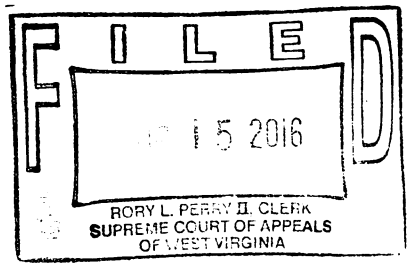
IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA
DOCKET NO. 16-0136



PATRICK D. LEGGETT;
KATHERINE F. LEGGETT;
GEORGE D. MCKAIN, by his
attorney in fact, ANITA
KATHRYN MCKAIN GREER;
and ADELE S. MCDOUGAL,

Plaintiffs,

v.

Civil Action No. 1:13-cv-0004 FPS
(U.S. District Court, Northern District)

EQT PRODUCTION COMPANY,
a Pennsylvania corporation;
EQT CORPORATION,
a Pennsylvania corporation;
EQT ENERGY, LLC, a
Delaware limited liability company;
EQT INVESTMENTS HOLDINGS, LLC, a
Delaware limited liability company;
EQT GATHERING, LLC, a
Delaware limited liability company; and
EQT MIDSTREAM PARTNERS, LP,
a Delaware limited partnership,

Defendants.

PETITIONERS' REPLY BRIEF

Respectfully submitted:

Marvin W. Masters (WVSB # 2539)
Richard A. Monahan (WVSB # 6489)
April D. Ferrebee (WVSB # 8034)
The Masters Law Firm lc
181 Summers Street
Charleston, West Virginia 25301
(304) 342-3106
and
Michael W. Carey (WVSB # 635)
Carey, Scott, Douglas & Kessler, PLLC
707 Virginia Street East, Suite 901
Charleston, West Virginia 25301
Counsel for Plaintiffs

TABLE OF CONTENTS

TABLE OF AUTHORITIES iv

A. Plaintiffs Response to Defendant's Procedural History and Facts 1

B. Argument .....

C. The Phrase "At the Wellhead" is Ambiguous 4

D. The Court Should Address the Second Certified Question 13

E. The Contracts Clause Is Not Violated By Retroactively Applying The Public Policy Set Forth in W.Va.Code § 22-6-8 17

F. Conclusion 19

TABLE OF AUTHORITIES

CASES

Abrams v. West Virginia Racing Commission, 164 W.Va. 315, 263 S.E.2d 103 (1980) 15,16,17

Bass v. Coltelli, 192 W.Va. 516, 453 S.E.2d 350 (1994) 14

Bruen v. Columbia Gas Transmission Corp., 188 W. Va. 730, 426 S.E.2d 522 (1992) 6

Cole v. Pond Fork Oil & Gas Co., 127 W.Va. 762, 35 S.E.2d 25 (1945) 11

Connecticut v. Johnson, 460 U.S. 73 (1983) 17

Consolidation Coal Co. v. Mineral Coal Co., 147 W.Va. 130, 126 S.E.2d 194, 203 (1962) 14

Cotiga Development Co. v. United Fuel Gas Co., 147 W.Va. 484, 128 S.E.2d 626 (1962) 13

Davis Memorial Hosp. v. West Virginia State Tax Com'r, 222 W.Va. 677, 671 S.E.2d 682 (2008) 3,9

El Paso v. Simmons, 379 U.S. 497 (1965) 18

Energy Reserves Group, Inc. v. Kansas Power and Light Co., 459 U.S. 400 (1983) 18

Estate of Tawney v. Columbia Natural Resources, 219 W.Va. 266, 633 S.E.2d 22 (2006), ... 2,3,4,5,6,7,9,12,13,15

Estate of Tawney v. Columbia Natural Resources, LLC, Civil Action No. 03-C-10E, 2006 WL 6056969 (W.Va.Cir.Ct. Aug. 4, 2006), ... 18

Garman v. Conoco, Inc., 886 P.2d 652 (Colo. 1994) 9

Gilmore v. Superior Oil Co., 388 P.2d 602 (Kan. 1964) 5

Jones v. Com., 429 S.E.2d 615 (Va. 1993) 7

Kanawha Valley Bank v. United Fuel Gas Co., 121 W.Va. 96, 1 S.E.2d 875 (1939) 10,11

Kilmer v. Elexco Land Services, Inc., 605 Pa. 413, 990 A.2d 1147 (2010) 11

Kohlsaat v. Main Island Creek Coal Co., 90 W.Va. 656, 112 S.E. 213 (W. Va.) 32

Mitchell v. Cline, 186 W.Va. 332, 412 S.E.2d 733 (1991) 7

Pauley v. Kelly, 162 W.Va. 672, 255 S.E.2d 859 (1979) 17

Payne v. Weston, 195 W.Va. 502, 466 S.E.2d 161 (1995) 23

Phillips v. Larry's Drive-In Pharmacy, Inc., 220 W. Va. 484, 491-92,
647 S.E.2d 920, 927-28 (2007) 8,9

Rogers v. Westerman Farm Co., 29 P.3d 887, 902 (Colo. 2001) 5,8.9

Shell v. Metropolitan Life Ins. Co., 380 S.E.2d 183 (W.Va. 1989) 8,17,18

State v. Appleby v. Recht, 213 W.Va. 503, 583 S.E.2d 800 (2002) 7

State v. Bonham, 173 W.Va. 416, 317 S.E.2d 501 (1984) 17

State v. Brown, 159 W.Va. 438, 223 S.E.2d 193 (1976). 14

State v. Stout, 142 W.Va. 182, 95 S.E.2d 639 (1956) 14

State ex rel. McGraw v. Scot Runyan Pontiac-Buick, Inc., 194 W.Va. 770,
461 S.E.2d 516 (1995) 10

