IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

No. 21-0179 0729

SWN PRODUCTION COMPANY, LLC and EQUINOR USA ONSHORE PROPERTIES INC.,

Defendants Below, Petitioners,

v.

CHARLES KELLAM, PHILLIS KELLAM, and other persons and entities similarly situated,

Plaintiffs Below, Respondents.

Upon Certified Questions from the United States District Court for the Northern District of West Virginia Case No. 5:20-cv-85

AMICUS CURIAE BRIEF OF THE WEST VIRGINIA LAND AND MINERAL OWNERS ASSOCIATION AND WEST VIRGINIA ASSOCIATION FOR JUSTICE IN SUPPORT OF RESPONDENTS

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STATEMENT OF IDENTITY OF *AMICI CURIAE*, THEIR INTERESTS IN THIS CASE, AND SOURCE OF AUTHORITY TO FILE[1]

The West Virginia Land and Mineral Owners Association ("WVLMOA"), is an association with over 80 landowner members, interested in issues affecting the ownership of mineral interests and real property in West Virginia, including, but not limited to, royalty interests in oil and gas estates. WVLMOA's mission focuses on promoting positive land management practices, lobbying public issues that affect land and mineral ownership, and providing members with valuable educational and networking opportunities that can increase their effectiveness in the natural resource marketplace. The association was established by concerned West Virginians who recognized the need for a collective voice to protect and advance the interests of land and mineral owners within our state.

The West Virginia Association for Justice ("WVAJ") is a voluntary bar association for attorneys licensed to practice in West Virginia and paralegals. WVAJ and its members are committed to protecting access to our state and federal courts, our civil justice system and our 7th Amendment right to jury trial. Founded in 1959, WVAJ represents approximately 500 attorneys practicing in West Virginia and surrounding states. Every day they seek justice in our courts for those who have been harmed physically and financially by the conduct and negligence of others. Their work has established safer workplaces, employee rights, safer products, better healthcare, consumer-protection law, property owners' rights, a cleaner environment and increased corporate responsibility. WVAJ is committed to providing West Virginians with quality legal representation.

[1]Pursuant to W. Va. R. App. P. 30(e)(5), WVLMOA and WVAJ state that no counsel for any party authored this *amicus curiae* brief, in whole or in part, and no party or its counsel made a monetary contribution specifically intended to fund the preparation or submission of this *amicus curiae* brief. No person other than the *amici*, their members, or their counsel made such a monetary contribution.

WVLMOA and WVAJ respectfully request the Court consider this brief submitted on the certified questions presented to the Court. WVLMOA and WVAJ have provided counsel for all parties with notice of their intent to file this amicus brief at least five (5) days prior to the filing of the due date for the brief of the Respondents in accordance with W. Va. R. of App. P. 30(b). Pursuant to Rule 30(a), all parties have consented to the filing of this brief.

SUMMARY OF ARGUMENT

This Court should unhesitatingly answer the District Court's Certified Question No. 1—which asks whether *Tawney v. Columbia Natural Resources, L.L.C.*, 219 W. Va. 266, 633 S.E.2d 22 (2006) remains good law—in the affirmative. Not only does the Court's decision in *Tawney* stand on firm legal ground, but both *Tawney* and its precursor, *Wellman v. Energy Resources, Inc.*, 210 W. Va. 200, 557 S.E.2d 254 (2001), have been relied upon by parties to oil and gas lease contracts for more than two decades, and the wholesale abandonment of what is now well-established law would cause great harm to royalty owners, including members of WVLMOA, who have depended on the default rules articulated by the Court in these cases to conduct their affairs, including when negotiating new lease agreements or amending existing lease agreements to allow for pooling and unitization of horizontal wells.

As to the Questions Nos. 2 and 3, which effectively ask the Court to decide whether a mere listing of deductible post-production costs in a lease is sufficient to meet *Tawney's* requirements, this Court should reject the approach taken by the Fourth Circuit in *Young v. Equinor USA Onshore Properties, Inc.*, 982 F.3d 201 (4^{th} Cir. 2020), and conclude that *Tawney's* third prong demands that a lease contain an objective statement of the methodology to be used in allocating post-production costs—one that both binds the lessee and gives fair notice to the royalty owner.

Finally, Question No. 4's query concerning whether indirect costs may be deducted from royalties should be answered by holding that such costs, whether they take the form of salaries, office overhead, pipeline construction, or a hundred other incidental costs of doing business, are not directly responsible for bringing oil or gas to market or increasing its value, and should not be permitted to be deducted from royalties.

ARGUMENT

I. THE COURT SHOULD ANSWER CERTIFIED QUESTION NO. 1 IN THE AFFIRMATIVE AND CONFIRM THAT WELLMAN AND TAWNEY REMAIN GOOD LAW.

