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Demystifying Louisiana Revised Statutes § 30:10

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Demystifying Louisiana Revised Statutes § 30:10

Patrick S. Ottinger[*]

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INTRODUCTION[1]

There is arguably no single section of the Louisiana Conservation Act[2] that is of greater significance to an oil and gas operator, as well as other unit participants who have cost liability, than Section 10 of Title 30 of the Revised Statutes.[3] This important statutory provision addresses the allocation of cost-bearing responsibility among owners of interests in a compulsory unit[4] in the absence of a contract or other agreement between the parties.

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1. Portions of this Article represent an adaptation of prior articles or other publications by this author, principally including: Patrick S. Ottinger, *From the Courts to the Code: The Origin and Development of the Law of Louisiana on Mineral Rights*, 1 LSU J. OF ENERGY L. & RES. 5 (2012) [hereinafter Ottinger, *From the Courts to the Code*]; Patrick S. Ottinger, *It's a Risky Business, but There's an Act for That: The Louisiana Risk Fee Act*, 63 ANN. INST. ON MIN. L. 61 (2016) [hereinafter Ottinger, *It's a Risky Business*]; and Patrick S. Ottinger, *The "Free Rider" in Louisiana—the "Louisiana Risk Fee Act,"* THE PIPELINE (Aug. 14, 2022), https://thepipeline742032307.wordpress.com/2022/08/14/the-free-rider-in-louisiana-the-louisiana-risk-fee-act/ [https://perma.cc/JVG8-SE4Y] [hereinafter Ottinger, *The "Free Rider" in Louisiana—the "Louisiana Risk Fee Act"*]. Other material is drawn from PATRICK S. OTTINGER, LOUISIANA MINERAL LEASES: A TREATISE (2016) [hereinafter OTTINGER, MINERAL LEASE TREATISE].

2. Act No. 157, 1940 La. Acts 610 (now codified in LA. REV. STAT. ANN. §§ 30:1–101.15 (2023)). Over the years since its adoption in 1940, the Louisiana legislature had added many disparate provisions to Title 30, not all of which are conservation-related, properly speaking. Technically, the Conservation Act is composed of Chapter One, Parts I through VIII of Title 30, being sections 1 through 101.15. All subsequent sections, albeit reposing within Title 30, are not technically speaking a part of the Conservation Act, as originally adopted and thereafter from time to time amended.

3. For ease of reference, this statutory section in its entirety is herein referred to as "Section 10," with specific references to distinct subsections as necessary.

4. "A unit formed by order of a governmental agency is termed a 'compulsory unit.'" LA. REV. STAT. ANN. § 31:213(6) (2015). There are five kinds of compulsory unit, *viz.*, a "drilling and production" unit, *id.* § 30:9; a "fieldwide" or "reservoirwide" unit (sometimes called a "441 unit," being a reference to Act No. 441 of 1960), *id.* § 30:5C; a "deep pool" unit, *id.* § 30:5.1A; an "ultra deep structure" unit, *id.* § 30:5.1B; and a "[c]oal seam natural gas producing" unit, *id.* § 30:5.2. However, except as next noted, the provisions of Section 10 pertain expressly only to a "drilling unit which has been established by the commissioner as provided in R.S. 30:9(B)." *Id.* § 30:10A. Additionally, it is distinctly provided that "provisions of R.S. 30:10(A)(2) shall be applicable to ultra deep structure units, including the applicable risk charge." *Id.* § 30:5.1B(9).

If it is not rare, the drilling of a unit well on a heads up basis is certainly an exception to the general rule of multi-party development and operation.[5] Rather, there can be a variety of cost-responsible participants in a compulsory unit in addition to the operator, including lessees with whom the operator has no contractual relationship as well as unleased landowners or unleased mineral servitude owners.

This Article undertakes to explain and examine, and in so doing, to demystify, these critical statutory provisions.[6] As will be shown, due primarily to legislative add-ons or revisions over the years since 1940, the Section is currently composed of several dissimilar provisions stitched together in somewhat of a haphazard fashion.[7]

Part I of this Article examines the rule of capture and the abuses resulting from its unfettered exercise. Part II discusses the national movement toward the adoption of measures by oil and gas producing states to conserve the valuable natural resources of oil and gas in order to address these abuses. Part III looks at Louisiana's adoption of the Conservation Act in 1940, including an examination of the regulatory tools assigned to the Office of Conservation to prevent waste and effectuate conservation of minerals, including particularly oil and gas. The current formulation of Section 10, one of the critical components of our conservation statute, is studied in Part V.[8]

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5. A well is said to be drilled on a "heads up" basis when it is drilled at the sole cost, risk, and expense of the participating parties (proportionately to the interest of each) without contribution by another other person. *See* Richard T. McMillan, *Obtaining Equity Capital for Drilling Operations: The Securities Aspect*, MIN. FIN. 6-1, 6-16 (1982) ("This structure has obvious sales appeal in that there is no promotion on subsequent wells, but rather the general partner and limited partners are participating on a 'heads up' (equal) basis.").

6. *Demystify*: "[T]o make something easier to understand." *Demystify*, CAMBRIDGE DICTIONARY, https://dictionary.cambridge.org/dictionary/english/demystify [https://perma.cc/HE4F-U9TS] (last visited Feb. 25, 2023). *Author*: "Absolutely no pressure there."

7. That Section 10 is composed of many "moving parts" was tacitly acknowledged by the United States Court of Appeals for the Fifth Circuit when it reviewed various aspects of such section and then stated, "The foregoing is intended merely as a generalized summary of the principal provisions of LSA–R.S. 30:9 and 10, and, among other things, does not purport to encompass all the details of those provisions or the various exceptions and qualifications thereto, none of which are relevant for present purposes." Trahan v. Superior Oil Co., 700 F.2d 1004, 1014 n.14 (5th Cir. 1983).

8. When Act No. 157 of 1940 was adopted, the Conservation Act thus enacted was composed of 19 sequential and substantive sections. In 1950, that original text was amended by Act No. 100, 1950 La. Acts 100 so as to add to the

I. THE RULE OF CAPTURE

As will be demonstrated, Section 10, as a part of the Conservation Act, was enacted as one of several important statutory provisions to address the abuses and inefficiencies arising out of the unfettered exercise of the rule of capture. Critical to that early conservation legislation were a few regulatory tools, including well spacing, prevention of waste, and unitization. This regulatory scheme constitutes the context in which Section 10 operates to regulate or allocate costs for the drilling of a unit well.

A. Preface

Oil and gas exist in their natural state embedded in subsurface rock formations called *pools*.[9] By its very nature, a *pool* may underlie one or more distinct surface tracts with differing owners. Thus, a well drilled on one surface tract and completed in a particular subsurface pool thereunder may permit the recovery of hydrocarbons which in reality are drawn from under an adjacent tract or other surface tracts underlain by the same pool.[10]

Conservation Act a new Section 1 (essentially, but not identically, as it currently exists), and the original sections 1–19 were renumbered accordingly, each increasing numerically by 1, so as to thus be reconstituted as §§ 30:1–20. Thus, the statutory provisions now contained within Section 10 originally reposed in section 9 of the 1940 legislative act. As noted in note 2 *supra*, the Conservation Act, properly so called, constitutes Chapter One of Title 30, currently composed of §§ 30:1–101.15.

9. According to LA. REV. STAT. ANN. § 30:3(10) (2022):

> "Pool" means an under–ground reservoir containing a common accumulation of crude petroleum oil or natural gas or both. Each zone of a general structure which is completely separated from any other zone in the structure is covered by the term "pool" as used in this Chapter. However, to promote the development and production of marginally commercial sands, a zone may contain one or more common accumulations and the overall stratigraphic interval of the zone may be considered and treated as a pool for all purposes of this Chapter.

A functionally similar, albeit not identical, definition is contained in article 213(3), Louisiana Mineral Code.

10. Corbello v. Sutton, 442 So. 2d 610, 614 (La. Ct. App. 1st Cir. 1983) ("To prevent an abuse of the rule of capture and wasteful drilling, Louisiana adopted the concept of forced or compulsory pooling. This concept requires that all persons in the 'pool' of gas, oil or other fugacious minerals share in its production." (internal citation omitted)).

The Louisiana law of property distinguishes between *products* and *fruits*. Oil and gas as produced are *products*, not *fruits*, because production of these minerals diminishes the resource. Oil and gas do not replenish like fruits such as corn, soybeans, sugar cane, etc.[11] "Products derived from a thing as a result of diminution of its substance belong to the owner of that thing. When they are reclaimed by the owner, a possessor in good faith has the right to reimbursement of his expenses."[12]

Because of the physical nature of oil and gas—as distinguished from what are termed "solid minerals" such as sulphur, coal, or lignite—such products are said to be *migratory* or *fugacious*.[13] The landowner owns the right to migratory minerals underlying its land but does not own such minerals in physical form until they are produced and brought to the surface of the earth.[14] In contrast, "[o]wnership of land includes all minerals occurring naturally in a solid state. Solid minerals are insusceptible of ownership apart from the land until reduced to possession."[15] This is a foundational principle pertinent to the ownership of the rights to minerals held by a landowner.

In the significant case of *Frost-Johnson Lumber Co. v. Salling's Heirs.*,[16] the Louisiana Supreme Court acknowledged the fugacious character of oil and gas. On second rehearing, the Court, in large part due to the migratory nature of oil and gas, held that such products are not susceptible of ownership separate and apart from the land under which they might be found.[17] Rather, one may only own a *servitude* which permits its owner to enter upon designated land and conduct drilling

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11. Comment (c) to Louisiana Civil Code article 551 instructs that "[m]ineral substances extracted from the ground and the proceeds of mineral rights are not fruits, because their production results in depletion of the property." LA. CIV. CODE ANN. art. 551 cmt. c (2019).

12. *Id.* art. 488 (in part).

13. Nunez v. Wainoco Oil and Gas Co., 488 So. 2d 955 (La. 1986).

14. LA. REV. STAT. ANN. § 31:6 (2022):

> Ownership of land does not include ownership of oil, gas, and other minerals occurring naturally in liquid or gaseous form, or of any elements or compounds in solution, emulsion, or association with such minerals. The landowner has the exclusive right to explore and develop his property for the production of such minerals and to reduce them to possession and ownership.

15. *Id.* § 31:5.

16. Frost-Johnson Lumber Co. v. Salling's Heirs, 91 So. 207 (La. 1922).

17. *Id.* at 242.

operations thereon and to reduce oil or gas to possession and, hence, ownership.[18]

B. Rule of Capture

In Louisiana, the *rule of capture* has historically applied in connection with the production of oil and gas.[19] This foundational principle stands for the proposition that a landowner is privileged to use reasonable methods to produce migratory hydrocarbon minerals from under the landowner's own property and to thereby become the owner of such minerals when they arrive at the surface of the earth. Then, the oil and gas are said to be "reduced to possession,"[20] without any liability to adjacent property owners even though the minerals so produced might have in fact been drawn from under the adjacent owner's property.

The essential import of the rule of capture was summarized in a significant case on the remedy for drainage as follows:

> As we view the matter, a landowner has no right to prevent the owner of a neighboring tract from drilling on his own property and reducing to possession the fugitive minerals which he may find. The remedy which the first landowner has in such a case is either (1) to drill offset wells on his own property in order that he also may capture and retain a portion of the minerals before the common reservoir is depleted, or (2) he may attempt to have a

18. "A mineral servitude is the right of enjoyment of land belonging to another for the purpose of exploring for and producing minerals and reducing them to possession and ownership." LA. REV. STAT. ANN. § 31:21 (2022). *See* Patrick S. Ottinger, *A Primer on the Mineral Servitude*, 44 ANN. INST. ON MIN. L. 68 (1997); *See* PATRICK S. OTTINGER, MINERAL SERVITUDES, *in* LOUISIANA MINERAL LAW TREATISE ch. 4 (Patrick H. Martin ed. 2012); Patrick S. Ottinger, *All Good Things Must Come to an End: The Launch, Life and Loss of a Mineral Servitude*, 81 LA. L. REV. 1130 (2021).

19. La. Gas & Fuel Co. v. White Bros., 103 So. 23 (La. 1925); McCoy v. Ark. Nat. Gas Co., 143 So. 383 (La. 1932).

20. "Minerals are reduced to possession when they are under physical control that permits delivery to another." LA. REV. STAT. ANN. § 31:7 (2022). The phrase "reduced to possession" as appears in article 7 is a concept articulated by the Louisiana Supreme Court in the early case of *Rives v. Gulf Referee Company of Louisiana*, 62 So. 623, 626 (La. 1913), in which the court stated that "the owner of the soil has the exclusive right to reduce to possession the deposits of natural gas and oil found beneath the surface of his land." This important notion of "reducing [minerals] to possession" is embedded in six articles of the Mineral Code, *viz.*, articles 5, 6, 7, 8, 15, and 21.

> pooling or production unit created in order that he may share in the production from the neighboring well.[21]

Hence, it has been noted that "[t]he owner of a tract of land acquires title to the oil or gas which he produces from wells drilled thereon, though it may be proved that part of such oil or gas migrated from adjoining lands."[22]

"Under this rule [of capture] an owner has the right to conduct exploratory operations on his property and reduce the conquest to ownership. In so doing, no liability attaches to his actions should minerals acquired be drained from beneath the land of another mineral owner."[23]

"Under Louisiana's so-called 'rule of capture' a landowner is not the owner of minerals beneath the surface of his lands, but rather has only the right to search for and draw minerals through the soil and thereby become the owner thereof."[24] Article 14 of the Louisiana Mineral Code now codifies the rule of capture by providing that a "landowner has no right against another who causes drainage of liquid or gaseous minerals from beneath his property if the drainage results from drilling or mining operations on other lands."[25] This impunity from liability to a neighbor is an essential precept of the rule of capture.

Most recently, the United States Court of Appeals for the Fifth Circuit had occasion to explain the rule of capture as follows:

> Although Spindletop is an extreme example, similar wasteful over–production was once common. A cause was the "rule of capture," the common law doctrine initially used in hunting disputes to determine ownership of wild animals unconstrained by property borders. Taught during the first days of law school, the doctrine says if you catch it first, it is yours. Courts later applied

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21. Breaux v. Pan Am. Petroleum Corp., 163 So. 2d 406, 415 (La. Ct. App. 3d Cir. 1964). *See* OTTINGER, MINERAL LEASE TREATISE, *supra* note 1, § 3-13(e)(6).

22. Robert E. Hardwicke, *The Rule of Capture and Its Implications as Applied to Oil and Gas*, 13 TEX. L. REV. 391, 393 (1935).

23. Knighton v. Texaco Producing, Inc., 762 F. Supp. 686, 689 (W.D. La. 1991).

24. Pierce v. GoldKing Props., Inc., 396 So. 2d 528, 533–34 (La. Ct. App. 3d Cir. 1981).

25. LA. REV. STAT. ANN. § 31:14 (2022). *See also id.* § 31:6; *id.* § 31:8 (A landowner may "reduce to possession and ownership all of the minerals occurring naturally in a liquid or gaseous state that can be obtained by operations on or beneath his land even though his operations may cause their migration from beneath the land of another.").

> the doctrine to oil and natural gas, reasoning that they too cross property borders as they seep and spill through crevices underground. In that context, the rule means a landowner has a property right in oil and gas produced from wells on the owner's land, whether or not it migrated from other lands. So, under the common law, one landowner could drain an entire reservoir through wells on the landowner's property, even if the reservoir extended under others' lands. Naturally, surrounding owners usually would not sit idly by while valuable resources drained out from under them; instead, they raced to produce all the oil and gas they could through their own property, often drilling multiple wells to extract resources as quickly as possible. At Spindletop and elsewhere, this drove up production costs, reduced oil and gas market prices, and unnecessarily decimated the environment.[26]

The foregoing elucidates the issues brought about by the rule of capture and sets the stage for legislative efforts to address it.

II. THE CONSERVATION MOVEMENT

The rule of capture prevailed in all oil and gas producing states. The common experiences of those states were consistent in viewing the principle as being very wasteful and contrary to good public policy. Hence, efforts were undertaken to address these issues via legislation at the state level.

A. Abuses Arising Out of Unfettered Exercise of the Rule of Capture

As the Pennsylvania Supreme Court previously noted, the necessary corollary of the rule of capture is that the adjacent landowner's remedy is to "go and do likewise."[27] This admonition led to innumerable wells being drilled without regard to efficient and reasonable drilling and spacing practices. In 1913, one year prior to the adoption of the Louisiana

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26. TDX Energy, LLC v. Chesapeake Operating, Inc., 857 F.3d 253, 256–57 (5th Cir. 2017) (internal citations omitted). In the interest of full disclosure, the Author was counsel for the defendant in this case.

27. Barnard v. Monongahela Nat. Gas Co., 65 A. 801, 802 (Pa. 1907); *see also* BRUCE M. KRAMER & PATRICK H. MARTIN, THE LAW OF POOLING AND UNITIZATION § 2.01 (3d ed. 2021) (stating that the interest holder's protection "is the right to drill offset wells that would intercept the hydrocarbons otherwise being drawn to the neighboring wells").

Conservation Act, the Eastern District of Louisiana articulated this proposition as follows:

> It can readily be seen that, without the power to regulate or control conditions in an oil field, the temptation to acquire quick riches might easily produce an intolerable situation in drilling indiscriminately upon any size or shape of tract, sufficient to permit derrick operations, resulting in waste and exhaustion of underground energy consisting of natural gas, etc., and ultimately restricting recovery, involving useless expenditures by operators and preventing some, if not all, from recovering their investments.[28]

Thus, the wasteful consequence of the unfettered application of the rule of capture was one of the most compelling factors motivating the conservation movement of the 1930s and 1940s. Indeed, early commentators recognized the impetus for the conservation movement as follows:

> Plethoric production leads either to a market flooded with low-priced crude or to storage above ground. The loss of volatile elements by evaporation and the threat of fire and lightning hazards to oil and gas make storage above ground a wasteful practice. On the other hand, the marketing of oil and gas as soon as it is obtained at the fast rate of production which is necessitated by the law of capture strains or breaks the price structure. The decline of market prices, regardless of cause, results in the abandonment of marginal wells, with consequent waste in underground reserves and losses in money investment for well equipment.
>
> It is readily understood, therefore, that unregulated production, with the consequent waste due to natural and artificial factors affecting the oil and gas industry, ultimately results in the destruction of vital reservoir energies, permanent loss of unrecovered oil and gas, destruction of the price market and the consequent depletion of irreplaceable natural resources. Thus, unregulated production causes great losses to the public, the producers, the royalty owners and all others interested in oil and gas production. It is not surprising, then, that the legislatures of

28. Lilly v. Conservation Comm'r of La., 29 F. Supp. 892, 897 (E.D. La. 1939).

the various states have resorted to the police power for a remedy.[29]

A respected federal jurist explained the early Louisiana experience as follows:

> If Louisiana had adopted the rule in an unmodified form, an owner could have drilled as many wells on his land as he cared to drill. To avoid actual or perceived drainage, however, his neighbor could have drilled as many retaliatory wells as he deemed necessary. Soon, an oil field could have become so populated with wells that a pedestrian could have traversed the entire area by walking from drilling platform to drilling platform, his feet never touching the ground.
>
> Society would not tolerate the unbridled lust for oil and gas to dissipate a natural resource. The property owner's unlimited right to explore had to be curtailed in the name of conservation. Thus, exercising its police power to prevent waste, the Louisiana Legislature passed conservation measures that were, and are, administered by the Department of Conservation, headed by a Commissioner of Conservation.[30]

The foregoing observations and experiences set the landscape for Louisiana's adoption of its Conservation Act.