Toler v. Shelton, 159 W.Va. 476, 223 S.E.2d 429 (1976). 14

United States Trust Co. v. New Jersey, 431 U.S. 1, 31, n. 30 (1977) 18

Wellman v. Energy Resources, Inc., 210 W.Va. 200,
57 S.E.2d 254 ..... 3,4,6.12,13

Wood v. TXO Prod. Corp., 854 P.2d 880 (Okla. 1992) 5,8,8

STATUTES

58 PA Stat. Ann § 33.3

W. Va. Code, § 22-6-8

W. Va. Code, § 51-1A-1

W. Va. Code, § 51-1A-4

W. Va. Code, § 58-5-2

REFERENCES

Donley, *The Law of Coal, Oil and Gas in West Virginia and Virginia*, § 156, at p. 219 (1951)

"The History of Regulation." *NaturalGasorg*. NaturalGasorg, 20 Sept. 2013. Web. 14 Aug. 2016. http://naturalgas.org/regulation/history/

Williams & Myers Oil & Gas Law, Vol. 8

F:\5\864\btoc011.docx

A. Plaintiffs' Response to Defendant's Procedural History and Facts

Defendant raised several issues in its Procedural History and Statement of Facts Section which plaintiffs will address. As defendant points out, plaintiffs constitute 75% of the natural gas ownership on the subject lease. The other 25% did not "join the case," as defendant claims, but it was because they also own the surface and defendant settled all matters including royalty issues with that party. Defendant claims that plaintiffs did not allege the lease was invalid or unenforceable. However, plaintiffs alleged and complained that defendant was obligated by its duties under the leases to, among other duties and responsibilities, pay plaintiffs the amounts required pursuant to the laws of the State of West Virginia (JA 16,) and plaintiffs complained that defendant "has failed and refused to pay plaintiffs herein for all royalty due them." (JA 16-19; Amended Complaint, Par. 28-30, 35, 38-39.) And, the District Court certified the questions and asked whether *W. Va. Code*, § 22-6-8 prohibits, not only "reworked" or new wells on a lease, but also whether it prohibits flat rate leases entirely. (JA 4.) The United States District Court asks this question because the defendant continues to pay only a flat rate royalty for production on some of plaintiffs' wells which defendant admits were not reworked. (JA 2-4.) The Court stated that "EQT has paid flat rate royalty to plaintiffs for wells on the premises identified under the 1906 lease that are not subject to the Flat-Rate Statute." (JA 2-4.)

Defendant claims plaintiffs stipulated that the lease is valid and in effect, however, the defendant raised these issues as prohibiting this lawsuit in the United States District Court and that Court ruled that the "plaintiffs did not release or disclaim EQT from liability for claims arising after December 8, 2008." "Thus, neither the 2008 settlement agreement nor the non-

violation provision"[1] standing alone, bar the plaintiffs' claims in this civil action. (JA 608-610 @ 610.)

Defendant claims that it does not take deductions for taxes, depreciation or returns. (Resp. Brief, 5.) However, defendant's F.R.C.P. 30(b)(6) witness, Mr. Bergonzi testified that plaintiffs' royalty records showed that they were taking taxes from his royalty. (JA 230; Bergonzi Deposition, p. 226.) Defendant also admits it takes deductions through various other companies, including EQT Corporation, EQT Gathering and other subsidiaries which it contends are independent entities.

Defendant claims that plaintiffs have no evidentiary support for claiming that EQT entered into a plan to circumvent *W. Va. Code*, § 22-6-8's requirements. Plaintiffs cite to the fact that EQT Production pays a sister company which was formed contemporaneously with the *Tawney* litigation to create a "proxy" price of the gas which is shown on their statements, but is not the real price, instead it is a calculated price created by defendant by deducting a "cost of service" estimated amount from what is represented to be the index price of the gas.

Defendant claims that it only has to pay the statutory amount on the volume of gas sold – not on the volume extracted at the wellhead. (Resp. Brief, 6.) However, the statute requires the payment to be made on all gas "extracted and produced." The defendant, on the one hand, claims it should not be required to pay on the volume at the wellhead, but should be able to pay royalty based on a false, calculated price at the wellhead.

Defendant claims that plaintiffs "leave the record behind" when plaintiffs state that the deductions are "estimates." (Resp. Brief, 6.) "Estimates" of deductions are defendant's words,

[1] The defendants claimed that the pooling agreement prohibited plaintiffs' claim after the settlement and pooling agreement were entered into. The pooling agreement is where the defendants included a lease ratification agreement.

not plaintiffs' creation.[2] According to defendant's F.R.C.P. 30(b)(6) witnesses, including Mr. Bergonzi, testified not only that they are estimates, but also that defendant does not do an audit and correct the estimates. (JA 185; Bergonzi deposition, p. 48.) Also, defendant claims that the costs are actually less than actual costs. (Resp. Brief, 6-7.) This contention is absurd given that defendant is not entitled to take any deductions from plaintiffs' royalty and it is incorrect.

Plaintiffs have no way of knowing what is being deducted except to file a lawsuit. Then defendant claims, nevertheless, the costs "inevitably are less than actual costs – a fact never mentioned by plaintiffs in their brief." (Resp. Brief, 7.) True, plaintiffs didn't mention this because it's not true for several obvious reasons depending upon whether all of EQT's subsidiaries are allowed to place their list of costs into the deduction bucket in the first place.