Echoing criticisms expressed in dicta by the majority of the Court in *Leggett v. EQT Production Co.*, 239 W. Va. 264, 800 S.E.2d 850 (2017), Petitioners and the *amici curiae* aligned with them broadly challenge the continued validity of both *Tawney* and *Wellman*. The Court should answer the District Court's Certified Question No. 1 in the affirmative and confirm that *Wellman* and *Tawney* remain controlling authority and that West Virginia follows the marketable-product rule adopted and applied in those cases. Not only are these cases soundly reasoned and in accord with the trend of authority from other states regarding the issue of allocating post-production expenses, but the doctrine of *stare decisis* strongly supports the Court adhering to the holdings of these cases because over twenty years have elapsed since the marketable-product rule was adopted in West Virginia, during which time thousands of West Virginia royalty owners have relied upon these cases to determine their rights and otherwise conduct their affairs, including when negotiating new lease agreements or amending existing lease agreements to allow for pooling and unitization of horizontal wells.

A. The Doctrine of *Stare Decisis* Strongly Favors Upholding *Wellman* and *Tawney*.

Even if there are significant faults with regard to the reasoning employed by the *Wellman* and *Tawney* Courts (which, as discussed anon, there are not), the doctrine of *stare decisis* strongly favors the Court continuing to adhere to the holdings in those cases. Over twenty years have elapsed since the marketable-product rule and related guidelines were formally adopted by these cases, during which time thousands of West Virginia landowners have relied upon them to understand and determine their rights under new and amended lease agreements. Importantly, the so-called "Shale Revolution" of the past two decades, which has seen a rapid expansion in oil and gas production in West Virginia's Marcellus and Utica shale formations, has resulted in thousands of landowners in this state entering into new and amended mineral leases with producers.[2] To suddenly change the rules regarding what lease language is necessary to impose responsibility for post-production costs would be highly detrimental to these land and mineral owners and would otherwise disrupt the contractual expectations that have developed since *Wellman* and *Tawney* were decided.

As this Court has long recognized, the doctrine of *stare decisis* counsels that "[v]ery weighty considerations underlie the principle that courts should not lightly overrule past decisions." *Meadows v. Meadows*, 196 W. Va. 56, 64, 468 S.E.2d 309, 317 (1996) (quoting *Moragne v. States Marine Lines, Inc.*, 398 U.S. 375, 403 (1970)). *Stare decisis* "is the preferred course because it promotes the evenhanded, predictable, and consistent development of legal principles, fosters reliance on judicial decisions, and contributes to the actual and perceived integrity of the judicial process." *Payne v. Tennessee*, 501 U.S. 808, 827 (1991).

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[2]The use of horizontal drilling techniques to reach these deep oil and gas formations often involves producing gas from several properties, thus implicating multiple existing lease agreements. The related need to obtain consent to pooling from the holders of royalty interests caused many producers to renegotiate and modify the royalty provisions of existing leases. Consequently, even where pre-*Wellman* oil and gas leases are involved, in many cases landowners have made decisions regarding the express terms of such lease agreements based upon the Court's decisions in *Wellman* and *Tawney*. And the Court's recent decision in *Gastar Expl., Inc. v. Contraguerro*, 239 W. Va. 305, 800 S.E.2d 891 (2017) (holding that the validity of pooling provisions in oil and gas leases and designated pooling units are not dependent upon the consent and ratification of nonparticipating royalty holders), did not change that fact, since there is the still the need to obtain pooling agreements from those landowners with executory rights in properties under leases that do not contemplate pooling.

Three factors must be weighed in the *stare decisis* analysis prior to rejection of a longstanding rule:

> "[1] the desirability that the law furnish a clear guide for the conduct of individuals, to enable them to plan their affairs with assurance against untoward surprise; [2] the importance of furthering fair and expeditious adjudication by eliminating the need to relitigate every relevant proposition in every case; and [3] the necessity of maintaining public faith in the judiciary as a source of impersonal and reasoned judgments."

Meadows, 468 S.E.2d at 317 (quoting *Moragne*, 398 U.S. at 403) (alterations in original). "While the principle of *stare decisis* admits of exception, deviation from its application should not occur absent some urgent and compelling reason." *Dailey v. Bechtel Corp.*, 157 W. Va. 1023, 1029, 207 S.E.2d 169, 173 (1974); *see also Hilton v. South Carolina Pub. Ry. Comm'n*, 502 U.S. 197, 202 (1991) ("For all of the[] [reasons] supporting the application of *stare decisis*, we will not depart from the doctrine of *stare decisis* without some compelling justification."). Thus, the proponent of overruling the prior case must articulate a strong reason to have a court overrule prior cases.