B. Early Conservation Legislation in Louisiana

From the earliest days of the oil and gas industry in Louisiana,[31] the Louisiana legislature would, from time to time, adopt incremental measures to address or respond to particular events or circumstances arising in the nascent stages of the petroleum industry.[32] In 1905, the

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29. R. Nolan Moosa & Kaliste J. Saloom, Jr., *The Oil and Gas Conservation Movement in Louisiana*, 16 TUL. L. REV. 199, 202–03 (1942).

30. Knighton v. Texaco Producing, Inc., 762 F. Supp. 686, 689 (W.D. La. 1991).

31. On September 21, 1901, the first commercially successful oil well in Louisiana, the Jules Clement No. 1, was successfully completed in a rice field on the "Mamou Prairie" in the community of Evangeline near Jennings, Louisiana. *See* Ottinger, *From the Courts to the Code*, *supra* note 1, at 7–11. See also *Jennings-Heywood Oil Syndicate v. Houssiere-Latreille Oil Co.*, 44 So. 481 (La. 1907), for an interesting exposition on these early ventures.

32. The history of the Louisiana Office of Conservation is discussed at *History*, STATE OF LA. DEP'T OF NAT. RES., http://www.dnr.louisiana.gov/

Savage-Morrical Well in the Caddo Field of Caddo Parish *blew-out*,[33] resulting in a conflagration which became a notorious event in the early history of conservation efforts in Louisiana. Two early commentators chronicled this blow-out in these terms:

> In North Louisiana, in 1905, two gas wells blew wild and caught fire, causing colossal physical waste. These conflagrations were the subject of notorious publicity which aroused public interest in the prevention of recurrences. As evidence of statewide anxiety, the first gas conservation law was enacted in Louisiana at the next session of the legislature.[34]

Thus, the Louisiana legislature enacted Act No. 71 of 1906.[35] That legislation was adopted "to provide for closing, capping or plugging of wild, uncontrollable or burning natural gas wells in this State or otherwise preventing the escape and waste of natural gas therefrom by the owners or proprietors thereof after due notice," among other things.[36]

The Louisiana Commission for the Conservation of Natural Resources was created in 1908.[37] Its purpose was to address general problems of conservation in Louisiana including inquiry into "prevention of waste in the extraction of oil, gas, and other minerals . . . ."[38]

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index.cfm/page/47 [https://perma.cc/W6CZ-KCUK] (last visited Feb. 25, 2023). Additionally, interesting and informative chronicling of the early legislative actions may be found in early published articles or treatises. *See*, *e.g*., Yandell Boatner, *Legal History of Conservation of Oil and Gas in Louisiana*, *in* LEGAL HISTORY OF CONSERVATION OF OIL AND GAS: A SYMPOSIUM 60 (1938); Moosa & Saloom, *supra* note 29; HARRIET SPILLER DAGGETT, MINERAL RIGHTS IN LOUISIANA § 98 (Rev. Ed. 1949); Brady Michael Banta, The Regulation and Conservation of Petroleum Resources in Louisiana, 1901–1940 (Volumes I and II) (1981) (Ph.D. dissertation, Louisiana State University) (on file with LSU Historical Dissertations and Theses, LSU Digital Commons). Portions of these historical expositions are adapted for inclusion here.

33. A *blow-out* is a "sudden, violent expulsion of oil, gas and MUD (*q.v.*) (and sometimes water) from a drilling well, followed by an uncontrolled flow from the well. It occurs when high pressure gas is encountered in the hole and sufficient precautions, such as increasing the weight of the mud, have not been taken." PATRICK H. MARTIN & BRUCE M. KRAMER, WILLIAMS & MEYERS: MANUAL OF OIL AND GAS TERMS 108 (18th ed. 2021).

34. Moosa & Saloom, *supra* note 29, at 207.

35. Act No. 71, 1906 La. Acts 11.

36. *Id.*

37. Act No. 144, 1908 La. Acts 200.

38. *Id.*

This commission was renamed in 1910 as the Conservation Commission.[39] Also enacted in 1910 was Act No. 190, which provided for the plugging of abandoned wells and making it unlawful for any person to permit the flow of gas to "escape into open air."[40] Additionally, Act No. 254 of 1910 established a Department of Mines and Minerals,[41] and Act No. 283 of 1910 amended and reenacted Sections 1 and 2 of Act No. 71 of 1906 so as to require any "owner or proprietor or person in possession" of a "wild, or uncontrollable, wasteful or wastefully burning natural gas well" to "close, cap or plug" such well, failing which, the Governor shall direct that work be undertaken to close such well "at the expense of the owner or proprietor thereof . . . ."[42]

Act No. 127 of 1912 reorganized the Conservation Commission, giving it authority to promulgate rules or regulations to protect state resources.[43] Some of the regulations established by Act No. 127 were to require the filing of drilling permits with maps of well locations, the use of surface casing and cement, and the plugging of abandoned wells. The Louisiana Department of Conservation was created in 1916 and came under the control of a single officer entitled the Commissioner of Conservation.[44] In 1918, the Louisiana legislature adopted Act No. 268, particularly directed to the prevention of the waste of natural gas.[45] Specifically, the statute made it unlawful to permit the waste of natural gas or to use gas in such a manner as would threaten the common source of supply with premature exhaustion. Act No. 133 of 1924 made it illegal to pollute the natural waterways of the state with salt water, oil, and other substances.[46] This Act was the first recorded incidence of environmental action taken on the oil industry by the legislature. The authority to establish allowables for the production of oil or gas so as to not exceed "reasonable market demand" was granted in Act No. 225 of 1934.[47]

That these discrete legislative efforts were adopted on a piecemeal, principally reactive basis was recognized in *Smith v. Holt*, wherein the Supreme Court noted that the "beginnings of legislative control in

39. Act No. 172, 1910 La. Acts 255.
40. Act No. 190, 1910 La. Acts 313.
41. Act No. 254, 1910 La. Acts 423.
42. Act No. 283, 1910 La. Acts 484.
43. Act No. 127, 1912 La. Acts 151.
44. Act No. 66, 1916 La. Acts 171.
45. Act No. 268, 1918 La. Acts 513.
46. Act No. 133, 1924 La. Acts 199.
47. Act No. 225, 1934 La. Acts 602.

Louisiana were piecemeal, each law giving recognition to some additional aspect of the importance of the industry to the State."[48]

In *Nunez v. Wainoco Oil & Gas Co.*, the Louisiana Supreme Court provided the following summary of the circumstances and events leading up to the 1940 adoption of the Conservation Act:

> A comprehensive statute modeled after New Mexico's law, regulated the spacing of wells and authorized compulsory pooling, in 1936. It failed, however, to adequately define "waste," and its general procedural articles were inadequate. Rather than amend the conservation measures piecemeal, the Legislature determined that a complete revision of existing legislation was needed. The result was 1940 La. Acts No. 157, which embodied the best features of the New Mexico law as well as the then recently enacted Arkansas law. Based on almost 50 years of legislative experience and judicial interpretations, this conservation statute was considered one of the best in the country. This act, as amended, constitutes Louisiana's basic conservation law with respect to the oil and gas industry.[49]

Thus, the Louisiana Conservation Act was enacted in 1940, granting to the Commissioner an array of powers and authorities to develop a sound program of conservation.[50] The Act enumerates the powers of the Commissioner relative to the regulation of the State's natural resources, vesting that officer with significant authority to regulate the oil and gas industry, including that authority to regulate aspects of drilling wells, well spacing, and unitization.

III. THE ENACTMENT OF THE CONSERVATION ACT

A. Preface

As noted, the Conservation Act regulates the oil and gas industry in Louisiana. The Commissioner of Conservation administers the provisions of the Conservation Act.[51] Appointed by the Governor,[52] this state officer has "jurisdiction and authority over all persons and property necessary to

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48. Smith v. Holt, 67 So. 2d 93, 95 (La. 1953).
49. Nunez v. Wainoco Oil & Gas Co., 488 So. 2d 955, 960–61 (La. 1986) (internal citation omitted).
50. Act No. 157, 1940 La. Acts 610. *See* discussion *supra* note 2.
51. LA. REV. STAT. ANN. § 30:1A (2022).
52. *Id.*

enforce effectively the provisions of this Chapter and all other laws relating to the conservation of oil or gas."[53] Certainly, so comprehensive and pervasive are the authorities of the Commissioner that courts have acknowledged that

> the orders of the Commissioner of Conservation supersede the contracts of the parties, are incorporated in the contracts of lease and govern the respective rights and obligations of the parties, and production from a force pooled unit operates as a substitute for performance of drilling obligations contained in a mineral lease.[54]

Among the many powers vested in the Commissioner of Conservation is the "authority to make . . . any reasonable rules, regulations, and orders that are necessary from time to time in the proper administration and enforcement of" the Conservation Act.[55]

The conservation laws of the Bayou State continue the rule of capture but regulate it by imposing reasonable restrictions in the exercise of the state's police power. The principal objectives of conservation legislation are preventing waste, avoiding the drilling of unnecessary wells, and affording each owner the opportunity to recover its just and equitable share of the common pool.[56] Indeed, at every public hearing before the Commissioner of Conservation in connection with the formation or revision of a compulsory unit,[57] testimony necessarily is offered by the applicant to establish certain predicate facts, i.e., that the formation of the proposed unit will promote conservation, prevent waste, and avoid the drilling of unnecessary wells; that the proposed unit will be economically and efficiently drained by one well; and that the proposed unit will afford the owner of each tract the opportunity to recover or receive its just and equitable share of the recoverable oil and gas in the unitized pool without unnecessary expense.[58]

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53. *Id.* § 30:4A.

54. Rebstock v. Birthright Oil & Gas Co., 406 So. 2d 636, 641 (La. Ct. App. 1st Cir. 1981). See also *Nunez v. Wainoco Oil & Gas Co.*, 488 So. 2d 955 (La. 1986), for a thorough analysis of the conservation laws and of the authority vested in the Commissioner of Conservation.

55. LA. REV. STAT. ANN. § 30:4C (2022).

56. *Id.* § 30:9A.

57. "No . . . order . . . shall, in the absence of an emergency, be made by the commissioner under the provisions of this Chapter except after a public hearing upon at least ten days' notice given in the manner and form prescribed by him." *Id.* § 30:6B.

58. This evidence is adduced to comport with the requirement that an order of an administrative agency must demonstrate the predicate findings of fact which

B. Judicial Challenge to the 1940 Conservation Legislation

The Louisiana Supreme Court responded to an immediate constitutional challenge in the important case of *Hunter Co., Inc. v. McHugh*, ultimately upholding the constitutionality of the Conservation Act.[59] The Court began its adjudication by observing that "Act No. 157 of 1940 is a statute which, in a very thorough and comprehensive way, regulates the conservation of the oil and gas resources of the state."[60]

The trial court found the statute to be unconstitutional for two reasons: (1) the statute impermissibly delegates to the executive branch (the Commissioner of Conservation) "the legislative power to adopt rules and regulations pertaining to drilling units, without a definite pattern or plan being first adopted and established by the Legislature";[61] and (2) the statute, "by attempting to authorize the Commissioner to compel the pooling of the interests of two or more landowners or leaseholders into a drilling unit,"[62] deprives the landowner or leaseholder "of his property without due process of law, especially where he has drilled a producing well and has established a market for the gas which is being produced from the well."[63]

Concerning the first alleged basis of unconstitutionality—the impermissible delegation of legislative power to the executive department—the Supreme Court stated that the Department of Conservation was created in the Constitution, which states that the Commissioner of Conservation "shall have and exercise such authority and power as may be prescribed by law."[64] Furthermore, the contention

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authorize the administrative action. *See id.* § 49:977 (as redesignated from § 49:958 by Act No. 663, 2022 La. Acts) ("A final decision shall include findings of fact and conclusions of law. Findings of fact, if set forth in statutory language, shall be accompanied by a concise and explicit statement of the underlying facts supporting the findings."). However, it has been held that

> "[w]hile the administrative agency must articulate the basis for its decision, where the findings and reasons therefor are necessarily implicit in the record and the record readily yields substantial evidence to support the administrative determination, the administrative order is not invalid merely because of the agency's failure to make explicit its finding which was already self-evident."

Summers v. Sutton, 428 So. 2d 1121, 1128 (La. Ct. App. 1st Cir. 1983).

59. Hunter Co., Inc. v. McHugh, 11 So. 2d 495 (La. 1942).
60. *Id.* at 496.
61. *Id.* at 498.
62. *Id.*
63. *Id.*
64. *Id.* (emphasis omitted).

that "the Legislature failed to adopt a pattern or plan to control the commissioner in the establishing of drilling units, and failed to define a 'drilling unit'"[65] was answered by the fact that "the Legislature was as specific as it was possible to be in adopting the method, or the so-called pattern or plan, to be followed by the commissioner in establishing a drilling unit, and was as specific and definite as the Legislature could have been in defining a drilling unit."[66]

Moreover, the Court observed that the statute provides a remedy of judicial review, which the court saw as "sufficient protection against abuse of [the Commissioner's] discretion . . . ."[67]

On the second alleged basis of unconstitutionality—the deprivation of property without due process—the Court noted that such contention had been rejected by the United States Supreme Court in *Ohio Oil Co. v. Indiana*,[68] where that Court "upheld the State's police power to regulate such rights . . . ."[69] Pursuant to this police power, the Court found the statute to be constitutional.[70]

Among other things, the Supreme Court addressed the plaintiff's contention that the Conservation Act was invalid because, among other challenges, it made "no provision . . . for collecting or enforcing" the operator's right of reimbursement of drilling costs.[71]

The Supreme Court rejected this contention by noting that

> The answer to this [contention] of course is that the [operator] has had and will have possession of all of the proceeds from the production of the well and may retain all of the proceeds until the drilling of the well and putting it on production is entirely paid for.[72]

C. Fundamental Precepts of Conservation Laws

The Conservation Act embodies a few fundamental precepts that are intended to regulate the rule of capture. These tools include well spacing, the assignment of allowables and proration of production, and pooling and unitization.

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65. *Id.* at 500.
66. *Id.*
67. *Id.* at 501.
68. *Id.* at 502 (citing Ohio Oil Co. v. Indiana, 177 U.S. 190 (1900)).
69. *Id.*
70. *Id.* at 506.
71. *Id.* at 509.
72. *Id.*

1. Well Spacing

One of the principal devices to regulate the rule of capture is the notion of well spacing, that is, the governmental regulation of the placement of wells, one from another, in such a way as to promote the goals of conservation legislation.[73]

Many of the older fields in Louisiana provide visual lessons demonstrating the prudence of a well-spacing program.[74] The existence of wooden derricks in the shadow of other such structures serves as a monument to the wisdom of the conservation movement in general and of well spacing in particular.

Included within the statutory grant of authority to the Office of Conservation is the power to "regulate the spacing of wells and to establish drilling units, including temporary or tentative spacing rules and drilling units in new fields."[75] Pursuant to this explicit grant of authority, the Commissioner of Conservation promulgated Statewide Order No. 29-E effective August 1, 1957.[76] As a general proposition, absent special rules which apply to certain designated fields (such special field rules being exceptions to the following general rules), no permit for drilling a well to a depth below 3,000 feet may be issued, unless the well is so located in compliance with the following offset distances from another well "completed in, drilling to, or for which a permit shall have been granted to drill to, the same pool[,]" to-wit:

OIL: No closer than 330 feet from a lease line or 900 feet.

GAS: No closer than 330 feet from a lease line or 2,000 feet.[77]

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73. LA. REV. STAT. ANN. § 30:4C(13) (2022). *See* PHILIP N. ASPRODITES, LOUISIANA MINERAL LAW TREATISE ch. 15 (Patrick H. Martin ed. 2012).

74. For historic photographs of the early Louisiana oil and gas activity, see Louisiana Geological Survey, *Jennings Field—the birthplace of Louisiana's Oil Industry—*, 9 PUB. INFO. SERIES (Sept. 2001), https://www.lsu.edu/lgs/publications/products/Free_publications/jennings-field.pdf [https://perma.cc/53DH-MYBT].

75. LA. REV. STAT. ANN. § 30:4C(13) (2022).

76. *See* LA. ADMIN. CODE tit. 43, pt. XIX, §§ 1901–1909 (2023) (Statewide Order No. 29-E).

77. *See* Statewide Order No. 29-E; LA. ADMIN. CODE tit. 43, pt. XIX, § 1905 (2023).

A well's location that complies with the spacing requirements of Statewide Order No. 29-E is said to be at a *legal location*.[78] It is often said that a well's location that does not comport with the strictures of Statewide Order No. 29-E is at an illegal location, terminology which is somewhat misleading as the word *illegal* normally is suggestive of criminality.[79] Such a well may be produced on a lease basis[80] upon issuance of an allowable by the Commissioner of Conservation.

In practice, the Commissioner of Conservation will issue a permit to drill a well,[81] even at a location which is not legal, but the permit to drill will be expressly conditioned upon the stipulation that no allowable to produce will be issued until the well is unitized or otherwise brought into compliance with Statewide Order No. 29-E.[82] Additionally, in a proper case, the Commissioner may grant an exception to the spacing requirements of Statewide Order No. 29-E in lieu of unitization.[83]

The prudent operator will obtain an escrow agreement from all parties who would participate in production if the producing well were producing on a lease basis. The escrow agreement should authorize the operator to produce the well prior to the issuance of the unit order, require the operator to escrow all proceeds of the sale or other disposition of production from the borehole in question, and to release such proceeds in accordance with the unit survey plat created in connection with the unit ultimately established by the Office of Conservation after issuance of the unit order. The failure of the operator to obtain such an escrow agreement while

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78. A *legal location* is defined in the regulations promulgated by the Commissioner as "any location which is in accordance with applicable special and statewide orders." *See* LA. ADMIN. CODE tit. 43, pt. XIX, § 2903 (2023) (Statewide Order No. 29-K-1).

79. This is not to say, however, that violations of conservation laws are immune from criminal prosecution. *See* LA. REV. STAT. ANN. § 30:18 (2022).

80. A *lease basis* well is a well that is not unitized. *See*, *e.g.*, Eads Operating Co. Inc. v. Thompson, 537 So. 2d 1187 (La. Ct. App. 1st Cir. 1988). "The Richard well was drilled on a non-unitized, lease basis in a geological stratum which correlated to the geological stratum of the 1948 unitized well known as the Miller No. 1 Zone." *Id.* at 1190. In the interest of full disclosure, this author represented the petitioner-operator in this suit.

81. "No well or test well may be drilled in search of minerals without first obtaining a permit from the commissioner of conservation . . . ." LA. REV. STAT. ANN. § 30:28A (2022).

82. *See* Exxon Corp. v. Thompson, 564 So. 2d 387, 388 (La. Ct. App. 1st Cir. 1990).

83. LA. ADMIN. CODE tit. 43, pt. XIX, § 1907 (2023).

producing the well prior to unitization can result in severe consequences, including having to pay double royalties.[84]

2. *Proration and Allowables for Oil Production*[85]

Also associated with the issue of well spacing is Statewide Order No. 29-H-1 governing the determination and setting of allowables for the production of oil[86] and gas.[87] The imposition of a program of allowables led to discipline in the commodity markets, resulting in greater stability in prices.

Act No. 225 of 1934[88] authorized the Commissioner of Conservation to impose a regime of proration by adopting rules and regulations "[t]o limit and prorate the production of oil or gas or both from any pool or field for the prevention of waste."[89] The imposition of a limit on the quantity of oil and gas that might be produced from a particular well constituted a drastic restriction on the exercise of rights under the rule of capture. Modifying the rule of capture resulted in a predictable amount of oil or gas that a bank's borrower might be able to produce. This, in turn, enabled a lender to have confidence in extending credit, collateralized by the oil and gas that the borrower would be able to reliably produce, because the borrower's production would be unaffected by the ability of the neighboring landowner to lawfully remove or diminish such produced stream of oil and gas.