Defendant argue that plaintiffs' claim that the "age-old" industry practice of paying royalties based on "1/8 of the amount received, without deductions," is "simply wrong," citing to cases obviously not agreeing with *Wellman* or *Tawney*. (Resp. Brief, 7.) However, later in its brief, defendant admits there are two lines of cases considering these issues and West Virginia has squarely adopted the "marketable-product rule" based on this Court's holdings in Tawney.

B. Argument

This Court should find that the legislative intent was that the working interest owner (lessee) is required to pay "no less than one-eighth" of the "total amount" it receives for "all of the gas" which is "extracted" from the natural gas wells and that "at the wellhead" is ambiguous since it is "susceptible of two or more constructions of such doubtful or obscure meanings that reasonable minds might be uncertain or disagree as to its meaning." *Davis Memorial Hospital v. West Virginia State Tax Commissioner*, 222 W. Va. 677, 682-83, 671 S.E.2d 682, 687-88 (2008.)

[2] Defendant claims that it deducts what it considers "its best judgment" of the actual costs, which greatly emphasizes the unfairness of the defendant's practice. (Resp. Brief, 6.) Well, "its judgment" is to take as much as it can get, amounting to huge deductions from the plaintiffs' royalty, including costs referred to as a "laundry list."

This Court should find that the statute is susceptible of two or more meanings because first, it is in conflict with other terms and phrases in the same statute and even in the same subparagraphs in which it appears. Second, the phrase is consistent with referring to a volume calculation which the defendant rejects by paying the lesser amount at the interstate pipeline and third, it is inconsistent with West Virginia's long history of practice in the oil and gas industry of the lessee being required to make the gas marketable as set forth in the holdings of *Wellman* and *Tawney* and cases cited therein, along with the recognized authority on oil and gas law in West Virginia, Mr. Donley, in 1951. The Court should hold that in order to reconcile and harmonize the statute and its terms, the Court must look to the other terms used in the statute and in reading from all four corners of the statute, it is clear that the Legislature intended that the owner of the working interest must pay the owner of the gas a minimum of 1/8 of what the working interest owner received on all of the gas extracted, produced or marketed and that the practice was consistent with the historical practice in West Virginia, which is a "marketable product" jurisdiction. The Court should also find that the lessee, owner of the working interest, has had decades to comply with what the public policy has been in West Virginia since 1982. The Court should find that a reasonable time to have converted and paid the lessor 1/8 on all wells on the lease would have been 10 years from 1982, and that the Legislature having declared the public policy, the Court must now enforce that public policy and as to this lease which includes leases both converted and not converted, the lease should be abrogated as to the wells thereon which do not receive a 1/8 royalty and that the terms therein be construed as to being consistent with the terms and provisions as forth in *W. Va. Code*, § 22-6-8 (e).

C. The Phrase "At the Wellhead" is Ambiguous

Defendant claims that the statute is not ambiguous, however, the District Court stated in its Order that [t]he phrase "at the wellhead" under the flat rate statute is just as ambiguous as the language in the *Tawney* leases. (JA 604.) The Court also pointed out that the subject 1906 lease does not indicate an intent contrary to the general rule.[3] *Id.* Plaintiffs believe the District Court was referring to the general rule, as stated in *Tawney*, that the "at the well" language did not authorize deductions. The Court pointed out that the 1906 lease did not allocate expenses or indicate how deductions may be calculated and "[i]ndeed the 1906 lease even appears to state that the lessors should receive the royalty in'full equal one eighth (1/8) parts or share of the same, delivered free of charge.'" *Id.*

It is important to keep in mind in resolving the questions in this case that there are two lines of authority in the United States on the general law applicable as to whether the gas company can take deductions from the owners 12.5%. In its brief, defendant actually acknowledged that there are two separate lines of authority and stated that "[t]he courts in other states, including West Virginia, have held that the lessee is required to make the gas marketable and to bear all of the costs for doing so. Syl. Pt. 1, *Tawney*, 219 W.Va. 266, 633 S.E.2d 22; *Rogers v. Westerman Farm Co.,* 29 P.3d 887, 902 (Colo. 2001); *Wood v. TXO Prod. Corp.*, 854 P.2d 880, 882-83 (Okla. 1992); Syl. Pt. 3, *Gilmore v. Superior Oil Co.*, 388 P.2d 602 (Kan. 1964). The Gilmore case was decided in 1964 before 1982 when *W. Va. Code*, § 22-6-8 was adopted and was relied upon in Tawney. (Resp. Brief, 9.)

Regardless of defendants' acknowledgement that West Virginia is a "marketable product state," defendant cites this Court to cases which are "at the wellhead" states as controlling.

[3] The Court set forth a very precise and informative analyses of the Court's findings as to why the Court decided to certify this question. (JA 599-603)

Defendant argues that Robert Donley didn't say or mean what he was quoted to say in both *Wellman* and *Tawney*. Mr. Donley however, also stated that "[i]n the absence of an express covenant to market either oil or gas, the court implies one in order to effectuate the basic purpose of the lease, which, after all, is to enable the lessor to convert his minerals into cash. *Id.* 104. Robert Donley has been recognized for decades as an authority on oil and gas leases and agreements and the practices in West Virginia related thereto. *See Bruen v. Columbia Gas Transmission Corp.*, 188 W. Va. 730, 426 S.E.2d 522 (1992),