All three of the *Meadows* factors weigh heavily in favor of not disturbing the core holdings of either *Wellman* or *Tawney*. Importantly, the "clear guide" provided by *Wellman* and *Tawney* as to what lease language is required to shift responsibility for post-production costs has no doubt informed the conduct of individual royalty owners in West Virginia, who have relied upon such decisions to inform their choices as to form and content of the express terms of mineral leases entered into with oil and gas producers in the more than twenty years since the marketable-product rule was first adopted in this state.

Moreover, oil and gas producers have adjusted to the requirements imposed by *Wellman* and *Tawney* by, in most instances, reviewing their existing lease agreements and paying royalties in accord with the requirements imposed by those cases. If the Court were to backtrack at this juncture and remove the protections afforded by *Wellman* and *Tawney*, there is little doubt that producers will proceed to reevaluate their leases and attempt to impose unilateral offsets against current royalties to recoup deductions that were not previously taken as to past production—offsets that could reach back years if not decades. It is therefore entirely conceivable that the wholesale abandonment of *Wellman* and *Tawney* would result in many thousands of West Virginia royalty owners seeing their mineral-related incomes slashed to nothing for the foreseeable future. The untold hardships that would be imposed upon West Virginias—many of moderate means—by such a result is impossible to imagine.

The doctrine of *stare decisis* has its greatest force in circumstances where, like here, overturning established precedent will unquestionably disturb settled expectations: "Predictability is at the heart of the doctrine of *stare decisis*, and regardless of what we think of the merits of [a particular] case, we must be true to a reasonable interpretation of prior law in the area of property where certainty above all else is the preeminent compelling public policy to be served." *Hock v. Morgantown*, 162 W. Va. 853, 856, 253 S.E.2d 386, 388 (1979). As the United States Supreme Court has recognized:

> *Stare decisis* has added force when the legislature, in the public sphere, and citizens, in the private realm, have acted in reliance on a previous decision, for in this instance overruling the decision would dislodge settled rights and expectations or require an extensive legislative response.

Hilton, 502 U.S. at 202; *see also State Oil Co. v. Khan*, 522 U.S. 3, 20 (1997) ("*stare decisis* concerns are at their acme in cases involving property and contract rights") (citing *Payne*, 501 U.S. at 828); *United States v. Mason*, 412 U.S. 391, 399-400 (1973) ("[I]f the doctrine of *stare decisis* has any meaning at all, it requires that people in their everyday affairs be able to rely on our decisions and not be needlessly penalized for such reliance.").

Not only have lessor royalty owners and lessee producers spent the past two decades adjusting their affairs to the requirements of *Wellman* and *Tawney*, but the West Virginia

Legislature too has embraced the rules enunciated in those cases. Following the Court's issuance of its final opinion in *Leggett* on May 26, 2017, the Legislature responded the next legislative session by passing Senate Bill 360, which legislatively overruled *Leggett* by amending the flat-rate statute, West Virginia Code § 22-6-8, to, as described in the bill's title, "clarify the royalty owed to a royalty owner in an oil and gas lease." S.B. 360, 83d Leg., Reg. Sess. (W. Va. 2018). More specifically, Senate Bill 360 amended § 22-6-8(e) by changing the statute's royalty basis from the "total amount . . . at the wellhead"—the language that the *Leggett* Court construed—to "the gross proceeds, free from any deductions for post-production expenses, received at the first point of sale to an unaffiliated third-party purchaser in an arm's length transaction." Thus, as to royalty owners having an interest in flat-rate leases, there is no question that the Legislature intended that they should be give the same protections afforded other royalty owners under *Wellman* and *Tawney*.[3] Overturning *Wellman* and *Tawney* at this juncture would thus have the anomalous result that some lessors under flat-rate leases would effectively have many of the rights and protections espoused in *Wellman* and *Tawney*, while the bulk of royalty owners would be left to circumstances that the Legislature clearly deemed to be inadequate.

What exists today bears no relation to the "chaos" in the law as described by the *Leggett* Court. *See Leggett*, 234 W. Va. at 277, 800 S.E.2d at 863 (citation omitted). Instead, royalty owner lessors, gas producer lessees, and the Legislature have responded in an orderly fashion to the law established by *Wellman* and *Tawney*, to the point where an equilibrium now exists. If

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[3]Given that the Legislature's amendment of § 22-6-8 was done with the intent to clarify existing law, such amendment has retroactive application. *See, e.g., Kay Co., LLC v. EQT Prod. Co.*, No. 1:13-CV-151, ECF No. 723 at 22 (N.D.W. Va. Nov. 14, 2018) ("In essence, the clarifying amendment confirms that the law all along was that post-production costs could not be deducted from the 1/8 royalty payable to converted flat rate leases."); *see generally*, Adam H. Wilson, Note, *Without a* Leggett *To Stand On: Arguing For Retroactive Application Of West Virginia's Amended Flat-Rate Well Statute*, 124 W. Va. L. Rev. 259, 287-89 (2021).

anything, the specificity now required before post-production expenses can be allocated to lessors will ultimately reduce the number of disputes concerning what deductions can and cannot be taken. To now wholesale jettison what has been established law for over two decades would create its own chaos—turmoil that have a severe negative impact upon individual landowners and spawn an entirely new generation of litigation.

