana Legislature intended to include these sorts of parties as obligors under article 206, using "former owner" was poor statutory drafting. To be more lucid about the legislative intent, the statute should have singled out both "former owners" and "parties who have a record *claim* of ownership" of a mineral right. Under this formulation, a landowner would have recourse against both true former owners and parties who have made an affirmative assertion that they are owners. Purely passive former mortgagees like Wells Fargo, whose only record interest was one that is universally recognized as accessory in nature, would remain protected. Though none is likely forthcoming, a revision to the statutes is in order to give effect to the legislature's probable original intent.

D. The Implications of the Gloria's Ranch Mortgagee Liability Holding

Though it is unlikely that the consequences to oil and gas financing would be as apocalyptic as predicted by Justice Bleich, there probably *would* be severe consequences if the Supreme Court declined to overturn the Second Circuit on this point. Neutral observers have already predicted

123. See Ottinger, *supra* note 45, at 331 (discussing the Third Circuit's conflicting opinions in *Cameron Meadows Land Company v. Bullard*, 348 So. 2d 193 (La. Ct. App. 1977) and *Dore Energy Corporation v. Carter-Langham, Inc.*, 997 So. 2d 826 (La. Ct. App. 2008)).

124. *Gloria's Ranch*, 223 So. 3d at 1224: "Jaratt asserted Wells Fargo's interests in the lease would create red flags for potential lessees."

a chilling effect on the flow of financing to oil and gas companies.¹²⁵ Though surely many lenders who saw the potential for returns would continue providing capital to operators, the possibility of major liability would encourage them to lend less and on less favorable terms. This throttling of capital would hurt lessees, but it would be detrimental to lessors as well, whose mineral rights would become far less valuable as fewer market participants had less money to bid against each other. If the *Gloria's Ranch* opinion was right on mortgagee liability, these policy considerations would be a clarion call for legislative action, rather than factors for the courts to weigh. The decision was *not* correct on this point, and the potentially severe consequences should be reason enough for the Supreme Court to take up the issue.

Furthermore, the mortgagee liability holding creates more legal questions than it answers. For instance, if the mortgagee is a “former owner” of a mineral right, then it would obviously have been a “present owner” of the lease at some point. That entails that *Gloria's Ranch* itself actually had statutory obligations to Wells Fargo during the pendency of its mineral right, pursuant to the correlative rights doctrine.¹²⁶ It further means that the plaintiffs also apparently owed contractual duties to Wells Fargo under the lease, as a synallagmatic contract.¹²⁷ What lease rights could Wells Fargo have enforced against *Gloria's Ranch* during the life of the lease? There is no obvious answer, casting more doubt on the Second Circuit's determination.

IV. SOLIDARITY OF THE OBLIGATION

A. Co-Lessee Liability

As detailed above, holding Wells Fargo liable at all was clear error. As detailed below, implicitly finding that EXCO breached its article 206 obligation may have been error. But on the issue of the solidarity of Cubic and Tauren's obligation, the Second Circuit got it right; those two

125. See Tyler L. Weidlich, *Lender Beware: Lender Held Liable for Borrower's Failure to Release Mineral Lease*, A.B.A. (Sept. 22, 2017), <https://perma.cc/SAV9-U2UP>; Tom Arceneaux, BLANCHARD, WALKER, O'QUIN & ROBERTS, <https://perma.cc/24PD-YL5S> (last visited Jan. 5, 2018).

126. See LA. REV. STAT. § 31:11 (2006), which states that “The owner of land burdened by a mineral right or rights and the owner of a mineral right must exercise their respective rights with reasonable regard for those of the other. Similarly the owners of separate mineral rights in the same land must exercise their respective rights with reasonable regard for the rights of other owners.”

127. LA. CIV. CODE art. 2668 (2017).

companies owed the same obligation (providing the Article 206 instrument in response to demand) and the same damages for a failure to perform that obligation. These defendants argued that their damages should have been reduced proportionately to each defendant's share of the Lease after the various assignments, an argument wisely rejected by the courts.

Still, the Second Circuit took the wrong path to this correct result. The appellate panel's misstep on the solidarity of the liability between the defendants was founded on the incorrect premise that "ownership of a mineral right, such as a mineral lease, is indivisible."¹²⁸ As putative support, the court cited to article 168, which actually states that "[m]ineral rights are *susceptible* of ownership in indivision."¹²⁹ However, mineral rights are also susceptible of division, along many possible lines. Though it is not divisible by a partial assignment or partial sublease, a mineral lease can be divided if the lease contains an "assignability clause" and the assignor assigns all of his interest in a portion of the lease.¹³⁰ This division operates to divide the obligations due under the lease. The proper conception is of two separate leases, each with a distinct set of obligations due to the lessor.¹³¹ If the assignor of a divided lease breaches one of his lease obligations, the assignee will not be held liable.¹³² Similarly, the assignor and assignee must independently maintain their respective lease interests by separate production or operations after the primary term.¹³³ It naturally follows from the "two new leases" picture that a lessee of a divided lease can only be liable for damages caused by his own failure to perform.