Defendant argues that *Kilmer v. Elexco Land Services, Inc.*, 990 A.2d 1147 (Pa. 2010) and the Pennsylvania statute control the Court's action here. Defendant's reliance on *Kilmer* is misplaced because that case is factually distinguishable and adopts law contrary to well-settled law in West Virginia. First, it is noteworthy that the landowners in *Kilmer* filed suit in 2008 to invalidate leases they entered into in 2007. These circumstances are in stark contrast to the facts in this case. The relevant portion of the lease in *Kilmer* provided for the calculation of royalties as "*one eighth (1/8th) of the sales proceeds actually received by Lessee from the sale of such production, less this same percentage share of all Post Production Costs.*" *Kilmer*, at 1150. In addition, the statute allowed for post-production costs. This lease provision is in no way similar to the language at issue here. The plaintiffs in *Kilmer* challenged the lease as violating a Pennsylvania statute that guaranteed minimum royalties for oil and gas. 58 P.S. § 33 ("GMRA").[4] The court in *Kilmer* ignored the first marketable product rule and cited authority in accord with the Texas line of cases (rejected in *Wellman* and *Tawney)* to define royalty and post-production costs and found that the defendants could use the net-back method to calculate the plaintiffs' royalties under the GMRA. *Kilmer,* at 1157-1158. The *Kilmer* court's legal

[4] Plaintiffs note that this statute is not similar or analogous to West Virginia Code § 22-6-8.

reasoning is in direct contrast with the principles applicable under West Virginia law but so is the lease and statute at issue therein.

In defendant's argument, it focuses solely upon the "at the well" phrase, not the other terms in the statute and how the phrase could mean anything other than that it is entitled to take deductions from the plaintiffs' royalty. Words and clauses should be given a meaning which harmonizes with the subject matter and the general purpose of the statute. The general intention is the key to the whole and the interpretation of the whole controls the interpretation of its parts. *Mitchell v. Cline*, 186 W.Va. 332, 412 S.E.2d 733 (1991); *State v. Appleby v. Recht*, 213 W.Va. 503, 583 S.E.2d 800 (2002). When the meaning of a word in a statute may have a special or limited meaning, the meaning of the word must be construed in a manner that gives full effect to the legislative intent embodied in the entire statutory enactment. *Jones v. Com.,* 429 S.E.2d 615 (Va. 1993).

Defendant claims that plaintiffs rely solely on Tawney as the basis for its position. Plaintiffs pointed out in District Court that there is not even a hint that deductions can be taken and that the language ends any argument that deductions may be taken. (JA 522.) What plaintiffs did argue was that any ambiguity in the term "at the wellhead" must be resolved in favor of the "owner of the gas in place." (JA 523-530.) This argument was not based solely upon *Tawney*, but also based upon the fact that the Flat-Rate Statute is clearly a remedial statute which is to be construed liberally to accomplish the purpose intended. (JA 524-527.) Just as important is the statute's silence with respect to any duty of the owners of the gas to pay money back to lessee gas companies for getting the gas to market and selling it. If the Legislature intended for deductions to be taken, the Legislature would have plainly said so. It would have been simple to add a sentence to the statute to provide for deductions if that was the Legislature's intent.

Plaintiffs' argument and position was that if anything is clear, it is that the Legislature intended to assure that no matter how one read the statute, the owner of the gas would receive one-eighth of the money the producer received for the gas "extracted" from his property. This is evidenced by the following language which boxes in the options a producer may attempt to argue:

(a) not less than one-eighth of the total amount (received by lessee;)

(b) paid to or received by or allowed to (lessee;)

(c) at the wellhead;

(d) for the oil or gas so extracted, produced or marketed (at the wellhead;)

(e) before deducting the amount to be paid to or set aside; and

(f) on all such oil or gas to be extracted, produced or marketed (from the well.)

There is nothing in the language of § 22-6-8 that provides that Defendant is permitted to net-back post production costs to Plaintiffs. The statute is silent with respect to such costs and courts are not to arbitrarily read into a statute that which it does not say. *Phillips v. Larry's Drive-In Pharmacy, Inc.,* 220 W.Va. 484, 491, 647 S.E.2d 920, 927 (2007).

Defendant claims that the wellhead has a definitive meaning. However, Williams & Myers Oil & Gas Law, Vol. 8, Foreword, page v, in their Manual of Oil & Gas Terms, Williams & Myers in defining "at the well," noted such ambiguity. They not only cite jurisdictions which have adopted the marketable-product rule but also jurisdictions which adopt the at the wellhead rule. *Piney Woods Country Life School v. Shell Oil Co.,* 726 F.2d 225, 241 (5th Cir. 1984) which Defendants rely upon, but also cite *Rogers v. Westerman Farm Co.*, 29 P.3d 887, 897 (Colo. 2001) which plaintiffs rely on and which rejected the argument that "at the well" provides for allocation of costs. Williams & Myers Oil & Gas Law, Vol. 8, pages 65-67. *Rogers, supra,* also cited *Fox Wood III v. TXO Production Corp.,* 854 P.2d 880 (Okla. 1992) (implicitly determining

"at the well" is silent as to allocation of costs) and *Garman v. Conoco, Inc.,* 886 P.2d 652 (Colo. 1994) (rejecting Conoco's argument that industry practice allows proportionate allocation of post production costs).

"At the well" is not defined in *West Virginia Code*, § 22-6-8. However, this Court, in *Estate of Tawney v. Columbia Natural Resources,* 219 W.Va. 266, 633 S.E.2d 22 (2006), considered *Rogers and Garman, supra,* in concluding that "at the wellhead" type language is ambiguous because it is susceptible to more than one construction and reasonable people can differ as to its meaning. There is no reason to depart from *Tawney's* reasoning or analysis here. This Court, importantly, also rejected the Texas line of cases that Defendants rely upon to argue that "at the well" has a commonly accepted meaning in the oil and gas industry. *Tawney,* at 270, 26. This Court relied upon "our own settled law" to find "at the wellhead" language ambiguous. Id. at 271-271, 27-28.