In sum, overruling *in toto* the holdings in *Wellman* and *Tawney* and abrogating the marketable-product rule and associated requirements would undoubtedly undermine the long-settled expectations of West Virginia royalty owners, and in so doing would also weaken public faith in the judiciary as a source of reasoned judgments capable of guiding West Virginians in their daily affairs. Consequently, even if there is fault with the holdings in either *Wellman* or *Tawney* (which there is not, as discussed below), the Court should nevertheless retain the core principles enunciated in these cases, including adherence to the marketable-product rule.

B. The Court's Opinions in *Wellman* and *Tawney* are Well-Reasoned, Follow the Trend of Cases in Other Jurisdictions, and Should be Upheld.

Petitioners and the *amici curiae* supporting their position sweepingly request that the Court fully overrule its holdings in *Wellman* and *Tawney* and in so doing both abrogate the marketable-product rule adopted in *Wellman* and abandon the practical application of such rule as explicated in *Tawney*. There is no question that the law underlying these cases has not yet been fully developed in this jurisdiction, and that application of the marketable-product rule will require further refinement as the case law develops, but the core holdings of these cases are unassailable and should be upheld in the face of the current challenge.

1. *Wellman* is Good Law.

In the first instance, it is important to disentangle *Wellman* and *Tawney*. In *Wellman*, the Court addressed the question of the apportionment of post-production costs in the context of a lease providing for, as to gas sold by the lessee, a one-eighth royalty "of the proceeds from the sale of gas as such at the mouth of the well." *Wellman*, 557 S.E.2d at 258. The lessee had taken deductions for the cost of transporting the gas from the wellhead to the point of sale, as well as the cost of treating the gas to make it marketable.

In answering the question of whether such deductions were appropriate, the *Wellman* Court considered the conflicting authority from other jurisdictions on the issue of allocating post-production costs and adopted the so-called "marketable-products rule," which holds that "the duty to market embraces the responsibility [of the lessee] to get the oil or gas in marketable condition and actually transport it to market." *Id.* at 264. Specifically, the Court stated that "West Virginia holds that a lessee impliedly covenants that he will market oil or gas produced. . . . It, therefore, reasonably should follow that the lessee should bear the costs associated with marketing products produced under a lease." *Id.* at 265. The Court went on to hold that "if an oil and gas lease provides for a royalty based on proceeds received by the lessee, ***unless the lease provides otherwise***, the lessee must bear all costs incurred in exploring for, producing, marketing, and transporting the product to the point of sale." *Id.* (emphasis added). The Court also observed that if a lease does provide for the deduction of post-production costs, the lessee could deduct those costs from royalties "to the extent that they were actually incurred and they were reasonable." *Id.*

The Court in *Wellman* concluded that while the applicable lease language "might" indicate that the lessors were required to bear some of the costs of transporting the gas from the wellhead to the point of sale, the lessee's failure to offer any evidence demonstrating that its deductions were actually incurred or reasonable precluded it from prevailing. *Id.* at 265. In essence, *Wellman* merely provides a default rule regarding the allocation of post-production costs where the lease is otherwise silent. *See* Robert S. Raynes, Jr., Note, *A Royalty Pain in the Gas: What Costs May Be*

Properly Deducted From A Gas Royalty Interest?, 98 W. Va. L. Rev. 1199 (1996).

The relatively simple question asked and answered in *Wellman* leaves little room for criticism. The primary criticism leveled pertains to its use of the implied covenant to determine responsibility for such costs. *Leggett* commented that *Wellman's* "use of the implied covenant to market to reach the issue of cost allocation is highly questionable." *Leggett*, 800 S.E.2d 850 at 861 n.15. But that comment was made with no discussion whatsoever regarding West Virginia law, and Petitioners have been no more thorough, simply citing two journal articles and stating that the "implied covenant is limited to a duty to sell gas at a reasonable price, and bears no relationship to whether a lease permits deducting post-production costs from royalty." Pet'r Br. at 19. But this runs counter to *Wellman's* observation that "West Virginia [law] holds that a lessee impliedly covenants that he will market oil or gas produced." 557 S.E.2d at 265 (citing Robert Tucker Donley, *The Law of Coal, Oil and Gas in West Virginia and Virginia* §§ 70 & 104 (1951).[4] Nor is there any reason why, where a lease is silent as to the allocation of post-production costs, that the party charged with discharging a particular covenant, whether express or implied, should not bear the costs associated with such performance. As the *Wellman* Court rightly observed, "[l]ike the courts of Colorado, Kansas, and Oklahoma, the Court also believes that historically the lessee has had to bear the cost of complying with his covenants under the lease." *Id.* This would include both the cost of processing the gas to make it marketable, as well as moving it to a location

