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U.S. Supreme Court Holds California Wage-and-Hour Law Inapplicable to Offshore Workers Under OCSLA

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The proliferation of state wage-and-hour laws, particularly those mandating greater minimum wage and overtime benefits and providing narrower exemptions, has led to increased class action litigation against employers in recent years. Variations among state laws, and differences between state and federal laws, create additional administrative and legal headaches for employers with multi-state operations and mobile workforces. And, for companies with employees working offshore, courts previously have not formulated a consistent standard for determining whether adjacent state law applies when it imposes different or additional requirements than the federal law.

The U.S. Supreme Court, addressing a "close question of statutory interpretation" involving the Outer Continental Shelf Lands Act (OCSLA), held on June 10, 2019, that an offshore worker cannot assert California state wage-and-hour law claims. *Parker Drilling Management Services, Ltd. v. Newton,* No. 18-389 (June 10, 2019). The Court's ruling creates greater legal certainty and relieves administrative burden for companies with employees on the OCS to the extent it holds OCS workers subject only to the Fair Labor Standards Act (FLSA). It also minimizes the risk and burden of state wage-and-hour law class actions from offshore workers.

Brian Newton, the plaintiff in the lawsuit, had worked on drilling platforms off the coast of California for his employer, Parker Drilling Management Services. During two-week hitches, he was on duty for twelve hours per day and on standby for the other twelve hours, during which he was required to remain on the platform. The standby time was unpaid. Newton filed a California state court class action alleging violations of the state's wage-and-hour law, including a claim that the law required Parker to pay him for the standby time. Parker removed the case to federal court. While the parties agreed that the platforms at issue were subject to the OCSLA, they disagreed whether California wage-and-hour law was "applicable and not inconsistent" with the FLSA.

The district court had followed precedent from the U.S. Court of Appeals for the Fifth Circuit, concluding that under the OCSLA "state law only applies to the extent it is necessary 'to fill a significant void or gap' in federal law." Finding the FLSA to be a comprehensive federal wage-and-hour scheme, the federal district court found no gap for state law to fill, granting judgment on the pleadings to Parker because Newton asserted only state law claims.

The U.S Court of Appeals for the Ninth Circuit disagreed with this standard, holding that state law is "applicable" on the OCS if it pertains to the subject matter at hand. Further finding that California wage-and-hour law met this standard, it examined whether the state's law is "inconsistent with" the FLSA. The Ninth Circuit then articulated a standard for inconsistency, reasoning that state law is inconsistent with federal law only "'if they are mutually incompatible, incongruous, [or] inharmonious." Because the FLSA's saving clause expressly allows states to enact laws providing greater wage-and-hour benefits to employees, the Ninth Circuit decided there was no inconsistency, then it vacated and remanded the case.

The question presented to the Supreme Court was how to determine whether the law of a state adjacent to the OCS is "applicable and not inconsistent" with other federal law such that it should be followed offshore. A unanimous Court in an opinion delivered by Justice Clarence Thomas resolved conflicting standards articulated by the Fifth and Ninth Circuits to conclude that “where federal law addresses the relevant issue, state law is not adopted as surrogate federal law on the OCS.” The Court’s ruling aligns with Fifth Circuit precedent and, the Court noted, is supported by the OCSLA’s text, structure, and history, along with the Court's own precedent.

The Court explained that the OCSLA extends federal law and jurisdiction to the OCS, affirming its federal enclave status by providing that federal law applies “as if the [OCS] were an area of exclusive Federal jurisdiction within a State.” The Court was called upon to interpret the statute’s further language that adjacent state laws then or later in effect will be adopted as federal law governing the OCS if “they are applicable and not inconsistent with . . . other Federal laws and regulations . . . .” Newton urged the Court to adopt the Ninth Circuit’s analysis, essentially arguing that state law is “inconsistent” only if ordinary pre-emption principles would negate it. Parker urged the Court to adopt the Fifth Circuit’s gap-filler approach, arguing that more protective state law is inconsistent with the FLSA in this context because adopting state law as federal law would result in a body of federal law containing two different standards. The Court found Parker’s position more persuasive notwithstanding the close question of statutory interpretation.

The Court noted that language at issue must be read in context and in light of its place in the overall statutory scheme. The question was incapable of resolution based on an examination of the language alone because the terms, “applicable” and “not inconsistent,” are susceptible of interpretations that would render one or the other meaningless in context. The Court then pointed to the OCSLA’s emphasis on the federal government’s complete “‘jurisdiction, control, and power of disposition’” over the OCS, “while giving the States no ‘interest in or jurisdiction’ over it.” Thus, the Court observed that the only law on the OCS is federal law and any state laws that fill gaps are adopted as federal law. And, because state law has never applied of its own force on the OCS, the question of whether state law is “inconsistent” with other federal law is not the typical pre-emption analysis. “Instead, the question is whether federal law has already addressed the relevant issue; if so, state law addressing the same issue would necessarily be inconsistent with existing federal law and cannot be adopted as surrogate federal law.”