This interpretation relies on the language and context of the statute rather than improperly adding language that the legislature did not intend to include. *See Phillips, supra,* at 491, 927. Moreover, it is a stretch for the Defendant to argue that in 1982, the legislature intended the statute to allow them to net-back costs to the Plaintiffs long after the enactment of West Virginia Code § 22-6-8 and after the Federal Energy Regulatory Commission deregulated the natural gas industry. *See Tawney,* at 272, 28. *See also,* "The History of Regulation." *NaturalGasorg.* NaturalGasorg, 20 Sept. 2013. Web. 14 Aug. 2016. http://naturalgas.org/regulation/history/. Plaintiff's interpretation is also in accord with the spirit, purposes and objects of West Virginia Code § 22-6-8. *See,* Syl. Pt. 4, *Davis Memorial Hospital v. West Virginia State Tax Com'r*, 222 W.Va. 677, 671 S.E.2d 682.

Moreover, § 22-6-8 is a remedial statute, designed to furnish flat rate royalty owners wholly adequate compensation and relief from the oppression and unjust hardship caused by lessees who hold flat rate leases, and to provide royalty owners a cause of action to enforce their rights under the section. Accordingly, it must be construed "liberally so as to furnish and accomplish all the purposes intended." *State ex rel. McGraw v. Scot Runyan Pontiac-Buick, Inc.*, 194 W.Va. 770, 777, 461 S.E.2d 516, 523 (1995).

The Court addressed the question of whether an oil and gas lessee could allocate to the landowner a portion of the privilege tax due for entities engaged in the production of oil and gas and thereby reduce royalties in *Kanawha Valley Bank v. United Fuel Gas Co.*, 1 S.E.2d 875 (W. Va. 1939). The royalty clause there required the lessee to pay for gas "at the rate of one-eighth of the wholesale market value thereof at the well." *Id.* at 876. The Court found by this royalty clause, that "the lessee bound itself to pay the lessor a full one-eighth of the market price of the gas at the well - not such price less one-eighth of the production tax." *Id.* To the extent the lessor made a deduction, the Court added: "The lessee's deduction would be a material, unilateral modification of the contract, a modification courts cannot sanction." *Id.* The Court established clear precedent that royalties must be paid on the full value of the mineral extracted free of deductions.

Interestingly, eleven days after the *Kanawha Valley Bank* decision the legislature amended the statute in question to provide that oil and gas producers shall pay tax based on the "entire production, with no deduction by reason of payments...to the owners of the royalty interest...." The amendment provided: "[e]very person who is hereby required to pay said tax measured by the entire production of the property operated, is hereby authorized and empowered to deduct from any payment...to the owners of any royalty interest...that

proportion of the tax paid which the said royalty...bears to the entire production." *See Cole v. Pond Fork Oil & Gas Co.*, 35S.E.2d 25, 28 (W. Va. 1945).

The Court found that an amendment to the tax code which allows for tax deductions to be taken was unconstitutional in *Cole* on the basis that the statute violated the constitutional prohibition against impairing contracts. The premise for this conclusion was that the royalty clause in the lease required that the lessee pay the lessor "one-eighth part of the proceeds from the marketing or sale of natural gas." *Cole* at 26. As in *Kanawha Valley Bank* the Court found that this clause required payment on the gross proceeds with no deduction for a tax.

In *Kohlsaat v. Main Island Creek Coal Co.,* 112 S.E. 213 (W. Va. 1922) the Court was presented with an issue under a coal lease requiring the lessee to pay as royalty "ten (10) percent of the selling price of said coal above ninety (90) cents per ton." *Kohlsaat* at 214. During World War I, the President issued an executive order permitting an increase of 45 cents in the price of coal per ton, provided there was a corresponding increase in the wages of miners. The coal company availed itself of the opportunity and increased its sale price by 45 cents, and in addition, employed a sales agent to assist with sales. *Id.* In calculating royalty, the coal company deducted from the sale price before calculating royalty the 45 cent increase on the grounds that it received no benefit of the increased price, along with the commissions paid the sales agent. *Id.* at 216. Upon challenge by the lessor, the Court ruled that the lease, in requiring royalty of 10% of the sale price, was clear and unambiguous and required that the calculation be made on the gross sale price, including the 45 cent increase, with no deductions. *Id.* at 217. The Court reasoned that the defendant's interpretation:

> would place upon plaintiffs the ordinary risks of the business which they clearly did not assume. If a community of profits governed, the relation would be in the nature of a partnership. Plaintiffs did not rely upon the defendant for careful and economic conduct of its business. They have no voice or control in its policies. They were not concerned

> with the salaries of its officers and the wages of its employees. Whether the business was operated at a loss or profit was of no moment to them, except the laudable concern of a landlord for the success of the tenant.

Id. at 216.

With respect to commissions, which were deducted as post-production costs, the Court held they were "a necessary part of its business ...so far as the payment of royalties is concerned" and were not deductible from royalty. *Id.* at 217.

These cases demonstrate the consistent adherence by this Court to the proposition that with regard to mineral royalties, whether for coal or gas, the lessee must bear all costs of operations, including "post-production" costs. While Defendant argues that its duty to the royalty owners ends with production when the gas is brought to the surface, that argument only holds water in cases such as the Texas line of cases that this Court refused to adopt in *Tawney.* In West Virginia, Defendant's duty does not stop at the wellhead. Defendant is still obligated to market and sell the gas, and Defendant must do so without charging those costs to the Plaintiffs and others like them. Otherwise, as explained in *Kohlstaat, supra,* Defendant places upon Plaintiffs the ordinary risks of the business which they clearly did not assume. If a community of profits governed, the relation would be in the nature of a partnership. Defendant's post-production costs are a necessary part of its business and are not deductible from Plaintiffs' royalties.