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[4]Indeed, this Court recognized long before *Wellman* that "[t]he owner of a lease for the production of oil and gas, containing the usual terms and conditions, must, if either mineral is found in paying quantities on or near the lands leased, exercise due and reasonable diligence, in prosecuting operations thereunder, for the mutual benefit of himself and the landowner . . . ." Syl. Pt. 1, in part, *Jennings v. S. Carbon Co.*, 80 S.E. 368 (W. Va. 1913); *see also Hall v. S. Penn Oil Co.*, 76 S.E. 124, 124 (W. Va. 1912) ("Courts everywhere recognize an implied covenant on the part of the lessee in oil and gas leases to operate the mines or leased property for the mutual benefit of both parties thereto."); *Blue Creek Dev. Co. v. Howell*, 133 S.E. 699, 704 (W. Va. 1926) (lessee impliedly bound by what "could reasonably be expected of operators of ordinary prudence").

where it becomes marketable. *See* Owen L. Anderson, *Royalty Valuation: Should Royalty Obligations be Determined Intrinsically, Theoretically, or Realistically? (Part 2)*, 37 Nat. Res. J. 611, 634 (1997).[5]

In short, there is no basis for the Court to revisit and overturn the *Wellman* Court's adoption of the marketable-product rule, which rule has been adopted either by case law or statute in numerous jurisdictions. *See Sternberger v. Marathon Oil Co.*, 894 P.2d 788, 799 (Kan. 1995) ("The lessee has the duty to produce a marketable product, and the lessee alone bears the expense in making the product marketable."); *Garman v. Conoco, Inc.*, 886 P.2d 652, 659 (Colo. 1994) (en banc) ("[T]he implied covenant to market obligates the lessee to incur those post-production costs necessary to place gas in a condition acceptable for market."); *Wood v. TXO Prod. Co.*, 854 P.2d 880, 882 (Okla. 1992) ("[T]he lessee's duty to market ... include[s] the cost of preparing the gas for market."); Mich. Comp. Laws Ann. § 324.61503b(1) ("A person who enters into a gas lease as a lessee after March 28, 2000 shall not deduct from the lessor's royalty any portion of postproduction costs unless the lease explicitly allows for the deduction of postproduction costs."); *see generally* John Burritt McArthur, *Some Advice on* Bice, *North Dakota's Marketable-Product Decision*, 90 N.D. L. Rev. 545 (2014).

Moreover, *Leggett's* statement that the *Wellman* and *Tawney* Courts "refus[ed] to align with other states which have more fully developed this rule," 800 S.E.2d at 863, is simply wrong. Neither *Wellman* nor *Tawney* expressly staked out a path that diverges from that taken by other

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[5]*See also Rogers v. Westerman Farm Co.*, 29 P.3d 887, 906 (Colo. 2001) ("Absent express lease provisions addressing allocation of costs, the lessee's duty to market requires that the lessee bear the expenses incurred in obtaining a marketable product. Thus, the expense of getting the product to a marketable condition ***and location*** are borne by the lessee.") (emphasis added); *TXO Prod. Corp. v. State ex rel. Comm'rs of Land Office*, 903 P.2d 259, 262–63 (Okla. 1994) (holding that post-production costs of compression, dehydration, and gathering were not deductible from royalties because these costs were necessary to deliver the gas to market).

states adopting the marketable-product rule. Rather, the law in this area suffers from a dearth of development simply because related issues have not made their way to this Court. Of course, other courts within West Virginia have been applying *Wellman* and *Tawney* for the past two decades, in some cases taking steps to, either rightly or wrongly, put West Virginia law more on par with those jurisdictions whose marketable-product rule is, in *Leggett's* words, "more fully developed." *See, e.g., W.W. McDonald Land Co. v. EQT Production Co.*, 983 F.Supp.2d 790, 802 (2013) (concluding "that lessees have an implied duty to bear all post-production costs incurred until the gas reaches the market, which is the first place downstream of the well where the gas can be sold to any willing buyer and title passed to that buyer") (footnote omitted). There is simply no reason why the Court should make a U-turn and quash the development of the law in this area, particularly where, as discussed above in the context of the doctrine of *stare decisis*, the public has now relied for two decades upon this Court's decisions.