In an excellent book chronicling the history of oil and gas financing, the author made the following cogent observations regarding the advantageous consequences that resulted from the imposition of

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84. *See* Gladney v. Anglo-Dutch Energy, LLC, 210 So. 3d 903, 910 (La. Ct. App. 3d Cir. 2016) ("Anglo–Dutch could have modified the lease by entering into a royalty escrow agreement with Plaintiffs, but chose not to of its own volition."). In the interest of full disclosure, the author's law firm represented the petitioner in this suit.

85. Portions of the text that follows on the topic of production allowables represent an adaptation of Patrick S. Ottinger, *Secured Interests in Louisiana Mineral Rights*, 82 LA. L. REV. 1001 (2022).

86. *See* LA. ADMIN. CODE tit. 43, pt. XIX, §§ 3701–3709 (2023) (Statewide Order No. 151-A-2). *See also* ASPRODITES, *supra* note 73, § 1508.

87. *See* LA. ADMIN. CODE tit. 43, pt. XIX, §§ 2101–2103 (2023) (Statewide Order No. 29-F). *See also* ASPRODITES, *supra* note 73, § 1508.

88. Act No. 225, 1934 La. Acts 602.

89. LA. REV. STAT. ANN. § 30:4C(11) (2022); *see also* William Timothy Allen, III, *Drilling Permits, Well Spacing, Allowables and Louisiana Unitization Issues*, 43 ANN. INST. ON MIN. L. 205 (1996).

conservation laws, including the assignment of allowables and proration, to-wit:

> Without the introduction and subsequent court enforcement of conservation laws, the stability of the economic factors necessary for successful financing of oil may never have been achieved. Proration rules slowed the initial rate of well production and had the side effect of slowing the pace at which the producer was able to recover his investment. This created demand for longer-term credit. Fortunately, slower production also led to more disciplined commodity markets, which, in turn, created the crucial element: a predictable cash flow that bankers needed to lend with confidence.[90]

The national movement toward conservation was a positive and important one. An unanticipated but beneficial consequence of the adoption of a regime of conservation (particularly rules pertaining to the spacing of wells, the institution of rules of proration, the assignment of allowables, and unitization) was that certainty and predictability came to a chaotic industry, which in turn resulted in capital markets embracing the oil and gas industry by extending credit. These developments facilitated the advancement of one of the most important sectors of the American economy.[91]

Although not always in the forefront of the powers of the Office of Conservation, the significance of the regulatory authority to impose proration and establish allowables cannot be overstated in terms of its consequential promotion of access to much needed capital by operators.

3. Pooling and Unitization

"Well spacing and proration are two valuable conservation devices, but in order to obtain the greatest advantage from their use, they must be combined with provisions authorizing the compulsory pooling of all tracts of land within the spacing unit."[92] While there is a tendency to refer to the

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90. *See* BERNARD F. CLARK, JR., OIL CAPITAL: THE HISTORY OF AMERICAN OIL, WILDCATTERS, INDEPENDENTS AND THEIR BANKERS 96 (2016).

91. For an interesting examination of the experience in the oil fields in East Texas that at one point in August 1931 resulted in the declaration of martial law and the intervention of the Texas Rangers and the National Guard to enforce proration rules, see JAMES A. CLARK AND MICHEL T. HALBOUTY, THE LAST BOOM (1st ed. 1972). Chapter 12 addresses "Proration." *See id.* at 144–53.

92. Moosa & Saloom, *supra* note 29, at 205.

process that results in the consolidation of interests for the purpose of drilling a well as *unitization*, it is technically more accurate to have reference to *pooling and unitization*. Certainly, at the nascent stage of our conservation laws, two distinct steps were deemed necessary in this regulatory process, namely, *unitization* and then *pooling*.[93] Often, the pooling was effectuated on a conventional basis, with the right reserved to the Commissioner of Conservation to require pooling where the parties failed to do so.[94] However, early case law established the proposition that the mere issuance of a conservation directive, including a permit to drill or an order creating a drilling and production unit, effectuated a pooling of interests, even where the parties did not separately or independently do so.[95]

Indeed, well spacing serves as a triggering mechanism for unitization. As above explained,[96] if a well is not situated at a legal location, the Commissioner will not issue an allowable unless or until the well is unitized. Unitization is the allocation of designated acreage to a well for purposes of development, cost-sharing, and allocation of production.[97]

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93. Louisiana Revised Statutes § 30:10A provides:

> When two or more separately owned tracts of land are embraced within a drilling unit which has been established by the commissioner as provided in R.S. 30:9(B), the owners may validly agree by separate contract to pool, drill, and produce their interests and to develop their lands as a drilling unit.

LA. REV. STAT. ANN. § 30:10A (2022).

94. Louisiana Revised Statutes § 30:10A(1) states:

> Where the owners have not agreed by separate contract to pool, drill, and produce their interests, the commissioner shall require them to do so and to develop their lands as a drilling unit, if he finds it to be necessary to prevent waste or to avoid drilling unnecessary wells.

Id. § 30:10A(1).

95. *See, e.g.*, Everett v. Phillips Petroleum Co., 51 So. 2d 87 (La. 1950) ("[T]he drilling of the Tidewater well [pursuant to the unitization order], *even in the absence of a specific order of forced pooling* . . . was effective as a drilling upon the [non-drill site tract]." *Id.* at 94 (emphasis added)). *See also* Smith v. Holt, 67 So. 2d 93, 95 (La. 1953). Further commentary on this topic can be found in John B. Hussey, *Pooling and Unitization–Government's Point of View*, 2 ANN. INST. ON MIN. L. 28, 40 (1954), and George W. Hardy III, *Ruminations on the Effect of Conservation Laws and Practices on the Louisiana Mineral Servitude and Mineral Royalty*, 25 LA. L. REV. 824, 837–38 (1965).

96. *See* discussion *supra* Part III.C.1.

97. A *drilling unit* is explained in Louisiana Revised Statutes § 30:9B, which provides:

> A drilling unit, as contemplated [in Section 30:9B], means the maximum area which may be efficiently and economically drained by the well or

Production is usually allocated, and costs of operation and development are usually shared on a surface acreage basis.[98]

"To prevent an abuse of the rule of capture and wasteful drilling, Louisiana adopted the concept of forced or compulsory pooling. This concept requires that all persons in the 'pool' of gas, oil or other fugacious minerals share in its production."[99] In *Davis Oil Co. v. Steamboat Petroleum Corp.*,[100] the Louisiana Supreme Court recognized the role and purpose of unitization as follows:

> The general concept behind the establishment of drilling units is to prevent adjoining landowners or leaseholders from having to drill protective offset wells on their premises by permitting them to share production proportionately to the area of their acreage drained by the unit well.[101]

4. Ensuring Opportunity to Receive Just and Equitable Share of Unit Production

Louisiana Revised Statutes § 30:9A reads as follows:

> Whether or not the total production from a pool be limited or prorated, no rule, regulation, or order of the commissioner shall in terms or effect:
>
> (1) Make it necessary for the producer from, or the owner of, a tract of land in the pool, in order that he *may obtain the tract's just*

> wells designated to serve the drilling unit as the unit well, substitute unit well, or alternate unit well. This unit shall constitute a developed area as long as a well is located thereon which is capable of producing oil or gas in paying quantities.

LA. REV. STAT. ANN. § 30:9B (2022). *See* ASPRODITES, *supra* note 73, § 1504.

98. Another mode of allocation of unitized production is on the basis of "acre-foot" which takes into consideration the volumetric structure of the unitized reservoir. *Cf.* Mobil Oil Corp. v. Gill, 194 So. 2d 351, 354 (La. Ct. App. 1st Cir. 1966) (The court rejected contention that "under the provisions of R.S. 30:9(D) the 'just and equitable share' of any producer in a cycling unit must be determined on a volumetric basis [a]s *a matter of law*." The court acknowledged that "the Commissioner has the right to consider other factors in making his determination." (emphasis added)).

99. Corbello v. Sutton, 442 So. 2d 610, 614 (La. Ct. App. 1st Cir. 1983) (internal citation omitted).

100. Davis Oil Co. v. Steamboat Petroleum Corp., 583 So. 2d 1139 (La. 1991).

101. *Id.* at 1142.

> *and equitable share of the production of the pool*, as that share is set forth in this Section, to drill and operate any well or wells on the tract in addition to the well or wells that can without waste produce this share, or
>
> (2) Occasion net drainage from a tract unless there be drilled and operated upon the tract a well or wells in addition to the well or wells thereon that can without waste *produce the tract's just and equitable share of the production of the pool*.[102]

A tract owner's "just and equitable share" of production from a unitized tract is defined in Louisiana Revised Statutes § 30:9D as follows:

> Subject to the reasonable necessities for the prevention of waste, and to reasonable adjustment because of structural position, a producer's just and equitable share of the oil and gas in the pool, also referred to as a tract's just and equitable share, is that part of the authorized production of the pool, whether it be the total which could be produced without any restriction on the amount of production, or whether it be an amount less than that which the pool could produce if no restriction on amount were imposed, which is substantially in the proportion that the quantity of recoverable oil and gas in the developed area of his tract or tracts in the pool bears to the recoverable oil and gas in the total developed area of the pool, in so far as these amounts can be practically ascertained.[103]

Louisiana courts have consistently endeavored to protect a tract owner's "just and equitable share of the oil and gas in the pool without unnecessary expense."[104] Indeed, it has been recognized that "[t]he Commissioner has the authority to issue any order necessary to properly administer and enforce the requirement that the owner of each tract be given the opportunity to recover or receive his just and equitable share of oil and gas in the pool without unnecessary expense."[105]

It is no subtle observation to note that allocations of unit costs and of unit revenue are actually directed to the pertinent tract in question and are then reallocated among owners of the unitized tract according to interests

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102. LA. REV. STAT. ANN. § 30:9A (2022) (emphasis added).
103. *Id.* § 30:9D.
104. *See* Amoco Prod. Co. v. Thompson, 516 So. 2d 376, 394 (La. Ct. App. 1st Cir. 1987).
105. Tex/Con Oil & Gas Co. v. Batchelor, 634 So. 2d 902, 909 (La. Ct. App. 1st Cir. 1993).

therein. In *Arkansas Louisiana Gas Co. v. Southwest Natural Production Co.*,[106] the unit operator brought a declaratory judgment action seeking an answer to this question:

> Are the royalty owners throughout the unit entitled to be paid on the basis of the return from the sale of all gas and distillate produced from the unit, or only on the basis of the amounts realized by their own lessees from the sale of the proportion of the production allocated to the tract in which they have an interest?[107]

The Court held for defendants, adopting the latter contention, stating that "[i]t is our conclusion, therefore, that the royalty owners in this unit are entitled to be paid from the proceeds realized from the share of the production of this well allocated to the tracts in which they have an interest, as specifically provided in their individual contracts."[108]

This tract allocation gives rise to an *in rem* responsibility of the tract for unit well expenses. Inarguably, a tract of land—being a corporeal immovable[109]—is insusceptible of being obligated personally for such expenses. This means that production allocable to the tract within the unit can be withheld by the operator, but no owner in the tract has personal responsibility in the absence of consent.

IV. THE CURRENT CONSTRUCT OF THE CONSERVATION ACT

As noted above, the current version of Section 10 is far from a model of legislative clarity in terms of its structure and disparate, disconnected provisions that would make Rube Goldberg proud.[110] To evaluate certain

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106. Ark. La. Gas Co. v. Sw. Nat. Prod. Co., 60 So. 2d 9 (La. 1952).

107. *Id.* at 9.

108. *Id.* at 11.

109. "Tracts of land . . . are immovables." LA. CIV. CODE ANN. art. 462 (2022).

110. *Rube Goldberg*, LEARNING WITH STEM, https://www.lumen-stem.com/chain-reactions.html#:~:text=RUBE%20GOLDBERG%20(1883%2D1970),zany%20contraptions%20of%20Professor%20Butts [https://perma.cc/F7BJ-X2P7] (last visited Mar. 17, 2023):

> RUBE GOLDBERG (1883-1970) was a cartoonist, an inventor, and the only person ever to be listed in Merriam-Webster's Dictionary as an adjective. Of the nearly 50,000 cartoons he drew in his lifetime, Rube is best known for the zany contraptions of Professor Butts. These inventions, also known as Rube Goldberg Machines, solved a simple task in the most overcomplicated, inefficient, and hilarious way possible.

provisions contained therein, it is necessary to take note of a few of the definitions employed in Section 10.[111]

A. Preface

Notably, the term *operator* is not defined in Title 30, although it is used in the definition of *owner* and in Subsection 10A(3), to be hereinafter noted.[112] Nevertheless, the notion and role of an *operator* is well known and understood in the industry.[113]

Importantly, the term *owner* is defined as "the person, including operators and producers acting on behalf of the person, who has or had the right to drill into and to produce from a pool and to appropriate the production either for himself or for others."[114] Prior to its amendment in 1993,[115] the definition of *owner* simply alluded to a "person . . . who has the right to drill into and to produce from a pool," that is, it did not extend to a person who *had* such right.[116] The Louisiana Supreme Court explained the motivation for this amendment as follows:

> The 1993 amendment to La. R.S. 30:3(8) merely gives the Commissioner the discretion to proceed under La. R.S. 30:4(C)(16)(a) against prior owners in certain circumstances. At oral argument, the Commissioner explained that the amendment was a "Commissioner's bill," drafted to give the Commissioner more discretionary authority to proceed against prior owners, not to encumber the Commissioner with the additional duty of having to ascertain every prior lease holder of a site and to determine which lease holder actually caused the subject contamination. It is

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111. A range of terms are defined in Louisiana Revised Statutes § 30:3, which section begins with the admonition that "[u]nless the context otherwise requires, the words defined in this Section have the following meaning *when found in this Chapter* . . . ." LA. REV. STAT. ANN. § 30:3 (2022) (emphasis added). Hence, the defined terms have no application beyond Chapter One of Title 30, being sections 1 through 101.10.

112. *See* discussion *infra* Part IV.I.

113. *See* Hunt Oil Co. v. Batchelor, 644 So. 2d 191, 196 (La. 1994) ("The Commissioner has the power to establish compulsory units and designate unit operators therefor."); EnerQuest Oil and Gas, LLC v. Honorable Philip N. Asprodites, Comm'r of Conservation, 843 So. 2d 535, 542 (La. Ct. App. 1st Cir. 2003) ("Louisiana Revised Statutes 30:9 gives the Commissioner the authority to designate unit operators.").

114. LA. REV. STAT. ANN. § 30:3(8) (2022).

115. Act No. 113, 1993 La. Acts 224.

116. LA. REV. STAT. ANN. § 30:3(8) (2022).

> well established in the State's oil and gas community that the current "operator of record" of a lease is responsible for remediation on that lease.[117]

Also undefined in the Conservation Act is the term *unleased*. This term is used in ten sections in Title 30, five of which are contained in the Conservation Act (Chapter One of Title 30 of the Revised Statutes),[118] including Subsection 10A(3), to be hereinafter noted. One might logically assume that a reference to an *unleased* interest would be to the interest of a landowner or mineral servitude owner which is not subject to any mineral lease whatsoever. However, two cases—one state, one federal—concluded otherwise, at least in reference to the workings of the Well Cost Reporting Statute, Louisiana Revised Statutes §§ 30:103.1–104.[119]

The term *unleased* is also used in Louisiana Revised Statutes § 30:111. As innocuous as this statute is, section 30:111 was invoked by a federal district court to justify its conclusion that a statutory reference to the owner of an *unleased* interest may include a mineral lessee other than the operator. Thus, in *Dow Construction, LLC v. BPX Operating Co.*, the court noted as follows:

> At times, Title 30 uses "unleased interests" to mean completely unleased, and, at other times, it means unleased only as to the operator of the well. In other words, based on the surrounding context, the Louisiana Legislature includes or excludes a lessee such as Dow from the term "unleased interests." For example, section 111 uses the phrase "[o]wners of unleased mineral interests *and lessees*." Additionally, section 10(A)(2)(e)(i) provides that the "provisions regarding a risk charge will 'not apply to any unleased interest *not subject to an oil, gas, and mineral lease*.'" It is clear based on the clarifying language in sections 10(A)(2)(e)(i) and 111 that a lessee is excluded from the term "unleased interests." However, the phrase "not subject to an oil, gas, and mineral lease" "would be superfluous if 'unleased

117. Yuma Petroleum Co. v. Thompson, 731 So. 2d 190, 193–94 (La. 1999).

118. LA. REV. STAT. ANN. §§ 30:5, 30:5.1, 30:5.2, 30:10, 30:10.1 (2022).

119. *See* XXI Oil & Gas, LLC v. Hilcorp Energy Co., 124 So. 3d 530 (La. Ct. App. 3d Cir. 2013); TDX Energy, LLC v. Chesapeake Operating, Inc., 857 F.3d 253, 256–57 (5th Cir. 2017). In the interest of full disclosure, the author was counsel for the defendant in the federal case and represented the defendant in the state case after rendition of the appellate decision to prosecute an application for writ of certiorari to the Louisiana Supreme Court, which was denied.

> interest' always meant an interest not subject to any lease."[120]

As of the date of this writing, the *Dow* case is on appeal to the United States Court of Appeals for the Fifth Circuit and is thus not final.[121] While awaiting appellate resolution, one is struck with the notion that the analysis as to legislative purpose or intention might be giving a bit more credit to the legislature than is justified.

B. Basic Rule of Sharing of Cost and Revenue

The first subsection of Section 10 serves as a *gatekeeper* to the provisions that follow. Thus, Subsection 10A reads as follows:

> When two or more separately owned tracts of land are embraced within a drilling unit which has been established by the commissioner as provided in R.S. 30:9(B), the owners may validly agree by separate contract to pool, drill, and produce their interests and to develop their lands as a drilling unit.
>
> (1) Where the owners have not agreed by separate contract to pool, drill, and produce their interests, the commissioner shall require them to do so and to develop their lands as a drilling unit, if he finds it to be necessary to prevent waste or to avoid drilling unnecessary wells.
>
> (a) All orders requiring pooling shall be made after notice and hearing. They shall be upon terms and conditions that are just and reasonable and that will afford the owner of each tract the opportunity to recover or receive his just and equitable share of the oil and gas in the pool without unnecessary expense. They shall prevent or minimize reasonable avoidable drainage from each developed tract which is not equalized by counter drainage.
>
> (b) The portion of the production allocated to the owner of each tract included in a drilling unit formed by a pooling order shall, when produced be considered as if it had been produced from his

120. Dow Constr., LLC v. BPX Operating Co., 564 F. Supp. 3d 479, 484–85 (W.D. La. 2021), *reconsideration den'd*, No. CV 20-9, 2022 WL 1433013 (W.D. La. May 5, 2022) (internal citations omitted).

121. Notice of Appeal, No. 22-30379 (5th Cir. June 24, 2022). Oral argument was held on May 2, 2023.

tract by a well drilled thereon.[122]

In view of the foregoing, Section 10A delineates the following circumstances under which a well is not governed by its provisions, to-wit:

1. The well is drilled on a non-unitized, "lease basis";[123]

2. The well is unitized on a conventional, not compulsory, basis;[124]

3. The well is unitized as a "reservoirwide" unit, a "deep pool" unit, or a "coal seam natural gas producing" unit;[125]

4. The unit for the well, even if created and established pursuant to Louisiana Revised Statutes § 30:9, is composed of a single tract of land entirely burdened by lease(s) owned or held by the operator (and perhaps its "well partners"),[126] which lease(s) cover and affect one hundred percent of the minerals thereunder, with no unleased tract of land or interest, i.e., there are no "separately

122. LA. REV. STAT. ANN. § 30:10A(1) (2022). Concerning Section 10A(1)(b), see SW. Gas Producing Co., Inc. v. Creslenn Oil Co., 181 So. 2d 63, 68 (La. Ct. App. 2d Cir. 1965) ("It logically follows that . . . the share of production allocated to the tracts comprising the original half section unit must be considered as production from a well drilled on that unit.").