These early cases are in accord with the authorities relied upon by this Court in *Wellman* and *Tawney, supra.* *Wellman* and *Tawney* did not announce new law. They applied existing precedent. What is important under all of the cases is the lessees' obligation to pay the lessors' their royalties free of costs, including the relevant statute. Lessors' royalties are to be paid free of costs regardless of the place of sale, unless expressly provided for otherwise. This is well-

settled under West Virginia law and it was also settled law at the time § 22-6-8 was enacted. The place of sale may have changed for the lessors, but their duty under West Virginia law remained and remains the same. Just as in *Kohlstaat, supra,* what the government does to affect the industry, is of no moment to the Plaintiffs here, except the laudable concern of a landlord for the success of the tenant. The industry changes caused by deregulation do not affect the relationship between the Lessors and Lessee. The obligations under the law with respect to their relationship remain, and post-production costs are a necessary part of Lessee's business and are therefore not deductible from royalties.

Furthermore, Defendant's reliance upon *Wellman* and *Cotiga Dev. Co. v. United Fuel Gas Co.,* 128 S.E.2d 626 (1962) for the proposition that at the wellhead meant a lessor could take deductions is misplaced. The Court in *Tawney* rejected the same argument Defendant attempts to make here with respect to *Wellman* because it was mere dicta. *See Tawney,* at 273, 29. Further, the issue in *Cotiga* was United Fuel's obligation to pay royalty at the rate received or sale price, as required by its lease, rather than the market value of gas in the field, the issue was not addressed in Cotiga. *Cotiga*, at 635-636.

Therefore, whether an analysis reviewing the intent of the statute by its own terms or reviewing the existing common law in the state of West Virginia, the at the wellhead language does not alter that intent such that it allows the lessees to take deductions from the 1/8 guaranteed by *W. Va. Code*, § 22-6-8.

D. The Court Should Address The Second Certified Question

Defendant first asserts that this Court should not address the second certified question because the Plaintiffs have not challenged the validity of their flat-rate lease and, in fact, have stipulated or ratified that their lease is valid. Defendant fails to note that this position is contrary

to the facts as found by the District Court. While the certification statute certainly grants this Court the right to reformulate certified questions, W.Va.Code § 51-1A-4 (1996), it does not grant the Court the right to reformulate the statement of facts submitted by the District Court. *See* W.Va.Code §§ 51-1A-1 *et seq.* Moreover, Defendant also fails to acknowledge that the District Court ruled against its argument that the Plaintiffs had stipulated or ratified the validity of their lease so as to prohibit or estop the claims raised in this lawsuit. J.A., Order, at 608-10. No certified question of law concerning this issue has been submitted to this Court by the District Court. Accordingly, this argument by the Defendant is a "red herring."

It should also be noted that a number of decisions cited by the Defendant may be distinguishable because they address issues raised by certified questions submitted from West Virginia Circuit Courts under W.Va.Code § 58-5-2 and not certified questions submitted from a federal court under the Uniform Certification of Law Act set forth in W.Va.Code §§ 51-1A-1 *et seq.* *See, e.g., Bass v. Coltelli*, 192 W.Va. 516, 521, 453 S.E.2d 350, 355 (1994) (addressing appropriateness of certified questions submitted under § 58-5-2). Obviously, to the extent that a certified question submitted under § 58-5-2 addresses the sufficiency of a pleading, this Court would be required to examine the sufficiency of the pleading at issue, including the facts alleged therein. However, that is not the certified question asked by the District Court. Moreover, this Court has also acknowledged that even when addressing a certified question of law under § 58-5-2, it cannot decide questions of fact. Rather, any such questions of fact must be resolved by the certifying court. *Toler v. Shelton*, 159 W.Va. 476, 481, 223 S.E.2d 429, 432 (1976); Syl. Pt. 1, *State v. Stout*, 142 W.Va. 182, 95 S.E.2d 639 (1956); *State v. Brown*, 159 W.Va. 438, 441, 223 S.E.2d 193, 195 (1976); *Consolidation Coal Co. v. Mineral Coal Co.*, 147 W.Va. 130, 145, 126 S.E.2d 194, 203 (1962).

Accordingly, for the above reasons as well as principles of comity and federalism, Plaintiffs submit that this Court should not refuse to answer Certified Question No. 2 on the basis that the Complaint or factual record does not support the question. Having said the above, Plaintiffs do not deny that this Court in *Abrams v. West Virginia Racing Commission*, 164 W.Va. 315, 263 S.E.2d 103 (1980), declined to answer a certified question concerning whether a specific state stature and rule violated the respective Due Process Clauses of the Federal or State Constitutions. The Court reached this conclusion, in part, because "[a] resolution by a state court of a federal constitutional claim is not binding on the federal courts[ ] . . . [and] any such resolution by this Court on th[e] State constitutional issue would not foreclose the federal court from deciding upon a different federal standard and ignoring our State constitutional standard." *Abrams*, 164 W.Va. at 318-19, 263 S.E.2d at 106 (citations omitted). However, there are several reasons why this Court should not refuse to answer Certified Question No. 2 on this basis.

First, even should this Court refuse to address the constitutional questions raised by the respective Contracts Clauses of the federal and state constitutions, this Court can answer the question as stated (or though reformulation) in a manner which does not resolve the constitutional analysis. As currently formulated, Certified Question No. 2 does not mention either of the respective Contract Clauses of the federal or state constitutions. However, the language of W.Va.Code § 22-6-8(a)(4) does expressly mention such clauses.