Finally, it must be stressed that this case does not directly implicate *Wellman* since the lease at issue is clear that the royalty is based upon "the price paid to Lessee," App. 57, and that the lessee is clearly responsible for all post-production costs other than, arguably, those "charges for transportation, dehydration and compression paid by Lessee to deliver the oil, gas, and/or coalbed methane gas for sale." What issues remain in this case go to the question of whether the language employed in the subject lease meets *Tawney's* specificity requirements so as to require the lessor to share in the costs of "transportation, dehydration and compression"—not whether the lessee is otherwise generally responsible for post-production costs.[6] This no doubt explains why

[6]This fact raises serious questions as to whether the Court has jurisdiction to consider the continued validity of *Wellman*, since it is not determinative of this case. Importantly, West Virginia Code § 51-1A-3, which gives this Court discretionary jurisdiction to answer certified questions of law, may only be resorted to "if the answer may be determinative of an issue in a pending cause in the certifying court and if there is no controlling appellate decision, constitutional provision or statute of this State."

the District Court's Question No. 1 asks only whether *Tawney* remains good law and why this Court should confine its review to such limited issue.

2. This Court Should Uphold *Tawney* Because it Provides Needed Protections to West Virginia Royalty Owners.

Going to the limited issue raised by Question No. 1, this Court should continue to adhere to *Tawney's* specificity requirements regarding what is required before a lessee can allocate post-production costs against a lessor's royalty. Importantly, while Petitioners and the *amicus curiae* who support their position level much criticism at *Tawney* regarding its interpretation of "at the well" lease language and statements concerning responsibility for and allocation of costs to the "point of sale," such issues are not relevant to the present case, where the royalty language at issue requires the lessee to pay royalties based upon proceeds received at the point of sale, not "at the well."

Tawney answered a question left in the wake of *Wellman*—what language is required in a lease in order to require the lessor to assume some responsibility for post-production costs? The *Tawney* Court first concluded that the subject "at the well" lease language was ambiguous, and then proceeded to apply long-recognized canons of contract interpretation. More specifically, the Court construed the lease language against the lessor, noting that "'[t]he general rule as to oil and gas leases ... that such contracts will generally be liberally construed in favor of the lessor, and strictly as against the lessee." *Tawney*, 219 W. Va. at 273, 633 S.E.2d at 29 (quoting Syl. Pt. 1, *Martin v. Consolidated Coal & Oil Corp.*, 101 W. Va. 721, 133 S.E. 626 (1926)). "Under our law, '[u]ncertainties in an intricate and involved contract should be resolved against the party who prepared it.'" *Id.* (quoting Syl. Pt. 1, *Charlton v. Chevrolet Motor Co.*, 115 W. Va. 25, 174 S.E. 570 (1934)).

The Court then proceeded to announce a three-pronged test to determine whether a lease "provide[s] otherwise" under *Wellman* so as to permit deductions from royalties for post-production costs:

> language in an oil and gas lease that is intended to allocate between the lessor and lessee the costs of marketing the product and transporting it to the point of sale must [1] expressly provide that the lessor shall bear some part of the costs incurred between the wellhead and the point of sale, [2] identify with particularity the specific deductions the lessee intends to take from the lessor's royalty (usually 1/8), and [3] indicate the method of calculating the amount to be deducted from the royalty for such post-production costs.

Id. at 274, 633 S.E.2d at 30 (alterations supplied).

Petitioners assert that these requirements were pulled from "thin air," and that the *Tawney* Court gave little in the way of guidance as to how they should be applied. Pet'r Br. at 23. As to the latter criticism, the common law has always developed incrementally, and this area of the law is no different. As to the former, there are good reasons for the Court to require the specificity set forth in *Tawney's* three-prong test.

This Court is apparently not alone in recognizing the need to protect unsophisticated mineral lessors. The Colorado Supreme Court in *Rogers v Westerman Farm Co*, 29 P.3d 887 (Colo. 2001), relied on the "against the lessee" rule of construction to support its conclusion that the defendant lessees could not use a workback methodology to calculate royalty payments. Like *Tawney*, the *Rogers* Court emphasized that it was "mindful of the generally accepted rule that oil and gas leases are strictly construed against the lessee in favor of the lessor." 29 P.2d at 901. The court noted further that "lessors are not usually familiar with the law related to oil and gas leases, while lessees, through experience drafting and litigating leases, generally are," *id.* at 902, and that "the bargaining power between a lessor and lessee is similar to that historically found between an insurance company and its customers." *Id.* Such concerns clearly informed the *Tawney* Court in formulating its three-prong test, and strongly support this Court continuing to adhere to it.