123. *See* discussion *supra* note 80.

124. *See* Patrick S. Ottinger, *Conventional Unitization in Louisiana*, 49 ANN. INST. ON MIN. L. 21 (2002). If the unit is "conventional," it is either a declared unit or a voluntary (contractual) unit. In either instance, there is likely unanimous consent among the working interest owners, certainly in the case of the declared unit. *Cf.* Union Oil Co. of Cal. v. Touchet, 86 So. 2d 50 (La. 1956). *See* OTTINGER, MINERAL LEASE TREATISE, *supra* note 1, § 4-21.

125. *See* discussion *supra* note 4. While these identified kinds of compulsory unit are beyond the purview of the cost regime articulated in Section 10, each statutory provision establishing the Commissioner's authority for the creation of such units articulates a particular cost regime that is essentially of the same functional import as provided in Section 10 with respect to a "drilling and production unit."

126. The vernacular term *well partner* is not used in the legal sense of a partnership, see LA. CIV. CODE ANN. art. 2801 (2022), but has reference to co-participants along with the operator who jointly assume the cost, risk, and expense of drilling a well.

owned tracts of land [] embraced within a drilling unit";[127] and

> 5. The unit for the well, even if there are no "separately owned tracts of land [] embraced within a drilling unit,"[128] is governed by a contract between the operator and all other interest owners, and there is no interest in the unit which is not subject to a contractual agreement with the operator.[129]

Some commentary on the meaning of "two or more separately owned tracts of land" is in order. After the Commissioner of Conservation creates and establishes a unit following a public hearing, the operator must prepare and submit a unit survey plat for review and approval by the Office of Conservation. Section 4103(A)(2) of Statewide Order No. 29-B sets forth the following requirements for the preparation of this unit survey plat:

> The affected tracts shall be identified on the survey plat by the names of the fee[130] and lease owners, based on the best available information. Further, each unit plat shall have an inset or attachment showing the number, name, acreage (or other basis of participation) and the unit percentage participation of each tract.[131]

Indicatively, the provisions of Section 10 are applicable absent any other contract or agreement between the parties to a compulsory unit.[132]

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127. As the Louisiana Supreme Court has observed, "[W]here there is a sole owner of a unit, a pooling order can serve no useful purpose." Smith v. Holt, 67 So. 2d 93, 96 (La. 1953).

128. *See id.*

129. As will be explained, a contract with the operator is typically a joint operating agreement, but other types of contracts might include cash contribution agreements, dry hole letters, a farm-in agreement, to name a few.

130. It is regrettable that, in this civil law jurisdiction, the term *fee title* is used, in this case, by an administrative agency, but also by the courts and legislators. *Fee title* is a common law term, unknown in the civil law of property. *See* Ottinger, *From the Courts to the Code*, *supra* note 1, at 12.

131. LA. ADMIN. CODE tit. 43, pt. XIX, § 4103(A)(2) (2023).

132. *See, e.g.*, LA. REV. STAT. ANN. § 30:10A(2)(g) (2022) ("Nothing contained herein shall have the effect of enlarging, displacing, varying, altering, or in any way whatsoever modifying or changing the rights and obligations of the parties thereto under any contract between or among owners having a tract or tracts in the unit."). See also the prefatory or opening language of Section 10A, noting that "the owners may validly agree by separate contract to pool, drill, and produce their interests and to develop their lands as a drilling unit" and stating the proposition that Section 10 is to apply "[w]here the owners have not agreed by separate contract to pool, drill, and produce their interests." *Id.*

Typically, a joint operating agreement might exist among working interest owners, in which instance, such contract—and not the default regime of Section 10—provides the relevant rules to determine cost responsibility.[133] Also, as to a landowner or mineral servitude owner if a mineral lease exists, the various provisions of Section 10 have no role in evaluating the rights and obligations of the lessor *vis-à-vis* the lessee as to the lessor's entitlement to revenue.[134]

As pertains to the lessee of a mineral lease covering a unitized tract of land, in which lease the operator owns no interest, and as to which no other contract exists between the operator and that lessee, the rights and obligations of the parties are governed by Section 10 and, in particular, the Risk Fee Act hereafter discussed.[135]

C. Components of Unit Costs to be Recouped by Operator

If there is an essential core feature of Section 10 as it pertains to the basic responsibility for unit costs, it would be the statutory enumeration of "actual reasonable" costs of "drilling, testing, completing, equipping and operating" the unit well for which a unitized tract is ratably liable.[136] This statement, while accurate, says nothing whatsoever about the rights of the operator to enforce its paramount right of reimbursement or the manner in which the operator might enforce its rights to be "made whole" with respect to such unit well costs which it personally incurred for the benefit of the unitized community of interests.

The five cost components of "drilling, testing, completing, equipping and operating" permeate Section 10 and have relevance in other associated contexts or relationships.[137] The proper characterization or categorization of unit costs incurred in the well is an endeavor that brings into play an array of specialists, certainly including accountants, geologists, and

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133. If no operating agreement exists among co-owners of a mineral lease, Mineral Code article 177 provides that a "co-owner of the lessee's interest in a mineral lease may not independently conduct operations . . . without the consent of his co-owner." *See* Patrick S. Ottinger, *Permission Granted: The Requirement of Consent Under the Louisiana Mineral Code*, 80 LA. L. REV. 1287, 1309 (2020) (quoting LA. REV. STAT. ANN. § 31:177 (2020)).

134. *See* Patrick S. Ottinger, *Calculating the Lessor's Royalty Payment: Much More Than Mere Math*, 6 LSU J. OF ENERGY L. & RES. 1 (2017).

135. *See* discussion *infra* Part IV.F.4.

136. LA. REV. STAT. ANN. § 30:10A(2)(b)(i) (2022).

137. *See* discussion *infra* Part IV.E.

petroleum engineers.[138] For these reasons, it is both necessary and appropriate to examine in some detail the ambit of activities or costs that each enumerated component encompasses.

1. Drilling Costs

The first component of the five enumerated functions—the costs of *drilling* the unit well—clearly relates to those costs and expenses incurred to conduct the physical activities to encounter and lead to the production of oil and gas. *Drilling* is defined as the "[a]ct of boring a hole through which oil and/or gas may be produced if encountered in commercial quantities."[139]

Certain costs falling under this moniker predate the actual *spudding in* of the unit well,[140] while the majority arise in the actual drilling activity from inception to objective depth. Thus, this category of costs is not restricted to expenditures arising solely with reference to actual physical activities while the well is being drilled by a drilling contractor[141] but would encompass costs and expenditures for preparatory, administrative, or regulatory functions that are necessary, and without which a well could not be drilled. These costs are typically set forth in an AFE[142] prepared by

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138. The purposes for which these costs are collected and assembled give rise to issues in terms of the manner or format in which they are reported, particularly in connection with the issue of production in "paying quantities." *See* Patrick S. Ottinger, *Maintaining "Two Sets of Books" in a Production in "Paying Quantities" Case: Nefarious or Necessary?*, 9 LSU J. OF ENERGY L. & RES. 435 (2021).

139. MARTIN & KRAMER, *supra* note 33, at 309.

140. The term *spud in* has been defined by one court as follows:

> [T]he term to "spud in" has a well-defined meaning in the oil industry as the first boring of the hole in the ground, that is, the first actual penetration of the earth with a drilling bit; it has a distinct meaning different from other terms of the industry, such as to "commence to drill", which refer to the first operations on the land preliminary to the actual drilling or spudding in.

Hilliard v. Franzheim, 180 So. 2d 746, 747 (La. Ct. App. 3d Cir. 1965). *See* OTTINGER, MINERAL LEASE TREATISE, *supra* note 1, § 5-04(a).

141. *See* Patrick S. Ottinger, *Drilling Contracts*, 38 ANN. INST. ON MIN. L. 99, 155–56 (1991).

142. An "AFE" is an Authorization for Expenditure, a document issued by an operator to a non-operator in which an estimate of the costs to drill a well (or conduct some other activity) is set forth, and seeking the approval of the non-operator to participate in the activity described therein, and to pay its share of the estimated costs. *See* M & T, Inc. v. Fuel Res. Dev. Co., 518 F. Supp. 285, 289

the operator to enable another party to have a clear understanding of the range of costs to be incurred in this seminal phase of a proposed operation.

2. Testing Costs

After the well is drilled to its objective depth, it is incumbent upon the operator to *test* the well to ascertain if the well has encountered oil and gas in commercial quantities so as to justify the expenditures to *complete* the well. If not, the well is a *dry hole*,[143] and the operation is abandoned. The term *testing* is not defined in the *Manual of Oil and Gas Terms*, but one case from Colorado referred to *drilling* as a "form of geologic testing, in order to explore for mineral deposits."[144] The principal mode of testing is the running of an *electric well log*, which yields a diagrammatical representation of what has been encountered in the borehole of the well.[145]

3. Completing Costs

As a result of the testing of the well, by examination and analysis of the electric log and perhaps core samples or other pertinent well data, the operator makes a determination as to whether the results of the well justify an attempt to complete the well. This typically entails running production casing and perforating the tubing at subsurface depths near the bottom hole so as to access any productive formations encountered. The *Manual of Oil and Gas Terms* does not contain a definition for the precise term *completing*, but it is explained that "[c]ompletion of a well involves those processes necessary before production occurs and after drillers have hit

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(D.C. Co. 1981) ("It is axiomatic that drilling costs cannot be established with certainty and that an AFE is at best a good-faith estimate. AFE's are usually exceeded, often by very substantial amounts. . . . In the oil and gas industry, it is understood and accepted that when one signs an AFE, he is committed to his proportionate share of the necessary costs in drilling to the objective specified in the AFE, unless the parties mutually agree to terminate drilling earlier or to attempt a completion at a shallower formation.").

143. A *dry hole* is defined as a "completed well which is not productive of oil and/or gas (or which is not productive of oil and/or gas in paying quantities)." MARTIN & KRAMER, *supra* note 33, at 341.

144. Grynberg v. Northglenn, 739 P.2d 230 (Col. 1987).

145. The running of an *electric well log* is a procedure of lowering certain instruments into a well and shooting electric currents through such instruments for the purpose of testing formations. Steeger v. Beard Drilling, Inc., 371 S.W.2d 684 (Tex. 1963).

the pay sand, *viz.*, perforating the casing and washing out the drilling mud."[146]

4. Equipping Costs

The *equipping* of a well entails the installation of a variety of equipment or fixtures as is necessary to enable the well to produce oil and gas. Again, no definition of *equipping* is contained in the *Manual of Oil and Gas Terms*, but one does find the term *equipment costs* as having reference to "[c]ost of equipment installed in a well prior to commencement of production."[147]

5. Operating Costs

Unlike the first four enumerated components of unit costs, the function of operating a well is one that spans time essentially commencing with the completion and equipping of the well and the concomitant commencement of production. All other components have a start and end date, accruing into the next phase. Clearly, drilling ends at the point that the well is tested unless the evaluation results in a decision to deepen or sidetrack the well. After testing, it might be that the operator elects to go to the next different phase of completing the well. And once the well is completed, it is then equipped for production.

After that phase, the well is operated in the sense of managing and administering the actions necessary to produce the well and to maintain its status as a producer. Generally, operating the well continues for the life of production and entails actions away from the wellsite that are necessary and give rise to administrative activities, the costs of which are also recoverable. Costs to operate the well are called current operating expenses[148] and constitute the relevant set of costs that come into play in a

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146. MARTIN & KRAMER, *supra* note 33, at 203.

147. *Id*. *See* Blanchard v. Pan-Ok Production Co., Inc., 755 So. 2d 376, 382 (La. Ct. App. 2d Cir. 2000) ("In a broad sense, completion means mechanically equipping a well so that the subsurface formation is open to the flow of hydrocarbons from the formation through the well bore and to the surface for sale."). *See also* OTTINGER, MINERAL LEASE TREATISE, *supra* note 1, § 5-12(d)(2).

148. These are sometimes called "lifting costs," a term having reference to those costs incurred by the operator and which are "necessary to lift the oil from the ground." Stewart v. Amerada Hess Corp., 604 P.2d 854, 857 n.8 (Okla. 1980). *See* OTTINGER, MINERAL LEASE TREATISE, *supra* note 1, § 3-15(b).

determination that the mineral lease is being maintained by production in "paying quantities."[149]

Although admittedly subtle, a point of distinction between the term *operating* and *operations* is in order. The Louisiana Mineral Code recognizes that "operations on the land burdened by the lease or land unitized therewith sufficient to maintain the lease according to its terms will continue it in force as to the entirety of the land burdened."[150] The Louisiana Supreme Court has held that *operations* means and relates to "the physical activity associated with the attempt to discover or maintain production."[151] This understanding of the term *operations* suggests a connotation of the word as being a mode of *lease maintenance*, while the act of *operating* more broadly contemplates the physical actions involved in producing the well.

D. Important Point of Demarcation Between the Development Phase and the Commencement of Production Phase

"Louisiana, as well as the oil and gas industry in general, makes a distinction between production costs and post-production costs. It is generally accepted that the production phase of oil and gas operations terminates at the wellhead when the minerals are reduced to possession."[152] Hence, the wellhead is the functional point in time when the first four of the five components have occurred, and the operation of the well commences when production is obtained and brought to the surface. It is also the point in

149. LA. REV. STAT. ANN. § 31:124 (2022). *See* Patrick S. Ottinger, *Production in "Paying Quantities"—A Fresh Look*, 51 ANN. INST. ON MIN. L. 24 (2004) (also published at 65 LA. L. REV. 635 (2005); 67 ROCKY MT. MIN. L. INST. 6-1 (2021)). *See also* Patrick S. Ottinger, 69th Institute on Mineral Law at the Paul M. Hebert Law Center, Louisiana State University: Prices Go Up, Prices Go Down: The Effect of Volatile Market Conditions on a Production in "Paying Quantities" Analysis (Mar. 31, 2022).

150. LA. REV. STAT. ANN. § 31:114 (2022). *See* OTTINGER, MINERAL LEASE TREATISE, *supra* note 1, at ch. 4, pt. II.

151. Bouterie v. Kleinpeter, 247 So. 2d 548, 555 (La. 1971) (citing Babin v. First Energy Corp., 693 So. 2d 813, 815 (La. Ct. App. 1st Cir. 1997)). *See* OTTINGER, MINERAL LEASE TREATISE, *supra* note 1, §§ 3-05(c), 4-09(c), 4-32(d)(1).

152. J. Fleet Oil & Gas Corp., L.L.C. v. Chesapeake La., L.P., No. CV 15-2461, 2018 WL 1463529, at *6 (W.D. La. Mar. 22, 2018) (unpublished) (citing Babin v. First Energy Corp., 693 So. 2d 813, 815 (La. Ct. App. 1st Cir. 1997)). In the interest of full disclosure, this author represented the defendant in the *J. Fleet* case.

time when a variety of consequences arise in the relationship between the operator and other parties in the unit.

E. Other Circumstances or Contexts in Which the Components of Unit Costs are Involved or Relevant

The pertinence of this enumerated string of cost components presents itself in other important associated contexts tangentially related to Section 10. For example, under the Risk Fee Act,[153] while the operator is entitled to recoup costs allocable to the unitized interest of a nonparticipating owner, generated in all five cost areas, the risk charge, if applicable, only applies to the cost of drilling, testing, and completing the unit well but does not pertain to the cost of equipping and operating the well.[154] This divergence is based upon the risk associated with the first three components of cost but not with regard to costs incurred in connection with equipping and operating the well, much to the same extent as under the *Subsequent Operations Clause* of a joint operating agreement.[155]

Regarding the forfeiture of costs an operator suffers who is judicially determined to have failed to timely or properly report costs under the Well Cost Reporting Statute, that Act provides that "such operator or producer shall forfeit his right to demand contribution from the owner or owners of the unleased oil and gas interests for the costs of the *drilling operations of the well*."[156]

While one might reasonably infer that the only costs to be forfeited were those arising out of *operations* associated with the *drilling* of the well, being those incurred *before* the point of production (but not including costs of testing or completing the well), the courts have been inconsistent in defining the scope of this forfeiture. For example, in *White v. Phillips Petroleum Co.*,[157] the court took up "plaintiffs' claim for recovery without deduction for drilling and operating costs."[158] It was not necessary to judicially resolve the issue, as the court found no violation of the reporting statute.

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153. *See infra* Part IV.F.4.
154. LA. REV. STAT. ANN. § 30:10A(2)(b)(i) (2022).
155. *See* discussion *infra* note 225.
156. LA. REV. STAT. ANN. § 30:103.2 (2022) (emphasis added).
157. White v. Phillips Petroleum Co., 232 So. 2d 83 (La. Ct. App. 3d Cir. 1970).
158. *Id.* at 90.

Later, in *XXI Oil & Gas, LLC v. Hilcorp Energy Co.*,[159] the appellate court stated that "[w]hen reading the two statutes in conjunction with one another it is obvious that costs of drilling operations include the costs of 'drilling, completing, and equipping the unit well.'"[160] Further, the court stated that it did "agree with the trial court that the penalty for 'costs of the drilling operations' includes both pre-production and post-production costs."[161] This statement is most troubling and problematic to future litigants if the decision is asserted as authority for the statement made by the majority.[162]

Ineluctably, the Well Cost Reporting Statute, being penal in nature, must be strictly construed.[163] It seems inconceivable that the author of the *XXI* opinion had in mind marketing costs, being the essence of what are often called *post-production costs*.[164] Rather, it is generally believed that the court's language in stating this conclusion appears to have misused the term *post-production costs*, employing it in a temporal sense to refer to *all* otherwise chargeable costs incurred after the wellhead to operate the well once it is drilled, and production commences, but not including marketing costs.[165] The casual, perhaps unartful, use of the words *post-production costs* in the *XXI* decision is demonstrably *obiter dictum*. Certainly, the

159. XXI Oil & Gas, LLC v. Hilcorp Energy Co., 206 So. 3d 885 (La. Ct. App. 3d Cir. 2016). This is the same case as is cited *supra* note 119 but taking up a different issue under the Well Cost Reporting Statute.

160. *Id.* at 890.

161. *Id.*

162. Judge Pickett dissented with respect to the two-judge majority's reference to "post-production costs" as being within the ambit of costs that are forfeited by the operator due to a violation of the reporting statute. *Id.* at 892.

163. *See* White v. Phillips Petroleum Co., 232 So. 2d 83, 90 (La. Ct. App. 3d Cir. 1970) ("This [Well Cost Reporting Statute] is a penal statute, requiring strict construction.").

164. Common marketing or post-production costs include "those related to taxes, transportation, processing, dehydration, treating, compression, and gathering." J. Fleet Oil & Gas Corp., L.L.C. v. Chesapeake La., L.P., No. CV 15-2461, 2018 WL 1463529, at *6 (W.D. La. Mar. 22, 2018). See also COUNCIL OF PETROLEUM ACCOUNTANTS SOCIETIES (COPAS), ACCOUNTING GUIDELINE NO. 15 GAS ACCOUNTING MANUAL G-26 (Apr. 2010), which defines "post-production" costs as "costs incurred after production, such as compression, dehydration, treating and transportation to the point of delivery to the purchaser /plant/mainline."