As argued by Plaintiffs in their initial brief and as concluded by Judge Evans in *Estate of Tawney v. Columbia Natural Resources, LLC*, Civil Action No. 03-C-10E, 2006 WL 6056969 (W.Va.Cir.Ct. Aug. 4, 2006), this Court can conclude that it was the intention of the Legislature to prohibit the continued uses of flat-rate leases to the fullest extent constitutionally permitted and that the Legislature was encouraging courts, consistent with their respective constitutional

duties and principles of separation of powers, to conduct the constitutional analysis necessary to determine whether the Contract Clauses of the federal or state constitutions would prohibit or allow a retroactive application of its declared public policy to all pre-existing flat-rate leases, including those where no activities requiring the issuance of a new permit have occurred since enactment of the statute.

Of course, analyses of the respective Contracts Clauses must occur before the ultimate conclusion can be reached as to whether such flat-rate leases can be abrogated or otherwise converted, modified, or reformed to meet the public policy of West Virginia. For reasons stated in *Abrams*, *supra*, this Court could refuse to determine whether the Contracts Clause of the West Virginia Constitution would be violated by retroactively applying the public policy set forth in the Statute and require the District Court to conduct both analyses on its own. However, Plaintiffs submit that the Court should not so refuse.

More specifically, the Court in *Abrams* also based its ruling upon the following reason:

> [T]he United States Supreme Court stated in *Zwickler v. Koota*, 389 U.S. 241, 248, 88 S.Ct. 391, 395, 19 L.Ed.2d 444, 450 (1967):
>
> "In . . . expanding federal judicial power, Congress imposed the duty upon all levels of the federal judiciary to give due respect to a suitor's choice of a federal forum for the hearing and decision of his federal constitutional claims. Plainly, escape from that duty is not permissible merely because state courts also have the solemn responsibility, equally with the federal courts, '. . . to guard, enforce, and protect every right granted or secured by the constitution of the United States . . . ,' (citation omitted) . . . ."
>
> * * *
>
> . . . To repeat the rule of Zwickler v. Koota, 389 U.S. 241, 248, 88 S.Ct. 391, 395, 19 L.Ed.2d 444, 450 (1967), a federal court must give "due respect to a suitor's choice of a federal forum for the . . . decision of his federal constitutional claims." Congress imposed this duty on the federal courts, not state courts.
>
> We, therefore, conclude that where a certification request is made to this Court by a federal court under W.Va.Code, 51-1A-1, Et seq., with respect to a question involving a federal constitutional issue which cannot be limited or avoided by our resolution of ambiguous or peculiar State law, *we will ordinarily*

> *decline* the certification request, since the federal courts are charged with the primary duty of interpreting the Federal Constitution.

Abrams, 164 W.Va. at 106-08, 263 S.E.2d at 318-22 (emphasis added).

Unlike the plaintiff in *Abrams*, the Plaintiffs in this case did not choose a federal forum to assert a federal constitutional claim for resolution. Plaintiffs filed their lawsuit in state court and did not expressly assert any federal claim. Defendants chose to remove the civil action to federal court on the basis of diversity jurisdiction. The federal constitutional claim arises more as a potential defense to one of the claims. This difference constitutes a basis upon which to distinguish *Abrams* and for this Court to change its "ordinary" practice.

Moreover, the Court in *Abrams* failed to acknowledge that the federal court could decide that the federal constitutional provision is not violated by the statute and, therefore, be forced to decide the state constitutional issues as well. Both this Court and the United States Supreme Court have recognized that a State may grant its citizens greater constitutional protections than those granted by the federal constitution. *Connecticut v. Johnson*, 460 U.S. 73, 81 n. 9 (1983); Syl. Pt. 1, *Women's Health Center of West Virginia, Inc. v. Panepinto*, 191 W.Va. 436, 446 S.E.2d 658 (1993); Syl. Pt. 2, *Pauley v. Kelly*, 162 W.Va. 672, 255 S.E.2d 859 (1979); Syl. Pt. 1, *State v. Bonham*, 173 W.Va. 416, 317 S.E.2d 501 (1984). While this Court has appeared to adopt the same framework for addressing whether the West Virginia Constitution's Contracts Clause is violated as does the United States Supreme Court for determining whether the United States Constitution's Contracts clause is violated, *see Shell v. Metropolitan Life Ins. Co.*, 181 W.Va. 16, 19, 380 S.E.2d 183, 186 (1989), the District Court could be required to address the State constitutional issue at the very least to opine that the same result occurs as found when addressing the federal constitutional question. Plaintiffs, who initially filed this action in state court, submit that they should be entitled to receive the opinion of this Court which has the

ultimate responsibility to decide issues of the state constitution as opposed to issues of the federal constitution.

E. The Contracts Clause Is Not Violated By Retroactively Applying The Public Policy Set Forth in W.Va.Code § 22-6-8

Defendant submits that both the state and federal Contracts Clauses would be violated by applying the public policies in § 22-6-8 to invalidate flat-rate leases. In this connection, Defendant argues both that a substantial impairment would occur and that the flat-rate statute is not directed at eliminating windfall profits. Neither argument of the Defendant has merit.

As previously argued by Plaintiffs and as previously found by Judge Evans in *Estate of Tawney*, *supra*, courts have concluded that "state regulation that restricts a party to gains it reasonably expected from the contract does not necessarily constitute a substantial impairment." *Energy Reserves Group, Inc. v. Kansas Power and Light Co.*, 459 U.S. 400, 411 (1983). *Accord United States Trust Co. v. New Jersey*, 431 U.S. 1, 31 (1977); *El Paso v. Simmons*, 379 U.S. 497, 515 (1965); *Shell*, 181 W.Va. at 21, 380 S.E.2d at 188 (same, quoting *Energy Resources Group*). As cited by Plaintiffs in its initial brief and as found by Judge Evans, when natural gas was first discovered it was of little or no value and its discovery was considered more of a burden than a blessing. Accordingly, if it was never the reasonable expectation or intention of lessees to obtain such windfall profits, it cannot be a substantial impairment of their rights to modify or adjust the contract to reflect the realities of the modern world and to achieve what the parties desired and intended all along—a reasonable price and consideration for the production and marketing of any natural gas. *See Estate of Tawney v. Columbia Natural Resources, LLC*, 2006 WL 6056969 at *__, Slip Op. at pp. 6-9.