The divisibility of leases, under certain circumstances, is not in any doubt in Louisiana.¹³⁴ The Second Circuit should not have suggested otherwise. But the court was correct in rejecting the oil company defendants' claims that

128. *Gloria's Ranch*, 223 So. 3d at 1219.

129. LA. REV. STAT. § 31:168 (1975) (emphasis added).

130. LA. REV. STAT. § 31:130 (1975) & Comment; *Roberson v. Pioneer Gas Co.*, 137 So. 46 (La. 1931).

131. *Id.* at 48.

132. *Roberson*, 137 So. 46; *Tyson v. Surf Oil Co.*, 196 So. 336, 344 (La. 1940).

133. *Davidson & Martin*, *supra* note 111, at 15-17; *Roberson*, 137 So. 46.

134. However, a recent Second Circuit decision, *Guy v. Empress*, 193 So. 3d 177 (La. Ct. App. 2016), effectively determined that a lease cannot be divided horizontally; that is, by an assignment of certain depths. This appears to be an inconsistent application of the lease division doctrine, for the reasons discussed in *Davidson & Martin*, *supra* note 111, at 9-13. However, it will likely be treated as controlling by subsequent courts, at least in the Second Circuit. By the logic of *Guy*, none of the depth assignments in *Gloria's Ranch* could have divided the lease.

their liability for damages should be reduced because of the various assignments of their lease interests. The “assignments” at issue did not divide the lease in the manner argued for by the defendants. Tauren took the lease in 2004 and assigned an undivided forty-nine percent of it to Cubic in 2006.¹³⁵ This “assignment” did not serve to divide the lease because, as a fractional assignment, it was not a transfer of *all* of Tauren’s interest in any part of the Lease.¹³⁶ Whether this was better deemed a partial assignment or a partial sublease, article 130 unambiguously declares that either cannot divide a lease.¹³⁷ After the transfer, Cubic and Tauren shared all lease obligations and could benefit from any actions of the other that satisfied such obligations or met lease conditions. The Lease was not divided at that point, and so each owed the same performance—their obligation was solidary.

B. Division of the Liability Across Depths

In late 2009, Tauren assigned all of its interest in the deep rights to EXCO. On its face, this may suggest a division between upper and lower depths, at least with regard to Tauren’s interest, as that company had then divested itself of all deep rights interest. However, Cubic’s forty-nine percent interest stretched across both the shallow and deep rights. As a result, production or operations on the lower depths would have served to maintain the Lease as a whole, indicating that there was no division of lease obligations, benefits, or conditions. Again, because there was no true division of the lease, each party who owed an obligation to provide the act evidencing extinguishment of the Lease owed the same performance.

Even if there were, in effect, separate leases on the shallow and deep rights after the transaction with EXCO, and further, if Tauren could not be held liable for any failure to perform as to the deep rights, the extent of liability would not change. The obligation is to provide a recordable act of extinction, and it applies to *all* former owners of a mineral right. Cubic and Tauren both qualify as former owners of the lease, and both count as

135. *Gloria’s Ranch*, 223 So. 3d at 1207.

136. Again, under the reasoning of *Guy*, 193 So. 3d 177, even a transfer of 100% of Tauren’s deep interest would not have served to divide the lease.

137. The author has previously argued that a sublease can, in theory, divide a mineral lease—but only under a highly specific set of facts. See Davidson & Martin, *supra* note 111, at 6-8, 29. *Johnson v. Moody*, 123 So. 330 (La. 1929). Under the reasoning of *Hoover Tree Farm*, 63 So. 3d 159, the Cubic-Tauren transaction would not be a true sublease, as there is no indication of a new lease “engrafted” on the original.

former owners of both the shallow and deep rights.¹³⁸ Even though Tauren may not have held any deep rights after the EXCO assignment, it was still obliged to provide the recordable act upon demand as a former owner. Nothing in the language of article 206 suggests that this obligation is meant to only apply to the most recent former owner of a mineral right. Louisiana is home to some truly ancient leases, some of which were assigned in whole a century ago.¹³⁹ The language of article 206 entails that, if a demand is made on him, an assignor from 100 years ago is obliged to provide the recordable act evidencing extinguishment. Simply put, as former owners, Cubic and Tauren owed the same performance: they were equally required to furnish the act declaring that they no longer held any interest in any portion of the Lease, deep or shallow.