Interestingly, Petitioners clearly agree with the *Tawney* Court's application of the "against the lessee" rule in this context, since they cite the rule as support for rejecting the District Court's policy concerns regarding the need to broadly construe the *Tawney* test. Pet'r Br. at 25. And while Petitioners argue that the application of this rule of construction leaves "no need for *Wellman* and *Tawney* to impose additional presumptions against lessees on the specific issue of post-production costs," *id.* at 25-26, they otherwise supply no reason why the three-prongs of the *Tawney* test do not adequately reflect the criterion that should be used to determine whether, under *Wellman*, a lease "provide[s] otherwise" on the issue of post-production costs.

Finally, Petitioners submit a smorgasbord of issues that they would like to see resolved in the event this Court does not take the drastic step of overruling *Wellman* and *Tawney* in their entirety. *See* Pet'r Br. at 30-31. Petitioners are effectively requesting the Court to issue an advisory opinion concerning the application of *Wellman* and *Tawney* that has nothing to do with the issues raised by this case, which the Court clearly does not have jurisdiction to do. *See* W. Va. Code § 51-1A-3 and footnote 5, *supra.*

II. THE COURT SHOULD ANSWER CERTIFIED QUESTIONS NOS. 2 THROUGH 4 IN A MANNER THAT PROTECTS THE REASONABLE EXPECTATIONS OF ROYALTY OWNER LESSORS.

This Court should answer Certified Questions Nos. 2 through 4 in accord with the reasoning employed by the District Court.

A. The Court Should Reject the Fourth Circuit's Approach in *Young* and Require that Leases Make Clear the Methodology to Be Used to Account for Any Otherwise Permitted Deductions from Royalties.

Certified Questions Nos. 2 and 3 present two related issues involving the scope and meaning of *Tawney*:

> 2. What is meant by *Tawney's* requirement that the lease set forth the "method of calculating" any post-production costs to be deducted?

3. Is a simple listing of the types of costs which may be deducted sufficient to satisfy that requirement?

Tawney's third prong requires that the lease "indicate the method of calculating the amount to be deducted from the royalty for such post-production costs." 219 W. Va. at 274, 633 S.E.2d at 30. Thus, to satisfy *Tawney*, a lease must not only identify the deductions themselves, but also the "method" to be used in calculating those deductions.

In this case, the relevant language from the lease provides that as to any gas sold the lessees shall be paid a royalty of "one-eighth (1/8) of the price paid to [Petitioners] . . . less any charges for transportation, dehydration and compression paid by [Petitioners] to deliver the oil, gas, and/or coalbed methane gas for sale." App. 57. Petitioners do not point to any language—here or elsewhere in the lease—identifying a method to be used in calculating the amount of these deductions. Instead, they insist that *Young v. Equinor USA Onshore Properties, Inc.*, 982 F.3d 201 (4th Cir. 2020) somehow fills the gap.

According to Petitioners, *Young* offers a "straightforward, commonsense interpretation of *Tawney*." Pet'r Br., at 27. In reality, however, *Young* eviscerates *Tawney's* third prong. Like this case, the lease in *Young* provided little more than a listing of post-production costs. Nevertheless, the Fourth Circuit concluded that the amount of the deductions could be calculated using what amounted to a "workback" method. *Young,* of course, is correct that *Tawney* does not "demand . . . an Einsteinian proof." 982 F.3d at 208. But the lease must, at a minimum, identify some "method" to guide its royalty calculations.

On this point, Judge Bailey has provided a helpful analysis:

> "[T]he word 'method' means 'a procedure or process for attaining an object: such as… a way, technique, or process of or for doing something.' The word 'calculate' means 'to determine by mathematical processes.' Thus, a 'method of calculation' is a procedure, technique, or process for mathematically determining something.

App. 124.

Furthermore, a lease cannot satisfy *Tawney's* methodology requirement simply by stating that only "reasonable," "actual," or "incurred" costs may be deducted. Judge Bailey correctly notes that these kinds of terms have no "fixed" meaning and tell the royalty owners "utterly nothing about the specific method of calculation used to derive those . . . post-production costs." App. 124. *Tawney's* third prong was meant to prevent gratuitous, unspecific language that "asks prospective lessors to blindly trust that the lessees' method of calculation, whatever it may be, will comply with the law." *Id.*

With these considerations in mind, *Young* cannot possibly be reconciled with *Tawney. Young's* workback method is illusory. The lease contained no formula or explanation of the process to be used in calculating royalties. Instead, *Young* did nothing more than interpret the lease to ***mean*** what the lessee, Equinor, had already ***done***. That is exactly what *Tawney* was meant to prevent.

Petitioners try to emulate *Young's* workback formula, claiming that the lease's "unambiguous" language "explains how to determine what portion of the costs will be shared with the royalty owner." Pet'r Br., at 28. But the hard truth is that the lease itself does not say anything about cost sharing. The lease identifies three categories of costs, but fails to provide any explanation of how these costs are to be apportioned between the parties. *Tawney* demands an objective statement of the methodology to be used—both to bind the lessee and to give fair notice to the royalty owner.