165. In *J. Fleet*, the district judge explicitly stated that "the term 'development' as it is written in the provision does not include marketing costs, *i.e.*, post-production costs[,]" a judicial recognition of the fact that the two terms are synonymous. *J. Fleet Oil & Gas Corp.*, 2018 WL 1463529, at *7.

structure of the sentence strongly indicates that the words were simply used in a temporal sense to contrast with the preceding reference to *pre-production costs*.

More tellingly, an examination of the record of the trial at the district court established beyond cavil that no marketing costs were at issue in the case, and no evidence as to such costs was introduced in the record. The case was tried in state district court in Lafayette Parish, Louisiana.[166] Rather, the case, as it pertains to the scope of costs, was tried solely on the basis of a stipulation between the parties which set forth four distinct categories of cost, namely, drilling, completing, equipping, and operating. The stipulation further provides definitions of each term which essentially comport with the universal understanding of those terms within the context of Section 10.[167] The parties explicitly stipulated that both the plaintiff and defendant did "waive the right to present evidence at the trial on September 21, 2015[,] regarding the Unit Well costs or their characterization."[168] Hence, clearly, the trial court did not have before it *any* evidence whatsoever of any marketing costs, and its ruling—based solely on the parties' joint stipulation—provided no insight into such expenses.

As it is conclusively *dictum*, a future litigant in a case in which the import of the *XXI* decision is argued to be relevant to the issue of whether post-production costs are subject to forfeiture might consider requesting the court to take judicial notice of the suit record, particularly the stipulation, pursuant to Rule 201 of the applicable (state or federal) rules of evidence.[169]

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166. *See* XXI Oil & Gas Co, LLC v. Hilcorp Energy Co., No. 2011-5292 (15th Jud. Dist. Ct. Jan. 6, 2012) (unreported). A review of the online civil records of the Clerk of Court reveals the Stipulation next mentioned.

167. "A stipulation has the effect of a judicial admission or confession, which binds all parties and the court. Stipulations between the parties in a specific case are binding on the trial court when not in derogation of law. Such agreements are the law of the case." R.J. D'Hemecourt Petroleum, Inc. v. McNamara, 444 So. 2d 600, 601 (La. 1983) (internal citations omitted). "A judicial confession is a declaration made by a party in a judicial proceeding. That confession constitutes full proof against the party who made it." LA. CIV. CODE ANN. art. 1853 (2022).

168. Joint Stipulations of Fact at ¶ 8, XXI Oil & Gas, LLC v. Hilcorp Energy Co., No. 2011-5292 (15th Jud. Dist. Ct. Sept. 21, 2015).

169. Functionally identical in both the state and Federal Rules of Evidence (FRE), article 201 requires the court to take judicial notice of an "adjudicative fact" if it is a fact that is "not subject to reasonable dispute" because it "can be accurately and readily determined from sources whose accuracy cannot reasonably be questioned." FED. R. EVID. 201. The term *adjudicative fact* is not defined in the Federal Rules of Evidence. *See id.* However, in the Notes of

F. Dealing with Non-Consenting Parties: The Louisiana Risk Fee Act[170]

1. The Free Rider

The free rider has been the proverbial thorn in an operator's side for as long as the industry has been around. By the moniker of *free rider*, one refers to a person or entity who, having the right to conduct drilling activities to exploit mineral resources, prefers to have another person or entity do so at its sole cost, risk, and expense. Then, if the exploration venture is unsuccessful (a dry hole), the free rider simply walks away, but, if successful (the completion of a well capable of producing oil or gas in commercial quantities), the free rider seeks to receive its share of the production, in both cases, with no responsibility for costs or expenses.

The practice of free riding was explained by commentators as pertaining to the situation in which "the developing cotenant bears the risk of development, with the non-developing cotenant free riding on the coattails of a successful well and disclaiming any responsibility for any unsuccessful well."[171]

In a presentation to the Mineral Law Institute predating the 1984 adoption of the Risk Fee Act, one respected commentator noted that the 1940 Conservation Act, although "a modern comprehensive statute which has been extremely effective in practice," is nonetheless "lacking in at least one respect." "It fails to provide for a satisfactory method by which the unit well costs can be recovered by the operator," thus "permit[ting] non-operators to enjoy a 'free ride' under certain circumstances."[172]

Subsequent to the adoption of the Risk Fee Act, the same commentator made the following observations at the 1991 Mineral Law Institute, after explaining the system by which unit well cost adjustments were accomplished:

> The system worked and was considered to be fair and equitable

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Advisory Committee on Proposed Rules, pertinent to FRE 201, it is stated that "Adjudicative facts are simply the facts of the particular case." *Id.* The rule further states that it is mandatory that the court "must take judicial notice if a party requests it and the court is supplied with the necessary information." *Id.*

170. Portions of this section are drawn and adapted from Ottinger, *It's a Risky Business*, *supra* note 1, and Ottinger, *The "Free Rider" in Louisiana—the "Louisiana Risk Fee Act," supra* note 1.

171. Timothy C. Dowd et al., *Statutory Pooling and the Unleased Mineral Owner*, 65 ROCKY MT. MIN. L. INST. 13, 13–15 (2019). *See also* ASPRODITES, *supra* note 73, § 1514.

172. *See* Robert T. Jorden, *Unit Well Costs*, 14 ANN. INST. ON MIN. LAW 15, 26 (1967).

by most industry representatives, but it was thought that there should be a risk charge applied to any free-riding owners who did not share in the original risk of drilling a unit well—something similar to the non-consent provisions in the typical joint operating agreement. An industry committee pushed for and after two or three failed attempts finally, with Commissioner Sutton's assistance, persuaded the Louisiana Legislature to adopt a statute designed to reward the risk takers and/or penalize the free riders, and that is the Risk Fee Act which will be discussed below.[173]

2. Basis of Enforcing Payment of Costs by Nonparticipating Party

Section 10A(2) straightforwardly acknowledges that "cost of development and operation of the pooled unit [are] chargeable to the owners therein."[174] It says nothing, however, as to the precise manner in which the costs might be recovered. In the absence of express consent on the part of a cost-bearing party in a compulsory unit,[175] the operator has no ability to enforce the obligation to reimburse except out of production, if any.

The jurisprudence recognizes an exception to this rule. If the nonparticipating owner is included in the compulsory unit as a consequence of action which it took in connection with the creation or revision of the unit, the courts have held that such an owner may be liable out-of-pocket to the operator. Under these circumstances, the risk that the well will never achieve *payout* shifts to the nonparticipating owner who may be required to pay its share of costs in cash.

The principal case that establishes this exception is *The Superior Oil Co. v. Humble Oil & Refining Co*.[176] Therein, the plaintiff-operator sued

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173. *See* Robert T. Jorden, *Unit Well Cost Adjustment in Louisiana*, 38 ANN. INST. ON MIN. LAW 81, 86–87 (1991) [hereinafter Jorden, *Unit Well Cost Adjustment in Louisiana*].

174. LA. REV. STAT. ANN. § 30:10A(2) (2022).

175. The term "cost-bearing party" has reference to the owner of an interest, the nature of which would intrinsically carry responsibility for costs. Thus, this would encompass a mineral lessee, LA. REV. STAT. ANN. § 31:114 (2000), as well as a landowner and mineral servitude owner who is unleased (respectively, *id.* §§ 31:6, 31:21). However, this would exclude, by way of example, a mineral royalty interest which is generally free of drilling or production costs. *See id.* § 31:80. *See* PATRICK S. OTTINGER, MINERAL ROYALITIES, *in* LOUISIANA MINERAL LAW TREATISE, *supra* note 18, at ch. 5.

176. The Superior Oil Co. v. Humble Oil & Refining Co., 165 So. 2d 905 (La. Ct. App. 4th Cir. 1964).

the defendant to recover a sum of money representing defendant's proportionate part of the cost of drilling and completing a unit well. After the well was drilled by plaintiff, the defendant applied for the creation of a compulsory drilling and production unit which was created and established, including a portion of lands held under lease, by defendant.[177] The issue presented was stated by the court as follows:

> Plaintiff contends it is entitled to recover the proportionate part of the adjusted well costs from the defendant in cash. To the contrary, defendant contends there is no authority for plaintiff to recover in cash, but only from the proceeds of production from the well accruing to defendant.[178]

The court stated it to be "obvious that, if [defendant]'s contention is maintained, it will have obtained a substantial advantage over [plaintiff-operator], in that the well satisfies its obligation to its lessor to develop and that it will ultimately receive its share of the proceeds thereof, all without the outlay of one penny."[179] Further, the court made the following cogent observation, to-wit:

> The suggestion that payment will ultimately be made from proceeds of production is not an answer to this situation, as [plaintiff-operator] will then be required to finance [defendant] during the entire time required to obtain reimbursement from proceeds of production. In short, [plaintiff-operator] alone will have been required to make the entire investment, whereas the return will accrue only partly to it, and partly to [defendant].[180]

The court in *Superior v. Humble* rejected defendant's contention that the Supreme Court in *Hunter Co. Inc. v. McHugh*[181] had "establish[ed] the rule that withholding the proceeds from the production of a well is the only method the driller of a unitized well may recover the proportionate cost of drilling from the owners included in the unit."[182] The court stated that *Hunter*, while recognizing the operator's right to withhold proceeds of unit production as a means of recovering well costs attributable to a unit participation, "did not . . . make this remedy exclusive."[183]

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177. *Id.* at 906–07.
178. *Id.* at 907.
179. *Id.* at 908.
180. *Id.*
181. Hunter Co., Inc. v. McHugh, 11 So. 2d 495 (La. 1942).
182. *Superior Oil Co.*,165 So. 2d at 908.
183. *Id.* at 909.

An interesting, if not humorous, sidebar was the argument by defendant, the corporate predecessor to today's ExxonMobil Corporation, that "a poor and impecunious owner may be subjected to heavy costs he is unable to pay if required to pay cash in the hope of continued production."[184] The court gave short shrift to this argument, noting that the issue "cannot be considered until the answer of defendant and the trial discloses whether or not defendant is impecunious and why it initiated the unitization by the Commission."[185]

In denying an application for rehearing, the court stated that its "decision at this time is limited to the case where the non-drilling owner and/or lessee has demanded the unitization, and no further."[186]

The rationale of the court in the *Superior v. Humble* case was further explained in its denial of rehearing as follows:

> To compel an owner and/or his mineral lessee to share the production from their well with the adjoining unitized owners and/or mineral lessees, without requiring immediate payment of the latters' pro rata cost of drilling and production, but limiting recovery solely from the adjoining owners' pro rata of production would, in effect, be unjust enrichment of the latter and the taking of property of the producing owner or lessee for the gain of the adjoining owners or lessees without adequate compensation. . . . In such case the producing owner and/or his lessee would be compelled to assume the entire risk of production, and the financing of the pro rata cost that should be borne by the non-drilling unitized adjoining owners and/or lessees.[187]

This right of the operator to be reimbursed as to monies expended for the benefit of another party who has not contributed to the cost, risk, and expense of drilling a unit will is paramount and has been called a "prior right to the proceeds."[188]

Following the decision in the *Superior v. Humble* case, it was unclear as to what actions on the part of the nonparticipating owner would be considered as sufficient to invoke the rule, exposing it to personal liability

184. *Id.* at 910.
185. *Id.*
186. *Id.* at 911.
187. *Id.* at 910–11.
188. *See* Scurlock Oil Co. v. Getty Oil Co., 344 So. 2d 1134, 1137 (La. Ct. App. 3d Cir. 1977) ("The party drilling the well, here Bauman, had the right under LSA-R.S. 30:10(A)(1)(c) and Hunter Co. v. McHugh, . . . to retain or receive the well proceeds until his well costs were paid and Waterbury therefore had no prior right to the proceeds.").

to the operator for its proportionate part of unit well costs. If the nonparticipating owner actually made application for the unit to *force* itself into the operator's production, that was the easy case. But what if the nonparticipating owner—while not actually applying for the unit—offered a counterplan or presented testimony or made a statement in reference to an application filed by the operator? Would this be sufficient?

The next case to explore the reach of this stated limitation was *Davis Oil Co. v. Steamboat Petroleum Corp.*,[189] in which Davis, owner of certain leases, filed an application with the Office of Conservation to form units for wells to be drilled by plaintiff. Defendant, as the adjacent lessee, filed a counterplan that opposed the Davis plan and urged the Commissioner to adopt defendant's unitization plan. The Commissioner's unitization order established two units, each of which included small parts of lands leased by defendant. Plaintiff drilled a well in each unit, both of which were dry holes. The defendant refused to participate in drilling of each well, and the operator submitted invoices to the defendant for its proportionate share of unit drilling costs. When the defendant refused to pay, plaintiff filed a suit against the defendant for a money judgment representing a proportionate part of costs incurred by plaintiff in the drilling of wells in the units that contained defendant's leases.[190]

The Supreme Court held that the defendant was not personally liable for unit well costs, stating as follows:

> Under the circumstances of the present case, in which the non-operating lessee merely introduced a counter-proposed unit plan at the Commissioner's hearing, prior to the drilling of the dry holes, only as a precaution against the uncompensated drainage of part of the land underlying its leases, the lessee did not consent to the unit operations.[191]

Hence, the Court established that a "non-operating owner of a mineral interest, who does not consent to operations within a compulsory drilling unit by an operating owner, has no liability for the costs of development and operations except out of his share of production."[192]

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189. Davis Oil Co. v. Steamboat Petroleum Corp., 583 So. 2d 1139 (La. 1991).
190. *Id.* at 1141.
191. *Id.*
192. *Id.* at 1143.

3. Cost Responsibility of a Unitized Tract That Becomes Unleased After Release or Expiration of Mineral Lease

Where costs are incurred during the existence of a mineral lease and are in fact paid by the lessee to the operator, but the mineral lease terminates prior to recoupment of such costs by the lessee, special issues arise.

The attributes of an unleased mineral owner—his rights and plights—are not different merely because he was previously leased.[193] As the district court judge in *Browning v. Exxon Corp.* stated,[194] an "expired mineral lease is just that, an expired lease. It is as though the Browning lease had never been written. The Louisiana statutes contain no exemption for 'recently leased, but now unleased, lands.'"[195]

These special issues were addressed in *Williams v. Seneca Resources Corp.*[196] In *Williams*, the plaintiffs' lessee, Yuma, entered into an operating agreement with Seneca, pursuant to which a well was drilled and then unitized. Yuma paid to Seneca, the operator, the share of well costs applicable to the lands covered by the Williams lease. After completion, the well was shut-in for lack of a pipeline connection. Apparently, Yuma failed to make a timely shut-in rental payment as required by the lease, which thereupon terminated. After production began, Seneca, as operator, withheld proceeds allocable to the Williams tract in order to reimburse Yuma, the Williams's former lessee. Williams sued Seneca to establish that Seneca had no right to withhold proceeds of unit production allocable to the (unleased) Williams's tract.[197]

Noting that "the costs associated with the Williams' tract have been paid already by Yuma,"[198] the court found that "Seneca does not have the right to collect the development costs incurred during the Lease from the Williams."[199] The court recognized that because the lease was in force and effect during the period of time that the well costs were incurred, it was the responsibility of Yuma, the lessee, to bear those costs.

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193. Except, of course, to the extent that the (now) unleased mineral owner has a claim against the (former) mineral lessee which has not prescribed.

194. Browning v. Exxon Corp., 848 F. Supp. 1241 (M.D. La. 1994).

195. *Id.* at 1247 (footnote omitted).

196. Williams v. Seneca Res. Corp., No. CIV. A. 91-832, 1991 WL 264562 (E.D. La. Dec. 4, 1991).

197. *Id.* at *1.

198. *Id.* at *2.

199. *Id.*

These issues were next visited in *Shanks v. Exxon Corp.*[200] Exchange Oil & Gas Corporation held a mineral lease on a tract of land which was subsequently placed in a unit around a well, as a result of which obligations accrued for the payment of well costs to Exxon, the operator of the well.[201] Because there was no contractual relationship between Exchange and Exxon, the latter withheld the proceeds of production attributable to Exchange's unitized premises to recoup that tract's proportionate share of well costs.[202] Exchange paid royalties out-of-pocket to its lessors for some period of time until it made the decision that the well would not pay out and elected to simply release the lease to be relieved of any further responsibility in connection therewith.[203] Since that previously leased tract's share of well costs had not yet been fully recouped by the operator, Exxon continued withholding such costs from the post-release share of production now owned by the plaintiffs (Exchange's former lessors) in their capacity as unleased mineral owners.[204]

The plaintiffs sued TXP (as successor to Exchange's interest in the lease) for such well costs, arguing that such costs were incurred during the existence of the lease and, therefore, were and remained the responsibility of the lessee.[205] TXP defended by asserting that it was relieved of this responsibility prospectively from the date of the release.[206] TXP argued that, since Exxon could only recoup such funds by withholding production attributable to the tract in question, the obligation arose only as and to the extent that production was actually obtained, and, therefore, it had no personal obligation to continue paying for such well costs after the release.[207]

The court agreed with TXP and found that the release of the lease resulted in the discharge of the (former) lessee's further obligations in connection therewith, including those dealing with well costs.[208] The court further explained its rationale as follows:

> While the factual situation in *Davis* [*Oil Co. v. Steamboat*

200. *See* Shanks v. Exxon Corp., 674 So. 2d 473 (La. Ct. App. 1st Cir. 1996) [hereinafter *Shanks I*].
201. *Id.* at 474.
202. *Id.*
203. *Id.*
204. *Id.*
205. *Id.* at 475.
206. *Id.*
207. *Id.*
208. *Id.* at 478.