Furthermore, even if the obligations were different (a separate obligation for each interest), Tauren and Cubic would be liable for the full amount of damages. Article 207 states that a party who does not comply with its article 206 obligation is liable for all damages caused by that failure.¹⁴⁰ When it comes to lost leasing opportunities because of an article 206 failure of multiple fractional lessees, it is impossible to realistically distinguish the extent of the harm suffered because of each lessee's non-performance. The cloud on the title caused by having "only" forty-nine percent of the rights tied up in a dispute will discourage potential new leasing activity roughly equal to having the entire lease so encumbered. It is just not the case that Gloria's Ranch could have received forty-nine percent of the calculated lost leasing opportunity money had Cubic acknowledged extinction but Tauren did not.

C. Date of Extinction of Mineral Right and Solidarity

The trial court reduced (and the Second Circuit affirmed) the damages due by the remaining defendants by twenty-five percent, representing EXCO's virile share thereof.¹⁴¹ This reduction suggests that the court decided that EXCO was, in fact, a former co-owner of the lease. Such a fact is far from clear, even apart from the sublease/assignment problem, because of the absence of discussion about when the Lease actually expired.

138. Unless, perhaps, if Cubic were merely a sublessee of Tauren. *See* discussion *supra* Part IV. B. 2.

139. *See* *Regions Bank v. Questar Expl. & Prod. Corp.*, 184 So. 3d 260, 261-62 (La. Ct. App. 2016), dealing with mineral leases executed in 1907.

140. LA. REV. STAT. § 31:207 (1982).

141. *Gloria's Ranch*, 223 So. 3d at 1215, 1224 n.19.

The plaintiff's claim in its petition was that the lease had expired at some point before suit for the failure to produce in paying quantities.¹⁴² The EXCO assignment did not occur until November 9, 2009.¹⁴³ If the lease expired prior to that date, EXCO never actually acquired an interest in anything.¹⁴⁴ Therefore, it appears that the courts implicitly determined that EXCO did in fact acquire an interest in the lease and that the lease subsequently expired at some point between November 10 and December 31, 2009. Neither court explicitly specified any date of lease expiration. The court did appear to use the eighteen month period prior to January 28, 2010 as the appropriate span to consider in the paying quantities analysis, but it did not give any reasons for selecting this total duration, as opposed to a shorter one.¹⁴⁵ Nor did the court explain why the date of the demand was the proper endpoint to work backwards from, rather than some earlier date in the secondary term. This lack of explanation may indicate that the Second Circuit did not even consider the issue. If EXCO never was an owner, it could not have been a solidary obligor, and no reduction for EXCO's settlement was warranted.

Determining the day of a mineral right's death with some degree of precision is crucial. Selecting an exact date will clearly be, to a large degree, a legal fiction. This is especially true in the lease context, where there are no rules dictating the appropriate span to consider in determining whether the right has been maintained.¹⁴⁶ In cases like *Gloria's Ranch*, where millions of dollars are at stake in the resolution of the question, it is a *necessary* legal fiction. Courts and litigants need to employ a more fine-grained approach to the issue.

142. Petition, *Gloria's Ranch*, 223 So. 3d 1202, ¶ 6:

The Lease or, alternatively, a portion of the Lease, has expired for a lack of production in paying quantities.

143. *Gloria's Ranch*, 223 So. 3d at 1208.

144. *Id.* at 1209.

145. The Second Circuit noted that Louisiana courts generally use a 12-month to 18-month period to evaluate whether or not a well is producing in paying quantities. *Id.* at 1211. Like every other Louisiana court that has dealt with the issue, it did not explain what factual conditions made the actual period selected appropriate under the circumstances.

146. *See id.* The requisite suspension of disbelief as to the exact date a mineral royalty or mineral servitude expired is less dramatic given that both rights have a hard ten year prescriptive period of non-use. *See* LA. REV. STAT. §§ 31:27, 31:85 (1975).

CONCLUSION

The Second Circuit's opinion in *Gloria's Ranch* traversed a wide field of complex legal issues, many of which were not discussed herein. Its determinations regarding the standards for a "paying quantities" analysis and on damages for failure to properly pay royalties were well stated and unquestionably correct. Other courts should look to the opinion on these conclusions. Courts can and should also learn from the Second Circuit's discussion of the article 206 obligation. This facet of the opinion should serve as a reminder that it is essential to begin with the most basic questions about the mineral rights (or purported mineral rights) at issue in a given case, such being:

- (1) What is the alleged mineral right?
- (2) What are the characteristics of ownership for that mineral right?
- (3) Does the party in question own the mineral right, or an interest in the mineral right?
- (4) Was the mineral right itself actually co-owned?
- (5) When did the mineral right expire?
- (6) How did the mineral right expire?

Riding on the proper resolution of these questions is something greater than the enormous sums of money at stake in cases like *Gloria's Ranch*: the coherent development of Louisiana's mineral law. Eventually, an appellate court will have to address some of the unanswered questions related to article 206 identified herein. To steer the jurisprudence in the right direction and avoid another dubious revolution, that court will need to work from the bottom up, piece by piece, by carefully identifying the rights and remedies available to each party.