Ironically, Petitioners accuse Judge Bailey of "overrid[ing] the express intention of the parties." Pet'r Br., at 28. But, again, *Tawney* begins with the premise that post-production costs are borne by the lessee. That is the historic rule, and it is presumed to be the intent of the parties.

Petitioners bear the burden of proving a contrary intent, which means they bear the burden of proving all three prongs of *Tawney's* test. If anything, it is Petitioners who are attempting to override the parties' intent.

Petitioners also claim that Judge Bailey's interpretation of *Tawney* will make West Virginia an "outlier." Pet'r Br., at 29. However, they only cite a single case from Oklahoma involving different and more specific lease language. In any event, gas leases are almost universally drafted by lessees, and it lies entirely within their power to draft leases that are *Tawney*-compliant. A recent law review article rightly emphasizes that case law provides "ample" guidance for drafting royalty clauses and admonishes lessees to "draft a royalty clause that plainly and unambiguously permits [them] to use a workback methodology to calculate [their] royalty payments." Byron C. Keeling, *In the New Era of Oil and Gas Royalty Accounting: Drafting a Royalty Clause that Actually Says What the Parties Intend It to Mean*, 69 Baylor L. Rev. 516, 570-71 (2017).[7] That, in essence, is what *Tawney's* requirements are meant to do—to place on the lessee the burden of setting forth a methodology for calculating royalties using plain and unambiguous language.

B. The Court Should Answer Certified Question No. 4 by Concluding that Indirect Costs May Not Be Deducted from Royalties.

With regard to Certified Question No. 4, Petitioners challenge the District Court's conclusion that only "direct" costs may be deducted and that "indirect" costs—including salaries, property taxes, construction costs, and the like—must be borne by the lessee. In fact, Petitioners go so far as to suggest that "there is nothing in *Wellman*, *Tawney*, or anywhere else that would distinguish between so-called direct and indirect costs." Pet'r Br., at 31-32. Petitioners, however,

[7]Instructively, Mr. Keeling provides an example of a royalty clause that would appear to satisfy *Tawney's* requirements. *See id.* at 570-71. That example not only specifies the categories of post-production costs that may be deducted, but also references and describes in detail the "workback" methodology and how it works.

are flatly wrong.

Petitioners cite *Young* again, claiming that the District Court's analysis is flawed because *Tawney* does not require "Einsteinian proof." Pet'r Br., at 31. But Petitioners are asking the wrong question. The question here is not a question of proof. Rather, the question is whether *Tawney* permits lessees to deduct a certain species of costs—i.e., indirect costs. That question was effectively answered by this Court in *Bryan v. Big Two Mile Gas Co.*, 213 W. Va. 110, 577 S.E.2d 258 (2001).

In *Bryan*, the Supreme Court determined that the subject gas lease had expired, and because the lessee continued to produce gas after the lease's expiration, it was deemed to be a trespasser. In determining the proper measure of damages in cases involving an innocent trespasser, the Court cited *Wellman*, quoted *Wellman*, and announced a rule that was "[c]onsistent with *Wellman*." *Bryan*, 213 W. Va. at 121-22, 577 S.E.2d at 269-70. Specifically, the Court held that the lessee could deduct costs, but only those "objectively reasonable operating costs that were actually incurred in the operation of the well." *Id.* at 122, 577 S.E.2d at 270. Thus, only ***direct*** costs incurred in ***operating*** the well were deductible. Furthermore, "any reasonable doubt as to the proper nature and measure of damages is to be resolved in favor of the mineral owner, as opposed to the trespasser." *Id.* To drive home its point, the Court cautioned lessees not to engage in "creative accounting" to avoid this all-important distinction. *Id.*

Bryan's distinction between direct and indirect costs is not only easy to apply, but it also guarantees an equitable result. Indirect costs, whether they take the form of salaries, office overhead, pipeline construction, or a hundred other incidental costs of doing business, are not directly responsible for bringing the gas to market or increasing its value. *Bryan* correctly draws the line at direct costs, thereby ensuring that lessors are only charged for expenses directly related to bringing their gas to market. Consequently, the Court should answer Question No. 4 by concluding that indirect costs may not be allocated to lessors under *Tawney*.

CONCLUSION

For all the reasons set forth above, WVLMOA and WVAJ respectfully request that this Court answer Certified Question No. 1 in the affirmative, and otherwise answer Certified Questions Nos. 2 through 4 consistent with the foregoing arguments.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on this 10th day of February 2022, a true and correct copy of the foregoing *Amicus Curiae Brief of the West Virginia Land and Mineral Owners Association and West Virginia Association for Justice in Support of Respondents* was served by United States Mail, first class, postage prepaid, addressed to the following:

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