> *Petroleum Corp.*[209]] differed from the facts herein, we believe that the pronouncements therein are nonetheless controlling. Applying the dictates of *Davis*, we conclude that liability for well costs does not necessarily accrue at the time the costs are incurred. Moreover, even the inclusion of the leased lands at issue within the compulsory unit did not, of itself, render TXP liable for well costs. Pursuant to *Davis*, TXP had no liability for well costs, but was only liable for such costs out of production. TXP's liability for well costs accrued only as there was production from the unit well and only to the extent of its proportionate share of production. TXP's, or Exchange's, entire proportionate share of production was applied to the payment of well costs during the existence of the leases. Thus, we conclude that TXP paid all well costs for which it was liable by law.[210]

The identical set of facts as was considered in *Shanks I* gave rise to another decision in the same case against another defendant. In *Shanks v. Exxon Corp.*,[211] the plaintiff sought relief against C. T. Carden, the original lessee who later assigned the lease to Exchange, which interest was later assigned to TXP. [212] "Because the principal defendant in this matter was TXP, all of the parties agreed to sever their claims against Exxon and the Cardens, both as to the original claim and the incidental claims."[213] *Shanks II* took up the previously severed claim against Carden.[214]

After its claims against TXP were dismissed in *Shanks I*, the plaintiffs pursued their original lessee, C. T. Carden. The character of the plaintiffs' claim against this defendant was stated as follows:

> Plaintiffs then filed the instant appeal, contending that the trial court erred in: (1) holding that "the issues presented are the same" in this case against mineral lessee Carden as in the case of sublessee TXP in the earlier trial as reported in *Shanks [I];* (2) finding that "this situation has already been dealt with by this court and by the 1st Circuit" and failing to recognize the distinction between the personal, contractual liability of the mineral lessee, Carden, to plaintiff-lessors for payment of well drilling costs and

209. Davis Oil Co. v. Steamboat Petroleum Corp., 583 So. 2d 1139 (La. 1991).
210. *Shanks I*, 674 So. 2d at 477.
211. Shanks v. Exxon Corp., 984 So. 2d 53 (La. Ct. App. 1st Cir. 2007) [hereinafter *Shanks II*].
212. *Id.* at 55.
213. *Id.*
214. *Id.*

> the limited, in rem liability of sublessee TXP, as decided in *Shanks [I]* on the basis of oil and gas unitization law; and (3) failing to recognize and apply the provisions of the Mineral Code in that the lessee-sublessor Carden "is not relieved of his obligations or liabilities under a mineral lease unless the lessor has discharged him expressly and in writing," LSA-R.S. 31:129, as distinguished from a sublessee who assumed only an in rem interest in the lease and whose responsibility to the lessor is limited "to the extent of the interest acquired," LSA-R.S. 31:128.[215]

The court stated the issue in *Shanks II* to be as follows:

> Thus, as was the case in *Shanks [I]*, the primary issue now before us is when liability for well costs, incurred for a well drilled on someone else's property prior to unitization, becomes chargeable to an owner (or lessee) who did not consent to unitization or to the drilling activities of the operating owner.[216]

Holding to its determination in *Shanks I* that the obligation of a non-consenting owner to pay well costs only arises as and when—and to the extent that—production is captured and reduced to possession, the court in *Shanks II* rejected plaintiffs' demands against Carden, saying as follows:

> Inasmuch as liability for the remaining unpaid well costs attributable to the tracts of land covered by the leases was a **future** obligation, *i.e.,* a liability only incurred as the unit well produced and only to the extent of the proportionate share of production, Carden was relieved of this future obligation by execution of the release in accordance with the provisions of the leases.[217]

4. Legislative Remedy to Address the Free Rider

In Louisiana, the practice of free riding was essentially unrestrained or unfettered prior to January 1, 1985. Before adoption of the Risk Fee Act,[218] and as noted by the Louisiana Supreme Court in the *Davis v. Steamboat* case, it was the established law that an owner in a compulsory unit had no personal, out-of-pocket responsibility for costs of drilling a

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215. *Id.* at 56.
216. *Id.* at 58.
217. *Id.* at 60 (citing *Shanks I*, 674 So. 2d 473, 478 (La. Ct. App. 1st Cir. 1996)).
218. Act No. 345, 1984 La. Acts 929.

unit well in the absence of expressly consenting to have such personal responsibility. At the time of adoption of this legislation, *owner*, for purposes of Louisiana's Conservation Act, was defined as "the person, including operators and producers acting on behalf of the person, who has the right to drill into and to produce from a pool and to appropriate the production either for himself or for others."[219]

At the same time, a landowner (or mineral servitude owner) had no duty to grant a mineral lease and could elect to hold out and not facilitate the drilling by another.[220] The operator could nonetheless drill the well and assume all responsibility for the cost, risk, and expense of such venture.

If the well was successful, the operator had the right to withhold *all* revenue attributable to the share of unit production allocable to the free rider until the operator recouped the free rider's share of the cost of drilling, testing, completing, equipping, and operating the unit well.[221] However, upon achievement of payout, the free rider was due its share of production (called "8/8ths"), subject to bearing its proportionate share of current operating expenses. While there is no statutory definition of *payout* for purposes of the Conservation Act, industry custom and usage would deem *payout* to have been achieved when the operator has been reimbursed the costs of drilling, testing, completing, equipping, and operating the unit well out of production.

As previously noted,[222] the courts have recognized that the potential of the operator eventually being reimbursed out of production can be a hollow remedy. After several unsuccessful attempts to enact a legislative

219. LA. REV. STAT. ANN. § 30:3(8) (2022).

220. *See* Ark. Fuel Oil Corp. v. Weber, 149 So. 2d 101, 108 (La. Ct. App. 2d Cir. 1963) (recognizing that the "right of an owner to refrain from exercising his right of ownership is absolute"). *See* OTTINGER, MINERAL LEASE TREATISE, *supra* note 1, § 4-25(d)(4)(ii).

221. LA. REV. STAT. ANN. § 30:10A(2)(b)(i) (2022).

222. The Superior Oil Co. v. Humble Oil & Refining Co., 165 So. 2d 905, 908 (La. Ct. App. 4th Cir. 1964).

solution to the problem of free riding,[223] the legislature finally enacted what is now called the Risk Fee Act in 1984.[224]

In many respects, the structure of the legislation mimics the contractual regime for the conduct of subsequent operations under a Model Form Operating Agreement.[225] To be sure, the Risk Fee Act is a very comprehensive enactment of immense importance to the drilling of a well for a compulsory unit in which disparate, non-contractually related interests exist. It is impossible to dissect each and every aspect of the Act, and the reader is invited to examine prior commentary on this important legislation.[226]

In summary, as adopted, the Risk Fee Act established a mechanism whereby an operator desiring to drill a unit well may call upon all other owners in the unit by certified mail to make an election to participate or not in the cost, risk, and expense of the well.[227] The notified party has 30 days to respond to the operator's notice.[228] Should a notified party fail to affirmatively elect to share in these costs, the operator is entitled to withhold—in the normal, historic fashion—all proceeds allocable to the interest of the nonparticipating party until payout is achieved.[229]

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223. A presenter at the 1985 Mineral Law Institute commented on one of the "significant statutes" enacted in 1984, saying:

> There is one in particular which had been pushed for passage by many in the industry for the past three or four years and which was finally passed last session, albeit not in the form originally sought, but in one that at least represents a major change in Louisiana law.

James H. Napper II, *Recent Developments in Legislation*, 32 ANN. INST. ON MIN. L. 317 (1985).

224. Notably, the legislation, which now reposes in Subsections 10A(2)(a)–(i) [exclusive of §§ (2)(f) and (g), later discussed at *infra* Part IV.F], does not utilize the term "risk *fee*" but characterizes the recoupment factor that an operator might, in a proper case, impose as a "risk *charge*." LA. REV. STAT. ANN. § 30:10A(2)(a)–(c), (e), (g)–(i), (C) (2022).

225. *See* Patrick S. Ottinger, 63rd Annual Institute on Oil and Gas Law: Chapter 7: Be Careful What You Ask For: Subsequent Operations Under the Model Form Operating Agreement, at the Center for American and International Law (2012).

226. *See* discussion *supra* note 1.

227. As noted and explained in note 4, *supra*, the provisions of the Risk Fee Act only pertain to drilling and production units established pursuant to Louisiana Revised Statutes § 30:9(B) and by explicit statutory reference to ultra-deep structure units authorized by § 30:5.1B.

228. LA. REV. STAT. ANN. § 30:10A(2)(a)(ii) (2022).

229. *Id.* § 30:10A(2)(b)(i).

Additionally, the operator may assess a risk charge, being a stated percentage of such party's share of the costs of drilling, testing, and completing the unit well; the risk charge does not apply to costs of equipping and operating the well. This risk charge was originally set at 100% and was increased in 2008 to 200% of such costs.[230]

Other amendments have been made to the Risk Fee Act, including an amendment in 2012 to expand the provisions of the Act to a substitute unit well, an alternate unit well, or a cross-unit well.[231] However, the risk charge is 100% with respect to an alternate unit well or cross-unit well that will serve as an alternate unit well. Additionally, the mode of transmittal was changed from *certified* mail to *registered* mail.[232]

Importantly, under no circumstance may the operator assess a risk charge to an unleased mineral owner. Louisiana Revised Statutes § 30:10A(2)(e)(i) now states expressly that the provisions of the Act "with respect to the risk charge shall not apply to any unleased interest not subject to an oil, gas, and mineral lease."[233]

After the enactment of the Risk Fee Act but prior to 2012, the free rider was nevertheless obligated to pay royalties to its own lessor even though it received no revenue out of the well prior to payout.[234] This accommodation, of course, constituted a disincentive to a party to avoid participating in the drilling of the unit well, as it would be required to pay its lessor royalty out-of-pocket.

In 2012, controversial amendments were made to the Risk Fee Act that removed that disincentive by requiring the operator to pay over to the free riding lessee the necessary amount of proceeds in order that its lessor royalty would be paid. This amendment overturned a century of jurisprudence as outlined above.[235] This newly imposed requirement had the result of diminishing the revenue stream to which an operator was entitled, thus delaying payout. The reversal of the former entitlement was not well received by the industry.

After 2012, the legislature in 2016 adopted Senate Resolution No. 31 to study the Risk Fee Act, particularly as it pertains to the new requirement that an operator must pay over to a free rider the proceeds for payment of

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230. Act No. 115, 2008 La. Acts 1176.

231. LA. REV. STAT. ANN. § 30:10A(2)(a)(i) (2022).

232. Act No. 743, 2012 La. Acts 3030.

233. LA. REV. STAT. ANN. § 30:10A(2)(e)(i) (2022).

234. Gulf Explorer, LLC v. Clayton Williams Energy, Inc., 964 So. 2d 1042 (La. Ct. App. 1st Cir. 2007). *See* OTTINGER, LOUISIANA MINERAL LEASE, *supra* note 1, § 4-25(d)(4)(iii).

235. Act No. 743, 2012 La. Acts 3030. *See* Ottinger, *It's a Risky Business*, *supra* note 1, at 77–84.

the lessor's royalty. The Resolution tasked the Louisiana State Law Institute (LSLI) to undertake this study, and the LSLI formed the Risk Fee Act Committee for that purpose.[236]

After delays caused by the COVID-19 pandemic, this author, on behalf of the Committee, submitted a report which the Council of the LSLI adopted in December 2020 and thereafter sent to the legislature for its consideration. Introduced as Senate Bill No. 59 of 2021, it was converted during the legislative session to yet another study resolution,[237] and a Risk Charge Commission was formed.[238] The Commission rendered a report after conducting extensive studies and debates over several months. The recommendations of the Commission were introduced as Senate Bill No. 38, which was unanimously adopted, resulting in Act No. 5 of the 2022 legislative session, effective August 1, 2022.[239]

The new legislation amended the Louisiana Risk Fee Act in several respects, with the result that the scope and coverage of the legislation has been extended. The following is an excerpt from the author's Article in the *Pipeline Blog* titled "The 'Free Rider' in Louisiana—the 'Louisiana Risk Fee' Act" regarding the 2022 Amendments:

> The new legislation amended the Risk Fee Act in many respects, clarifying existing inconsistencies and adding new beneficial features to both the "drilling owner," as well as to the lessor of a nonparticipating owner. The following is a "high level" summary of the salient provisions now incorporated into the Act as a result of the 2022 legislation.
>
> The 2022 legislation addresses textual uncertainties in the original legislation by defining the terms "risk charge notice" (a written notice to "all other owners in the unit of the drilling or the

236. The Louisiana State Law Institute was formed by the Louisiana legislature. LA. REV. STAT. ANN. § 24:201 (2022). Its purpose is "to promote and encourage the clarification and simplification of the law of Louisiana and its better adaptation to present social needs, to secure the better administration of justice, and to carry on scholarly legal research and scientific legal work." *Id.* § 24:204. It operates through a number of committees with jurisdiction of particular matters, and its membership is composed of lawyers, judges, and law professors. In the interest of full disclosure, this author served as Reporter of this Committee.

237. The Risk Charge Commission was created by Senate Concurrent Resolution No. 44 of 2021 "to study and make recommendations regarding the costs and risks in drilling a well in a compulsory unit created by the office of conservation." S. Con. Res. 44, 47th Reg. Sess. (La. 2021).

238. In the interest of full disclosure, this author served as Vice-Chair of this Commission.

239. Act No. 5 (Aug. 1, 2022).

intent to drill," giving "each owner an opportunity to elect to participate in the risk and expense of such well") and "lessor royalty."

The Risk Fee Act now authorizes the "drilling owner" issuing a risk charge notice to include a "cash call." If a cash call is included in the risk charge notice, then, in order to avoid the imposition of a risk charge, the party affirmatively electing to participate in the proposed operation must also advance its share of costs as estimated in the AFE required to accompany the risk charge notice. So as to ensure that the costs estimated in the AFE are reasonably current and accurate, the AFE "shall be dated within one hundred twenty days of the date of the mailing of the risk charge notice." As the costs advanced are only an estimate, the 2022 legislation contains a provision for a "true up" of estimated v. actual costs of the operation, to be accomplished "within sixty days of receipt of detailed invoices in order to account for the difference between any cost estimates and actual costs."

If the well proposed by a risk charge notice is not commenced within ninety days of receipt of the initial risk charge notice, the drilling owner must send a supplemental notice in order for the provisions of the Act to apply.

As previously noted, amendments to the Risk Fee Act in 2012 imposed a new (and controversial) duty on the part of the operator to pay over to the nonparticipating party the amount of royalties to which its lessor is entitled. The scope and nature of this duty was clarified in 2022 to require the nonparticipating party to provide to the "drilling owner" (typically, the operator) certain specified information, including a copy of the relevant mineral lease (which may be redacted provided it includes those lease provisions pertaining to the calculation of royalty) and a "sworn statement of ownership." In its discretion, the nonparticipating owner may also provide a copy of any title opinion in its possession. The operator is authorized to procure a title opinion on the lands burdened by the mineral lease held by the nonparticipating owner, and charge the costs thereof to the tract in question.

These new deliverables are important because it is often the case that the operator has not examined title to any tract in which it owns no interest and, thus, might not have any basis to calculate the royalty to which the lessor of the nonparticipating party might be entitled. The royalty to be paid over by the "drilling owner" to the nonparticipating party is to be calculated and paid in

accordance with the terms of the relevant mineral lease. Although Louisiana law permits parties to file for registry, in lieu of the actual mineral lease, a memorandum or extract of lease to serve as public notice to third parties, the statute authorizing the filing of this simple instrument does not require that it include the royalty to which the lessor is entitled, and certainly not the lease terms pertinent to the calculation of the lessor's royalty. Hence, the operator—having no interest in the land or lease in question—is unaware of the amount of the royalty or of any contractual provisions relative to the computation thereof. By way of example, if the nonparticipating lessee's mineral lease contains a "No Deductions Clause," which contractually disallows the assessment of "post-production costs" against the lessor's royalty, that provision must be honored in the computation of the lessor's royalty. While not explicitly addressed, the lessee's interest in the tract should remain responsible for these costs *vis-à-vis* the operator.

The Act explicitly negates any presumption or contention that it creates a relationship between the operator and the lessor of the nonparticipating party, and does not relieve the nonparticipating party from its obligations under its lease to its own lessor. Further, the operator is to be indemnified by the nonparticipating party with respect of royalties paid by the operator in reliance on the information provided by the nonparticipating party. The 2022 legislation also introduces a "notice of change of ownership" feature that creates a safe harbor for the operator to continue to pay royalties unless and until it is notified of a change in ownership of the land or minerals giving rise to the royalties being paid over to the nonparticipating party for the benefit of its lessor.

Provisions comparable in nature to those features dealing with the payment of the lessor's royalty are also contained with respect to any overriding royalty burdens of the nonparticipating owner. An important distinction is that there is a cap on the amount of the overriding royalty burdens for which the "drilling owner" is duty-bound to pay over to the nonparticipating owner. It is only required to pay over the "lesser of: (I) the nonparticipating owner's total percentage of actual overriding royalty burdens associated with the existing lease or leases which cover each tract attributed to the nonparticipating owner reflected of record at the time of the risk charge notice; or (II) the difference between the weighted average percentage of the total actual lessor royalty and overriding royalty burdens of the drilling owner's leasehold

within the unit and the weighted average percentage of the total actual lessor royalty of the nonparticipating owner's leasehold within the unit reflected of record at the time of the risk charge notice." While admittedly "wordy," this mechanism is intended to avoid any concern or possibility that the nonconsenting owner would endeavor to "game the system" by creating an unreasonably excessive overriding royalty to an affiliated entity for which the "drilling owner" would be liable to pay over proceeds.

A lessor under a mineral lease held by a nonparticipating owner who has not received its lessor royalty may invoke the remedies of the Louisiana Mineral Code relative to unpaid royalty. However, the procedure is expanded to include the requirement that any notice of non-payment must include a copy of the relevant mineral lease.

Importantly, the provisions of the Risk Fee Act have been extended to "subsequent unit operations." The term is defined in the legislation, as are the various types of activities or operations coming within the ambit of that term. A proposal to conduct a "subsequent unit operations" is issued in the same manner and form as a proposal to drill an initial well, with different set of enumerated information to be included.

If the "subsequent unit operation" is proposed at a time when the notified party is subject to an outstanding, and unsatisfied, risk charge arising out of a prior operation in which it went non-consent, the "drilling owner" can require the notified owner to "come current" on the prior expenditures (and risk charge) as a prerequisite to participation in the proposed "subsequent unit operation" so as to avoid the imposition of a further risk charge associated with that "subsequent unit operation." The risk charge for such an operation is 100% "of the tract's allocated share of the actual reasonable expenditures incurred in conducting the subsequent unit operation, including a charge for supervision, regardless of whether the wellbore on which such operations were conducted is a unit well, alternate unit well, substitute unit well, or cross-unit well."[240]

240. Ottinger, *The "Free Rider" in Louisiana—the "Louisiana Risk Fee Act,"* *supra* note 1.

5. Jurisprudence Under the Louisiana Risk Fee Act

A significant decision involving the Risk Fee Act arose out of a dispute between an operator and a lessee in the Haynesville Shale.[241] In *Jones Energy Co. v. Chesapeake Louisiana, L.P.*,[242] Chesapeake, as operator of ten units, sent a series of letters to Jones, a lessee, proposing the drilling of wells on such units.[243] The court determined that "Jones Energy affirmatively elected to participate in the drilling of each of the ten wells, received invoices for its pro rata share of expenses for each of the ten wells, yet failed to pay within 60 days of receipt as required under the statute."[244] Jones filed suit to secure a judicial declaration that it "should be considered an 'owner not notified' despite its affirmative election to participate and subsequent failure to pay its proportionate share."[245]

The basis of Jones's suit was that the notices sent by Chesapeake were allegedly insufficient under the statute. The precise basis of the contention was not explained in the reported decision, but the court found that "Chesapeake substantially complied with the notice requirements of 30:10 because Jones Energy received most, if not all, of the information required under the statute."[246] The court then noted as follows:

> The statute is not intended to allow an owner to elect to participate and then sit aside to discern whether a well is producing or not, and if so, attack the operator's notice with the hope that a Court will construe the statute so strictly that they will be deemed an "owner not notified." Such a holding would allow an owner to reap all of the lucrative benefits of drilling without any of the inherent risk of such a venture. In finding that Chesapeake's notice letters substantially complied with the language and spirit of 30:10, this Court noted that Jones Energy is a sophisticated owner who repeatedly elected to participate without seriously questioning the contents of the notice letters. The equities in this case lie with Chesapeake.[247]

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241. Kennedy v. Saheid, 209 So. 3d 985, 994 n.3 (La. Ct. App. 2d Cir. 2016) ("This court would take judicial notice that March 2008 marked the beginning of the land-leasing boom associated with the Haynesville Shale formation.").
242. Jones Energy Co. v. Chesapeake La., 873 F. Supp. 2d 779 (W.D. La. 2012).
243. *Id.* at 782–83.
244. *Id.* at 785.
245. *Id.*
246. *Id.* at 785–86.
247. *Id.* at 786.

Three aspects of the ruling deserve examination. First, the court considered "whether Jones Energy is personally liable for the amount it owes to Chesapeake (inclusive of the 200% risk-fee) or whether Chesapeake is limited to recovering the amount *in rem* from production of the subject wells."[248]

After analyzing the issue, the court ruled as follows:

> Upon due consideration, the Court concludes that any collection of Jones Energy's pro-rata share and risk-fee charge must be taken *in rem* from production. Further, the collection *in rem* should be credited to each well from the proceeds of that specific well. The statute refers to the drilling unit well in the singular form, and the Court does not interpret the statute to allow production revenues from one unit well to pay for the costs associated with a separate unit well.[249]

Next, the court took up Jones's complaint that the filing by Chesapeake of privileges under Louisiana Revised Statutes §§ 9:4881–4889[250] constituted a violation of the Unfair Trade Practices and Consumer Protection Law.[251] The court rejected this argument saying:

> Chesapeake had a valid reason to file liens against the subject wells, and only took such action after Jones Energy repeatedly failed to remit payment to Chesapeake for its pro rata share of expenses after electing to participate in the drilling of the subject wells. Chesapeake's decision to file the liens was merely the result of prudent business judgment to protect its interests using a legally available avenue.[252]

This ruling is somewhat curious in view of the intrinsic element that an operator can assert a privilege over a non-operator's interest "to secure payment of all obligations incurred in the conduct of operations which the non-operator is *personally bound to pay or reimburse*."[253] Hence, the court's holding "that any collection of Jones Energy's pro-rata share and risk-fee charge must be taken *in rem* from production" would seem to disallow any resort to the privilege statute on which the operator relied.