Contrary to the Defendant's argument, it is impossible to reasonably conclude that the public policy set forth in W.Va.Code § 22-6-8 is not designed to address and eradicate windfall

profits. W.Va.Code § 22-6-8(a)(2) ("That continued exploitation of the natural resources of this state **in exchange for such wholly inadequate compensation is unfair, oppressive, works an unjust hardship on the owners of the oil and gas in place, and unreasonably deprives the economy of the state of West Virginia of the just benefit of the natural wealth of this state**" (emphases added)). It is simply absurd for the Defendant to even suggest otherwise.

Indeed, even if a substantial impairment is found, it cannot be disputed that West Virginia has a legitimate and significant public policy and that reasonable accommodation can be achieved by requiring the Defendant to convert, modify, or reform the flat-rate leases into 1/8th royalty leases, similarly to the conversion or modification required by the Statute for the issuance of new permits. *See Estate of Tawney v. Columbia Natural Resources, LLC*, 2006 WL 6056969 at *__, Slip Op. at p. 21.

Lastly, to the extent that the West Virginia Oil and Natural Gas Association, as *amicus curiae*, submits that some natural-gas owners may benefit more favorably with flat-rate leases than they would with 1/8th royalty leases as to low-producing wells, courts and parties can resolve such an issue on a case by case basis by conducting relevant discovery to ascertain the truth of such issue in a particular case. Certainly, the public policy of West Virginia will not be violated by the owners of natural gas receiving the higher of the amounts as royalty if such is indeed the case on occasion. On the other hand, if such is only the case because the producer is failing to honor the implied duties in law to produce and market the gas (instead choosing to hold onto the wells for potential future development or storage or any other reason which does not reasonably maximize current production), a contrary ruling can be reached by the Court, consistent with the applicable public policies.

Conclusion

Plaintiffs therefore request the Court for the reasons stated in the briefs to find that at the wellhead does not allow defendant to take deductions from the 1/8 royalty under the statute and that the Court order that the lease and rights thereunder for wells not converted be abrogated and for such other and further relief as the Court deems just and proper.

Respectfully Submitted,

PATRICK D. LEGGETT;
KATHERINE F. LEGGETT;
GEORGE D. MCKAIN, by his
attorney in fact, ANITA
KATHRYN MCKAIN GREER;
and ADELE S. MCDOUGAL,

By Counsel

Marvin W. Masters
West Virginia State Bar No. 2359
Richard A. Monahan
West Virginia State Bar No. 6489
April D. Ferrebee
West Virginia State Bar No. 8034
The Masters Law Firm lc
181 Summers Street
Charleston, West Virginia 25301
304-342-3106

Michael W. Carey
West Virginia State Bar No. 635
Carey, Scott, Douglas & Kessler, PLLC
707 Virginia Street East, Suite 901
Charleston, West Virginia 25301
304-345-1234
Counsel for Plaintiffs
F:\5\864\b011.docx

IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA
DOCKET NO. 16-0136

PATRICK D. LEGGETT;
KATHERINE F. LEGGETT;
GEORGE D. MCKAIN, by his
attorney in fact, ANITA
KATHRYN MCKAIN GREER;
and ADELE S. MCDOUGAL,

Plaintiffs,

v.

Civil Action No. 1:13-cv-0004 FPS
(U.S. District Court, Northern District)

EQT PRODUCTION COMPANY,
a Pennsylvania corporation;
EQT CORPORATION,
a Pennsylvania corporation;
EQT ENERGY, LLC, a
Delaware limited liability company;
EQT INVESTMENTS HOLDINGS, LLC, a
Delaware limited liability company;
EQT GATHERING, LLC, a
Delaware limited liability company; and
EQT MIDSTREAM PARTNERS, LP,
a Delaware limited partnership,

Defendants.

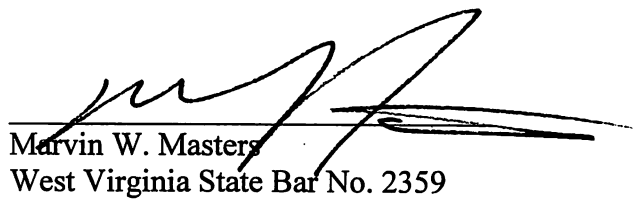
CERTIFICATE OF SERVICE

I, Marvin W. Masters, counsel for plaintiffs, do hereby certify that on August 15, 2016, true and exact copies of the foregoing "Petitioners' Reply Brief" were served upon:

David K. Hendrickson
Carl L. Fletcher, Jr.
Hendrickson & Long PLLC
Post Office Box 11070
Charleston, West Virginia 25339
Counsel for Defendants

Michael W. Carey
Carey, Scott, Douglas & Kessler, PLLC
707 Virginia Street East, Suite 901
Charleston, West Virginia 25301
Co-Counsel for Plaintiffs

via electronic mail and in envelopes properly addressed, stamped and deposited in the regular course of the United States Mail, this 15th day of August, 2016.



Marvin W. Masters
West Virginia State Bar No. 2359

F:\5\864\xsupremecourt.docx