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248. *Id.*
249. *Id.* at 788.
250. *See* OTTINGER, MINERAL LEASE TREATISE, *supra* note 1, § 12-14.
251. LA. REV. STAT. ANN. §§ 51:1401–1418 (2022). *See* OTTINGER, MINERAL LEASE TREATISE, *supra* note 1, § 13-08(h).
252. *Jones Energy Co.*, 873 F. Supp. 2d at 788.
253. LA. REV. STAT. ANN. § 9:4882A (2022).

Finally, the court's treatment of a statute that should be subject to the principle of strict construction seems to relax that relevant test to some degree.[254] The court stated that the "risk-fee statute is to be liberally construed in favor of the owner operator because it is the owner and operator who initially shoulders the expense and risk of drilling the unit well,"[255] and it also found that the sufficiency of the operator's notice was subject to a standard of *substantial compliance*, seeming to again depart somewhat from principles of strict construction. The notion of *substantial compliance* seems fundamentally incompatible with the principle of *strict construction*.[256]

6. Operator's Paramount Right of Recoupment with Respect to a Mineral Royalty Burdening an Unleased Mineral Interest

If the interest of an unleased mineral owner is burdened by a mineral royalty,[257] does the operator have any different obligations to pay royalties to that mineral royalty interest owner prior to payout? This author suggests that the answer is "no."

As heretofore explained in greater detail, the language in the Risk Fee Act that imposes this new duty on the part of the drilling owner refers to "that portion of production due to the lessor royalty owner under the terms of the contract or agreement creating the royalty between the royalty owner and the nonparticipating owner."[258] The mineral royalty owner is

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254. "It is the universally recognized rule of law that statutes imposing penalties must be strictly construed and every doubt must be resolved against the imposition of the penalty." Tichenor v. Tichenor, 181 So. 863, 864–65 (La. 1938). *See also* White v. Phillips Petroleum Co., 232 So. 2d 83, 90 (La. Ct. App. 3d Cir. 1970) ("This is a penal statute, requiring strict construction.").

255. *Jones Energy Co.*, 873 F. Supp. 2d at 786.

256. *Cf.* Inexco Oil Co. v. Crutcher-Tufts Corp., 389 F. Supp. 1032, 1040 (W.D. La. 1975) ("[I]n Louisiana, the doctrine of 'substantial compliance' is *limited to construction contracts* and is not appropriate or pertinent to a contract such as a farmout agreement." (emphasis added)).

257. A *mineral royalty* is defined in article 80 of the Louisiana Mineral Code as follows:

> A mineral royalty is the right to participate in production of minerals from land owned by another or land subject to a mineral servitude owned by another. Unless expressly qualified by the parties, a royalty is a right to share in gross production free of mining or drilling and production costs.

LA. REV. STAT. ANN. § 31:80 (2022). *See* OTTINGER, *supra* note 175, *in* LOUISIANA MINERAL LAW TREATISE, *supra* note 18.

258. LA. REV. STAT. ANN. § 30:10A(2)(b)(ii)(aa) (2022).

not a *lessor royalty owner*, and its rights are not created "under the terms of the contract or agreement . . . between the royalty owner and the nonparticipating owner."[259] Rather, a mineral royalty is created in the first instance by a landowner by grant or reservation and not by or out of the mineral lease that is the source of the royalty interest to which the *lessor royalty owner* is entitled.[260] Importantly, the unleased mineral owner is not subject to the Risk Fee Act, as the "provisions of [the Act] with respect to the risk charge shall not apply to any unleased interest not subject to an oil, gas, and mineral lease."[261]

A mineral royalty differs significantly in nature and function from a royalty reserved by a lessor under a mineral lease. The former is a prescriptible right and survives the termination of the mineral lease,[262] while the latter is reserved to the lessor under the mineral lease and terminates with the lease.[263] The Louisiana Supreme Court has recognized

> that a mineral right is necessarily superior to a royalty right. . . . Of these two rights it has been correctly said by one of the authorities on the oil and gas law of this state that the royalty right is but an appendage of the right of the mineral owner, and depends upon the continued existence of the right to which it is an appendage.[264]

Whatever might be the obligations of the mineral owner to the owner of the mineral royalty interest that the mineral owner has created,[265] the fact remains that, prior to payout, the operator has a paramount right to withhold the entirety of production allocable to the burdened tract until it has recovered its costs.[266] It would indeed be illogical if the operator has

259. *Id.* § 30:10A(2)(b)(ii)(aa).

260. *Id.* § 31:15.

261. *Id*. § 30:10A(2)(e)(i).

262. *Id.* § 31:85(1). *See* DAGGETT, *supra* note 32, § 61 ("[The mineral royalty] usually becomes ultimately attached to a lease, as few landowners are producers. But it does not have to have a *present* lease nor *need* it have an ultimate lease upon which to ground its being, because its interest is in the *production*, by whatever method that may be achieved.").

263. *See* LA. REV. STAT. ANN. § 31:213(5) (2022).

264. Cont'l Oil Co. v. Landry, 41 So. 2d 73, 75 (La. 1949).

265. "The seller is bound to *deliver* the thing sold and to warrant to the buyer ownership and peaceful possession of, and the absence of hidden defects in, that thing. The seller also warrants that the thing sold is fit for its intended use." LA. CIV. CODE ANN. art. 2475 (2022) (emphasis added).

266. "[T]he [operator] has had and will have possession of all of the proceeds from the production of the well and may retain all of the proceeds until the drilling

the right to recoup its costs out of an unleased mineral servitude—a superior right or interest—but not out of a mineral royalty interest (an inferior right or interest) created by such mineral servitude owner. Said differently, the right of the operator to withhold proceeds of production allocable to an unleased interest should not be diminished or rendered ineffectual by reason of the fact that the mineral owner created a mineral royalty interest. With the mineral royalty being inferior to the mineral servitude, it is illogical that the royalty owner would have a claim to entitlement of production when its creator has no such right.[267] Nothing in the 2012 amendments to the Risk Fee Act purports to alter this conclusion.

G. Unit Well Cost Adjustments

If, for a period of time, a well produces on a *lease basis* prior to unitization, or a unit well produces prior to a revision of the unit, and if, as a consequence of the unitization or re-unitization, a new or additional tract of land not under lease to the operator is included within the unit, the occasion arises for an adjustment of the unit well costs for which the newly added tract(s) of land will be responsible.

1. Preface

The rationale for the adjustment of unit well costs is that, while the owner of the newly added lease has the obligation to compensate the operator for the costs of the unit well which is now benefitting the new owner, the operator—having recovered some portion of the costs of drilling the unit well out of pre-unitization or pre-revision production—is only entitled to recover *adjusted* or *depreciated* well costs from the newly unitized lease owner.[268] Such an adjustment is customarily based upon a

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of the well and putting it on production is entirely paid for." Hunter Co., Inc. v. McHugh, 11 So. 2d 495, 509 (La. 1942).

267. If the unleased mineral owner is not entitled to receive production, it is self-evident that such an owner may not convey to a mineral royalty owner greater rights than he himself has. *See* Frost-Johnson Lumber Co. v. Salling's Heirs, 91 So. 207, 245 (La. 1922) ("[N]o one can convey to another any greater right than he himself has."); Herlitz Constr. Co., Inc. v. Matherne, 476 So. 2d 1037, 1040 (La. Ct. App. 3d Cir. 1985) ("An assignee acquires no greater rights than its assignor."). See OTTINGER, MINERAL LEASE TREATISE, *supra* note 1, § 2-9, for authority supporting the proposition that a party cannot grant, lease, or convey any greater rights than it holds or owns.

268. As cogently stated by Mr. Jorden, the "Commissioner's rulings which adjusted unit well costs for prior production were obviously intended to require that each owner pay only for that part of the life of the unit well that would be

determination of the percentage of the reserves produced by the operator prior to unitization or re-unitization.

2. *Methodology of Calculation*

There is no statutory law prescribing the proper methodology of adjusting well costs. However, certain practices or customs have evolved, which furnish an equitable basis for adjusting unit well costs—a depreciated unit well cost adjustment.[269] An illustration of the two competing models is as follows:

Operator drills a commercially successful well for $3 million; it produces 10,000 barrels of oil on a lease basis for a period of time before being unitized. The oil is sold for $80 per barrel, or $800,000 gross. The well is then unitized, and Hartman Energy's lease is brought into the unit, constituting 20% of the unit. Hartman contends that it is only responsible for 20% of $2,200,000 ($3,000,000 minus $800,000) because, according to Hartman's theory, the operator made $800,000 prior to unitization and thereby recouped that amount of its out-of-pocket well costs. Hartman's proposed approach is based upon a dollar-for-dollar methodology—the operator's out-of-pocket well costs have been reduced dollar-for-dollar to the extent of $800,000, the gross value of pre-unitization production.[270]

Operator argues for a depreciated well cost adjustment. The operator's reservoir engineer estimates the reservoir to have originally contained 2,000,000 barrels of oil. Thus, prior to unitization, operator produced .5% (10,000/2,000,000 = 1/200 = .5%) of the estimated reserves. Based upon this amount of production, the original well costs ($3,000,000) should be reduced in the same proportion as pre-unitization depletion of the reserves, or .5% times $3,000,000, or $15,000. Thus, under the operator's theory,

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used by such owner." Jorden, *Unit Well Cost Adjustment in Louisiana*, *supra* note 173, at 86.

269. The Council of Petroleum Accountants Societies (COPAS), *see* discussion i*nfra* notes 310–12, has promulgated Accounting Guideline 1 entitled *Well Cost Allocations and Adjustments*, described as a

> a guide to an equitable basis for determination of values to be used with well cost adjustments required as a result of ownership changes occurring as a result of expansion or contraction of a unit, recompletion of a well, multiple completions, completion of a well in a zone of different ownership, or creation of a field wide or reservoir unit.

COUNCIL OF PETROLEUM ACCOUNTANTS SOCIETIES (COPAS), ACCOUNTING GUIDELINE NO. 1 WELL COST ALLOCATIONS AND ADJUSTMENTS (Apr. 2003).

270. Hartman's position is that a "dollar-for-dollar" adjustment is authorized (if not compelled) by the decision in *Desormeaux v. Inexco Oil Company*, 298 So. 2d 897 (La. Ct. App. 3d Cir. 1974), to be discussed.

there is yet to be recouped $2,985,000 of well costs utilizing the depreciated well cost methodology. Operator contends that Hartman is responsible for 20% of $2,985,000 in well costs.

3. Statutory Provisions Addressing Disputes as to Unit Well Costs

Under the Conservation Act as initially enacted, the statute governing well cost determinations was Louisiana Revised Statutes § 30:10A(1)(c) which read, in pertinent part, as follows:

> In the event pooling is required, the cost of development and operation of the pooled unit chargeable by the operator to the other interested owners shall be limited to the actual reasonable expenditures required for that purpose, including a charge for supervision. In the event of a dispute relative to these costs, the commissioner shall determine the proper costs, after notice to all interested persons and a hearing.[271]

Additionally, recalling that § 10A(1)(a) tasks the Commissioner, in issuing unitization orders, to "afford the owner of each tract the opportunity to recover or receive his just and equitable share of the oil and gas in the pool *without unnecessary expense*,"[272] guard rails to implement the requirement that the only chargeable expenses are those that are *necessary* are contained in Louisiana Revised Statutes § 30:111, which reads as follows:

> Owners of unleased mineral interests and lessees in any drilling unit authorized by the department of conservation of this state, shall not be liable or obligated to pay to the operator or producer for materials furnished or used in the drilling, completion, and production of any oil, gas, or mineral well drilled on said unit a sum in excess of the prevailing market price of such materials.[273]

Notably, expenses that might be charged by an operator to other unit parties are limited to necessary expenses, which seems to constitute an acknowledgment that expenses that are incurred post-wellhead may be charged if they meet the standard of necessity.[274]

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271. LA. REV. STAT. ANN. § 30:10A(1)(c) (1983) (prior to subsequent amendments, and repeal by Act No. 345, 1984 La. Acts 929).

272. LA. REV. STAT. ANN. § 30:10A(1)(a) (2022).

273. LA. REV. STAT. ANN. § 30:111 (2017) (added by Acts 1950, No. 526).

274. As one Louisiana court has recognized, "The presence of gas at the wellhead is of no value until it is marketed and transported to the purchaser . . . . [P]roduction is futile without distribution of the product." Culpepper v. EOG Res.,

As noted, the statutes did not specifically state the method to be used in adjusting unit well costs for pre-unitization production, and, indeed, the statutes did not even make it clear as to whether such well costs should be adjusted at all. Louisiana Revised Statutes § 30:10A(1)(c) required only that the well costs and operating expenses chargeable by the unit operator to the non-operators "shall be limited to the actual reasonable expenditures required" to operate the unit, "including a charge for supervision"[275] (i.e., "administrative overhead").

4. Jurisprudence

In *Desormeaux v. Inexco Oil Co.*,[276] the Third Circuit Court of Appeals for Louisiana held that, where the operator had recovered its well costs out of production from the well prior to unitization, the unleased mineral owner was entitled to participate in unit production from the effective date of the unit without any responsibility for well costs out of production.[277] The trial court held that "the cost of the well prior to unitization could not be charged to the landowner since these costs had been recovered from the production prior to unitization," since, to hold otherwise (according to the court), the "operators of the unit would be recovering twice, once from the production and once from the landowner."[278] The appellate court affirmed and stated as follows:

> We believe this to be a just result. Inexco drilled the well on property of plaintiff which it had under lease. The fact the unitization order included some of plaintiff's unleased acreage did not impose any additional obligation or expense on Inexco. The cost of the well had been fully recovered prior to the time of unitization. The result advanced by defendant would allow it to recover its costs twice.[279]

The *Desormeaux* decision was widely considered an incorrect application of the law, limited to a unique factual situation, and was not

Inc., 92 So. 3d 1141, 1444 (La. Ct. App. 2d Cir. 2012). *See* OTTINGER, MINERAL LEASE TREATISE, *supra* note 1, § 4-25(d)(6)(viii)(D).

275. LA. REV. STAT. ANN. § 30:10A(1)(c) (1983) (prior to subsequent amendments, and repeal by Act No. 345, 1984 La. Acts 929).

276. Desormeaux v. Inexco Oil Co., 298 So. 2d 897 (La. Ct. App. 3d Cir. 1974).

277. *Id.* at 901.

278. *Id.*

279. *Id.*

well received by the industry. The fallacy in the court's rationale resides in this statement in the court's decision:

> Nor does the statute [Section 10] apply to the situation. The statute applies to separately owned tracts, not to a division of interests between the landowner and his lessee.[280]

The fact that the non-operator within the compulsory unit was also the lessor of the mineral lease owned by the unit operator should not have led the court to decide that the leased and unleased tracts within the unit were not *separately owned*, thus rendering Section 10 inapplicable. For purposes of the Conservation Act (particularly including Section 10), the leased and unleased tracts of land in the *Desormeaux* case were truly vested in two different *owners*. Thus, under the Conservation Act's definition of *owner*, Inexco was the *owner* of the leased tract on which the well was drilled, and Mr. Desormeaux was the *owner* of the unleased tract of land brought into the unit. Hence, the two *tracts* were *separately owned* within the intendment and contemplation of Section 10.

Subsequent to its amendment by Act No. 345 of the 1984 Louisiana legislature and prior to its amendment by Act No. 595 of the 1991 Louisiana legislature, Louisiana Revised Statutes § 30:10A(2)(d) provided as follows:

> [T]hat the cost of drilling, testing, completing, equipping, and operating the unit well shall be reduced to account for monies received from prior production, if any, in which said tract or tracts did not participate prior to determining the share of cost allocable to the subsequently included tract or tracts.[281]

The language employed in the 1984 statutory formulation was not precisely clear in that it is not certain as to what is meant by the statement that costs "shall be reduced *to account for*" revenue from prior production. Does this mean that the well costs must be reduced dollar-for-dollar, or might some other method of well cost adjustment be utilized, e.g., reservoir depletion?

There are two principal scenarios that give rise to the need and occasion to adjust unit well costs. First, if a unit is revised so as to include a new, additional tract of land, and next, when the unit is modified so as to exclude a tract that previously participated in unit production. Addressing these scenarios, Act No. 595 of 1991 amended § 30:10A(2)(d)

280. *Id.*
281. LA. REV. STAT. ANN. § 30:10A(2)(d) (1983).

by changing the phrase that the cost of drilling, testing, completing, equipping, and operating the unit well shall be "reduced to account for monies received from prior production" to "reduced in the same proportion as the recoverable reserves in the unitized pool have been recovered by prior production . . . ."[282]

The legislation also reconfigured the well cost adjustment provisions as Subsection (i) and added Subsection 10A(2)(d)(ii), which addresses the latter circumstance identified above (unit revision results in exclusion of a previously unitized tract of land).

Act No. 743 of 2012, as subsequently amended by Act No. 524 of 2016, set forth Subsections (i) and (ii) to § 30:10A(2)(d) so as to read as follows:

> (i) Should a drilling unit be revised by order of the commissioner so as to include an additional tract or tracts, then the provisions of this Subsection for notice, election, and participation shall be applicable to such added tract or tracts and the owner thereof as if a well were being proposed by the owner who had drilled the well; however, the cost of drilling, testing, completing, equipping, and operating the unit well shall be reduced in the same proportion as the recoverable reserves in the unitized pool have been recovered by prior production, if any, in which said tract or tracts did not participate prior to determining the share of cost allocable to the subsequently included tract or tracts.
>
> (ii) Should a drilling unit be revised by order of the commissioner as to exclude a tract or tracts, the cost of drilling, testing, completing, equipping, and operating the unit well shall be reduced in the same proportion as the recoverable reserves in the unitized pool have been recovered by prior production to determine the share of cost allocable to the subsequently excluded tract or tracts.[283]

5. Hearings Before the Commissioner of Conservation

In a series of Orders issued on August 22, 1990, the Commissioner of Conservation determined, in well cost hearings held pursuant to Louisiana Revised Statutes § 30:10A(2)(f), that the statutory language meant that "the actual reasonable cost . . . should be reduced by the dollar amount of monies received from the prior production in which the tract included in

282. Act No. 595, 1991 La. Acts 1913.
283. Act No. 743, 2012 La. Acts 3030.

the unit did not participate less severance tax, in determining the share of cost allocable to said tract."[284]

The Commissioner further found that "the dollar for dollar reduction to be required herein follows the guidance of LSA-CC Art. 9, and is consistent with the concept enunciated by the court in the case of Desormeaux v. Inexco Oil Co . . . ."[285]

Subsequent to these hearings, Louisiana Revised Statutes § 30:10A(2)(d) was amended in 1991 by Act No. 595 of the Louisiana legislature[286] to provide that

> the cost of drilling, testing, completing, equipping, and operating the unit well shall be reduced in the same proportion as the recoverable reserves in the unitized pool have been recovered by prior production, if any, in which said tract or tracts did not participate prior to determining the share of cost allocable to the subsequently included tract or tracts.[287]

H. Hearing to Determine Unit Well Costs

The Commissioner has authority to determine well costs if the parties cannot reach an agreement as to the proper amount of well costs for which a party might be liable. This determination is made after the holding of a public hearing.

1. Preface

If the parties are unable to reach agreement as to the amount of well costs chargeable to the newly unitized lease owner, the Commissioner of Conservation may determine the well costs.[288] In this regard, Louisiana Revised Statutes § 30:10A(2)(f) provides that "[i]n the event of a dispute relative to the calculation of unit well costs or depreciated unit well costs,

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284. *See* Louisiana Office of Conservation Order No. 860-1 (August 22, 1990) (effective July 12, 1990) (relative to the calculation of unit well costs for the GER RD SUA in the Iberia Field, Iberia Parish, Louisiana).

285. *See also id.* Concerning the calculation of proper unit well costs for the 6900' RA SUA, Chandeleur Sound Block 71 Field, St. Bernard Parish, Louisiana, wherein the Commissioner found that "the monies received from prior production [having] exceeded the actual reasonable expenditures incurred in the drilling, testing, completing, equipping and operation" of the unit well, "the depreciated well cost" as a consequence of a revision of the unit "was zero dollars."

286. Act No. 595, 1991 La. Acts 1913.

287. LA. REV. STAT. ANN. § 30:10A(2)(d)(i) (1991).

288. LA. REV. STAT. ANN. § 30:10A(1)(c) (2022).

the commissioner shall determine the proper costs after notice to all interested owners and a public hearing thereon."[289]

For many years, the Commissioner would refuse to set for hearing an application for a determination of unit well costs, forcing parties to reach agreement on the matter.[290] This was chronicled by Robert T. Jorden in his paper presented to the Louisiana Mineral Law Institute in 1991 as follows:

> Several unit well cost hearings were held by the Commissioner of Conservation in the 1950's and the 1960's, but after a controversial hearing relating to the Larose Field held in 1965, the Commissioner actually refused to schedule unit well cost hearings until 1987. From 1965 to 1987, the working interest owners were forced to and did manage to negotiate settlement of all unit well cost disputes.[291]

Louisiana courts have indicated the Commissioner's authority to determine "proper [well] costs" does not include the authority to determine how such costs are to be adjusted or apportioned among the various unit participants, nor to render a money judgment for such costs.[292] In this regard, the court in *Desormeaux v. Inexco Oil Co.* recognized the important, but limited, role and authority of the Commissioner in a well cost hearing as follows:

> After careful reading of LSA-R.S. 30:10, subd. A(1)(c), we conclude that the statute contemplates a situation where there is a dispute as to the actual specific costs sought to be charged to the non-operator, that is, whether the costs sought to be charged by the operator are reasonable or necessary expenditures. When the statute states that "the commissioner shall determine the proper costs" it is obviously referring to the cost of development and operation of the pool unit and the reasonableness thereof. Therefore, the Commissioner only has the fact-finding authority to determine the amount of reasonable and proper costs. He has

289. *Id.* § 30:10A(2)(f).

290. *See* Jorden, *Unit Well Cost Adjustment in Louisiana*, *supra* note 173.

291. *Id.*

292. O'Meara v. Union Oil Co. of Cal., 33 So. 2d 506 (La. 1947); Anisman v. Stanolind Oil & Gas Co., 98 So. 2d 603 (La. Ct. App. 2d Cir. 1957); Monsanto Chem. Co. v. S. Nat. Gas Co., 102 So. 2d 223, 225 (La. 1958) ("It would be beyond the function and powers of the Commissioner to say whether or not alleged contractual rights under the conventional agreements between [the parties] with respect to their leasehold rights were recast and affected by the order [issued by the Commissioner]. That is clearly a function of the courts.").

> no authority to determine how costs are to be apportioned or what effect his orders have on pre-existing contractual or legal relationships.[293]

2. Jurisprudence After Well Cost Determination by Commissioner of Conservation

The most significant decision relative to the issue of adjustment of unit well costs is *Tex/Con Oil and Gas Co. v. Batchelor*.[294] In *Tex/Con*, the Commissioner of Conservation revised certain units in the South Lake Arthur Field. As a consequence of these unit revisions, certain acreage held under lease by Tex/Con was excluded from, and certain acreage held under lease by Hunt was included in, the revised units.[295] Pre-revision unit production exceeded (significantly) the reasonable unit well costs for the units in question.[296]

Tex/Con filed an application with the Commissioner of Conservation "for a determination of: (1) the reasonable actual cost of each of the [unit] wells; (2) the depreciated cost for each well; and (3) whether a well cost adjustment should be made among the former and present owners of these units."[297] After a public hearing, the Commissioner concluded that, pursuant to Louisiana Revised Statutes § 30:10 and consistent with the principles enunciated in *Desormeaux v. Inexco Oil Co.*,[298] it was necessary to apply the dollar-for-dollar method of well cost adjustment. Finding that the "monies received from production exceeded the reasonable well costs for each well," the Commissioner concluded that "the cost chargeable by the owners of the original units to the subsequent owners of the revised units was zero."[299]

Tex/Con filed a suit for judicial review under the provisions of Louisiana Revised Statutes § 30:12.[300] The trial court ruled that, as a matter

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293. Desormeaux v. Inexco Oil Co., 277 So. 2d 218, 220–21 (La. Ct. App. 3d Cir. 1973). This is an earlier decision in the same case previously discussed at *supra* note 276.

294. Tex/Con Oil and Gas Co., v. Batchelor, 634 So. 2d 902 (La. Ct. App. 1st Cir. 1993).

295. *Id.*

296. *Id.* at 904–05.

297. *Id.* at 905.

298. *Desormeaux*, 277 So. 2d 218.

299. *Batchelor*, 634 So. 2d at 905.

300. Louisiana Revised Statutes § 30:12 provides the exclusive procedure to challenge or question an order of the Commissioner of Conservation. *See* LA. REV. STAT. ANN. § 30:12 (2022). A challenge brought in any other manner is

of law, Louisiana Revised Statutes § 30:10A(2) and the custom and usage of the oil and gas industry "require that the unit of production depreciated well cost method of accounting be applied to determine depreciated unit well costs"[301] and that, accordingly, "the Commissioner erred in finding that application of the dollar-for-dollar method to determine unit well costs was consistent with the *Desormeaux* case . . . ."[302] The trial judge remanded the matter to the Commissioner "with instructions to adjust well costs for the subject wells by applying the unit of production depreciated well cost method."[303]

The Commissioner and Hunt appealed to the Louisiana First Circuit Court of Appeal. The appellate court stated that the principal issue on appeal was "whether the Commissioner erred in applying the dollar-for-dollar method in determining whether any well cost adjustment was due under LSA-R.S. 30:10 A(2)."[304] The court defined the competing methods of unit well cost adjustments as follows:

> Under the dollar-for-dollar method, well costs are reduced by the dollar amount of monies received from production prior to the unit revision, before any well cost adjustment is made between the parties. The unit of production depreciated well cost method contemplates reduction of well costs by the percentage of depletion of the unit's total recoverable reserves caused by production prior to unit revision.[305]

The court particularly noted that the relevant statute, Louisiana Revised Statutes § 30:10A(2)(d), was amended in 1991 by Act No. 595 of the Louisiana legislature. The court applied the pre-amendment version of the statute, saying that it was "effective at all times pertinent hereto."[306] The court stated as follows:

> We find, as did the Commissioner, that the wording of this statute mandated that the Commissioner apply the dollar-for-dollar method of depreciation. The statute, as it existed at the time this dispute arose, dictated that well costs "be reduced to account for monies received from prior production," phraseology which we

considered a "collateral attack" on an order of the Commissioner of Conservation. *See* Trahan v. Superior Oil Co., 700 F.2d 1004, 1014 n.14 (5th Cir. 1983).

301. *Batchelor*, 634 So. 2d at 905.
302. *Id.* at 906.
303. *Id.*
304. *Id.*
305. *Id.* at 907 (internal citations omitted).
306. *Id.*

> agree clearly contemplated use of the dollar-for-dollar method of determining well costs. Nothing in the wording of the statute, in its previous form, suggested or required that well costs were to be depreciated by the percentage of recoverable reserves that had been recovered by prior production. . . . Thus, under the clear wording of the statute, the Commissioner was required to use the dollar-for-dollar method in determining depreciated well costs.[307]

In reference to the post-amendment statute (effective in 1991), the court observed that the amendment "change[d] the phrase 'shall be reduced to account for monies received from prior production' to 'shall be reduced in the same proportion as the recoverable reserves in the unitized pool have been recovered by prior production.'"[308] In recognition of this change, the court posited as follows:

> This amendment evidences a clear change in the method of determining well costs to a unit of production well cost reduction method and provides further support for the conclusion that prior to this 1991 amendment, LSA-R.S. 30:12A(2)(d) mandated the use of the dollar-for-dollar method.[309]

Regardless of where the issue is to be litigated—judicially or administratively—a dispute concerning the equitable adjustment of unit well costs is certainly an expert-intensive endeavor, involving testimony from petroleum engineers, reservoir engineers, unitization geologists, landmen, accountants, and other disciplines. Guidance as to these issues might be obtained in accounting guidelines promulgated by COPAS,[310] particularly AG-1 Well Cost Allocations and Adjustments. "The Council of Petroleum Accountants Societies (COPAS), a national organization since 1961, has issued a succession of accounting forms which serve as the primary source of oil and gas accounting standards in the industry."[311] Courts continue to recognize COPAS publications as evidence of industry standards and guidelines on issues within the purview of that organization.[312]

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307. *Id.* at 908.
308. *Id.*
309. *Id.*
310. COPAS is an acronym for Council of Petroleum Accountants Societies.
311. Armstrong Petroleum Corp. v. Tri-Valley Oil & Gas Co., 11 Cal. Rptr. 3d 412, 417 (Cal. Ct. App. 2004).
312. A COPAS Accounting Guideline was accepted by an appellate court as "additional guidance as to industry standards on gas accounting." Red Willow

I. Disposition of Production Due to Unleased Mineral Owners

In 2022, Subsection 10A(3) of Section 10 of Title 30 was amended for the first time since its enactment in 1984. The following legislative markup for this subsection reflects the original text, marked with 2022 amendments,[313] to-wit:

> If there is included in any unit created by the commissioner of conservation[314] one or more unleased interests for which the party or parties entitled to market production therefrom have not made arrangements to separately sell or otherwise dispose of the share of such production attributable to such tract, and the unit operator ~~proceeds with the sale of~~ sells or otherwise disposes of such unit production, then the unit operator shall pay to such party or parties such tract's pro rata share of the proceeds of the sale or other disposition of production within one hundred eighty days of such sale or other disposition.

As ultimately adopted, Section 10A(3) was not part of the bill that was originally introduced.[315] Rather, the essential legislative package that was ultimately adopted as, in industry jargon, the Louisiana Risk Fee Act was sought and promoted at the behest of industry to address certain free rider abuses in the late 1970s and early 1980s, principally in the Tuscaloosa Trend productive area. The minutes of the meeting of the Senate

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Offshore, LLC v. Palm Energy Offshore LLC, 185 So. 3d 293, 300 (La. Ct. App. 4th Cir. 2016).

313. Amended by Act No. 5 (Aug. 1, 2022). The text shows deleted words as interlined and words added as underscored.

314. As noted in note 4, *supra*, there are five kinds of compulsory units. Despite the reference in Section 10A(3) to "*any* unit created by the commissioner of conservation," the provisions of the cited Section would be limited to a "drilling and production" unit as authorized and envisioned by Louisiana Revised Statutes § 30:9. LA. REV. STAT. ANN. § 30:9 (2022). However, by explicit statutory reference, such provisions also "shall be applicable to ultra deep structure units, including the applicable risk charge." *Id.* § 30:5.1B(9).

315. The legislative history of the adoption of the Risk Fee Act is taken from an Affidavit filed in the record of the case of *Johnson v. Chesapeake Louisiana, LP*, No. 16-01543, United States District Court, Western District of Louisiana, Shreveport Division, Doc. No. 58-3 filed April 30, 2019. This Affidavit was signed and attested to by the principal lobbyist for industry in connection with the formulation and adoption of the Risk Fee Act. In the interest of full disclosure, the author represented the defendant in this suit which will be discussed in greater detail.

Committee on Natural Resources held on June 21, 1984, reflect that an amendment was offered by a legislator, which amendment was acceptable to the proponents of House Bill No. 934.[316] The amendment was ultimately accepted and is embodied in Louisiana Revised Statutes § 30:10A(3).

The sole purpose of that amendment was to provide legal authority to an operator to market the share of production allocable to an unleased mineral owner and, if the operator undertook to market said share, to account to the unleased mineral owner in cash within a certain period of time. Indeed, as commentators had noted, "In Louisiana there is no express statutory or direct jurisprudential authority establishing the right of an operator to market a non-operator's share of the co-owned production absent a joint operating agreement or other contract allowing him to do so."[317] Because nothing in the amendment altered or upset the principal objective of House Bill No. 934 (addressing the free rider), the proponents found no reason to oppose the amendment.[318]

As stated, Section 10A(3) was principally designed to establish the authority of the operator to market unleased mineral owner's share of unit production and to fix the date by which proceeds were to be paid, subject, of course, to the paramount right of the operator to be reimbursed for well costs out of production.[319] The original text was not a model of clarity, employing, for example, the word "proceeds" twice, once as a verb, once as a noun.

Courts have consistently viewed Section 10A(3) as establishing a quasi-contractual relationship between the operator and the unleased

316. The legislative record reflects the following amendments to Louisiana Revised Statutes § 30:10A(3): Acts 1984, No. 345, § 1; Acts 1991, No. 595, § 1; Acts 2009, No. 115, § 1; Acts 2012, No. 743, § 1; Acts 2016, No. 524, § 1; Acts 2022, No. 5, § 1.

317. *See* Thomas M. McNamara, *Unitized Production—Rights of Operators and Non-operators*, 31 ANN. INST. ON MIN. L. 194, 205–06 (1984). Although this presentation was made in the same year as Act No. 345, 1984 La. Acts 929, it was made prior to the legislative session.

318. LOUISIANA HOUSE OF REPRESENTATIVES, LEGISLATIVE CALENDAR FOR HOUSE BILLS 246 (1984) (Senate amendment on the floor on June 26).

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

mineral owner.[320] For example, in *King v. Strohe*,[321] the court stated as follows:

> La. R.S. 30:10(A)(3) was enacted for the benefit of both the unit operator and the unleased interest. It protects the unleased interests and avoids undue delays in the sale of production. Leased interests are usually entitled to only an in kind share of production, which they then market. It is then the lessee's duty to distribute the proceeds under its contract with its lessor. When there is no lessee, the mineral interest owner must deal directly with the unit operator, with whom he has no contractual relationship. To facilitate the sale of the minerals, La. R.S. 30:10(A)(3) provides a quasi-contractual relationship between the unit operator and the mineral interest owner.[322]

The quasi-contractual relationship brings into play precepts of the Civil Code relative to the management of affairs of another (*negotiorium gestio*)[323] and enrichment without cause.[324]

In *Taylor v. Woodpecker Corp.*,[325] the court took up the contention of certain unleased mineral owners that the operator, in failing to account for the share of unit production, was liable to the owners under a theory of

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320. *See* Wells v. Zadeck, 89 So. 3d 1149, 1154 (La. 2012) (recognizing that a "quasi-contractual relationship is created between the unit operator and the unleased mineral interest owner with whom the operator has not entered into contract"). *See also* Taylor v. Smith, 619 So. 2d 881 (La. Ct. App. 3d Cir. 1993); Taylor v. Woodpecker, 633 So. 2d 1308 (La. Ct. App. 1st Cir. 1994); King v. Strohe, 673 So. 2d 1329 (La. Ct. App. 3d Cir. 1996); Hackett v. Murphy Expl. & Prod. Co., 216 So. 3d 63 (La. Ct. App. 3d Cir. 2017).

321. *King*, 673 So. 2d 1329.

322. *Id.* at 1338 (internal citations omitted). The court cited as authority the case of *Taylor v. David New Operating Co., Inc.*, 619 So. 2d 1251 (La. Ct. App. 3d Cir.), *writ denied,* 625 So. 2d 1046 (La. 1993).

323. LA. CIV. CODE ANN. art. 2292 (2022) ("There is a management of affairs when a person, the manager, acts without authority to protect the interests of another, the owner, in the reasonable belief that the owner would approve of the action if made aware of the circumstances.").

324. *Id.* art. 2298 ("A person who has been enriched without cause at the expense of another person is bound to compensate that person. The term 'without cause' is used in this context to exclude cases in which the enrichment results from a valid juridical act or the law. The remedy declared here is subsidiary and shall not be available if the law provides another remedy for the impoverishment or declares a contrary rule.").

325. *Woodpecker*, 633 So. 2d 1308.

conversion.[326] The court rejected this contention and explained the nature and origin of the operator's liability as follows:

> We agree that LSA–R.S. 30:10A(3) gives an unleased landowner a cause of action in quasi contract under these Civil Code articles. The unit operator acts as a *negotiorum gestor* or manager of the owner's business in selling the owner's proportionate share of oil and gas produced. In return for the right to sell the share of production of the unleased landowner, the unit operator is obligated by law "without any agreement" to pay the unleased landowner his proportionate share of proceeds within 180 days of the sale of production. The "purely voluntary act" of assuming the position of unit operator, and thereby obtaining the right to sell the unleased interest owner's share of production, results in this obligation to account to the unleased interest owner pursuant to LSA–R.S. 30:10 A(3).[327]

J. Residual Authority of Commissioner of Conservation

Louisiana Revised Statutes § 30:10B provides as follows:

> Should the owners of separate tracts embraced within a drilling unit fail to agree upon the pooling of the tracts and the drilling of a well on the unit, and should it be established by final and unappealable judgment of court that the commissioner is without authority to require pooling as provided for in Subsection A of this Section, then, subject to all other applicable provisions of this Chapter, the owner of each tract embraced within the drilling unit may drill thereon. The allowable production therefrom shall be such proportion of the allowable for the full unit as the area of the separately owned tract bears to the full drilling unit.[328]

This provision might be considered as somewhat of a relic in that it was adopted as part (then Section 9(b)) of the original Conservation Act enacted by Act No. 157 of 1940 and seemingly was included to anticipate court challenges to the authority of the Commissioner to "require pooling as provided for in Subsection A of this Section."[329]

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326. *Id.* at 1312.
327. *Id.* at 1313 (internal citations omitted).
328. LA. REV. STAT. ANN. § 30:10B (2022).
329. *Id.*

Finding the Conservation Act to be constitutional, the Supreme Court decision in *Hunter Co., Inc. v. McHugh*[330] put that issue to rest, such that this provision—while still appearing as a part of Section 10—is ineffectual for all practical purposes.

CONCLUSION

As previously noted, unit operations are typically undertaken by a multitude of parties rather than by a sole or single lessee. Thus, in this typical case, the unit operator, unless it has established contractual relationships with all other unit participants, will have occasion to evaluate its rights and duties with respect to any party not under contract.

In the absence of a contractual relationship, Section 10 of the Conservation Act steps in to fill this void, essentially providing specific rules but also guidelines to address issues of cost responsibility between parties.

As noted previously, the author suggests that consideration be given to a wholesale rewrite or reorganization of Section 10 so as to more logically set forth the provisions thereof which are currently in a formulation that might be deemed to be somewhat haphazard or illogical. It is the hope of the author that this Article has brought clarity to the important and disparate provisions of Section 10, but to the extent that this effort at demystification has not succeeded, perhaps the identification of open issues or questions will also serve an important purpose.

330. Hunter Co., Inc. v. McHugh, 11 So. 2d 495 (La. 1942).