Further, the Court squared its interpretation with the statute's treatment of the OCS as "an upland federal enclave," an area of federal jurisdiction located within a state to which state law presumptively does not apply after enclave designation. The statute's history reinforced for the Court its conclusion that the OCS should be treated as a federal enclave, not an extension of any state, such that state law applies only as a gap-filler for federal law.

The Court was careful to note that this ruling does not foreclose the possibility that a state law is inapplicable and inconsistent with federal law even in the absence of a federal law that is on point. This means that not every state employment law claim for which there is no federal counterpart is automatically fair game. The ruling applies only to employees on the OCS, and does not affect those employees' rights under the FLSA. Nor does it resolve other issues created by differences between federal and state laws as applied to land-based and other employees not on the OCS. This ruling, however, should bring an end to offshore workers' state wage-and-hour law class actions against their employers, at least for now.

Lamps: Dimming the Lights on Class Arbitration

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Lamps Plus, Inc. v. Varela[1] held that an ambiguous agreement will not require class arbitration under the Federal Arbitration Act ("FAA").[2] This article discusses the opinion and its implications.

I. Facts

After a hacker obtained tax information on some 1300 Lamps' employees and filed a fraudulent tax return in Frank Varela's name, Varela filed a class action suit against Lamps.[3] Lamps moved to compel individualized arbitration based on the arbitration agreement in Varela's employment contract and requested dismissal.[4] The district court dismissed the case, but authorized class arbitration.[5]

On appeal, the Ninth Circuit noted that *Stolt-Nielson*[6] prohibited compelling "class arbitration unless there is a contractual basis for concluding that the party *agreed* to do so" and that Varela's agreement "include[d] no express mention of class proceedings".[7] However, it distinguished *Stolt-Nielson* because absence of an express reference to class arbitration was not equivalent to the "silence" in *Stolt-Nielson* where the agreement's silence on class arbitration was stipulated.[8] The Ninth Circuit held the agreement was ambiguous about class arbitration and followed California law construing ambiguity against the drafter (Lamps).[9] Under California law, an agreement is ambiguous "when it is capable of two or more constructions, both of which are reasonable."[10]

II. The Court's Decision

The majority[11] decision did not determine that the agreement was ambiguous. Instead, the Court accepted ambiguity as a fact by deferring to the Ninth Circuit on California law in accordance with its general practice regarding state law issues.[12] Given the agreement's ambiguity about class arbitration, the Court based its opinion on two precepts: the fundamental FAA rule requiring consent to arbitrate, and the stark differences it perceived between class arbitration and "the

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[1] 587 U.S.___, 139 S. Ct. 1407 (2019).
[2] The Court also upheld jurisdiction to appeal because the district court dismissed the case and compelled arbitration and found standing because Lamps had sought, and not obtained, individual arbitration. *Id.* at 1413-14.
[3] *Id.* at 1412-13.
[4] *Id.* at 1413.
[5] *Id.*
[6] *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.,* 599 U.S. 662 (2010).
[7] *Lamps,* 139 S.Ct. at 1413 (quoting 701 Fed.Appx. 672).
[8] *Id.* Although not mentioned in *Lamps, Stolt-Nielsen's* stipulation that the agreement was 'silent' was understood to convey that the parties "had not reached any agreement on the issue of class arbitration". *Stolt-Nielsen,* 599 U.S. at 673.
[9] *Lamps,* 139 S.Ct. at 1413.
[10] *Id.* at 1414-15.
[11] Three justices joined Chief Justice Roberts' opinion without comment. Justice Thomas' concurrence stated that the agreement was "silent as to class arbitration" and, "if anything", suggested "the parties contemplated only bilateral arbitration." *Id.* at 1419-20. He wrote that, as the agreement provided "no "contractual basis" for concluding the parties agreed to class arbitration", he "would ...reverse on that basis." *Id.* However, after expressing skepticism about the Court's implied preemption precedents, Justice Thomas stated that "I join the opinion of the Court because it correctly applies our FAA precedents". *Id.* at 1420.
[12] *Id.* at 1415.

“traditional individualized arbitration” contemplated by the FAA”.[13] Those principles informed its holding that ambiguity was insufficient “to ensure that the parties actually agreed to arbitrate on a classwide basis.”[14]

The Court began with the oft emphasized “foundational FAA principle” that “[a]rbitration is strictly a matter of consent.”[15] It then discussed the “fundamental” difference between individualized and class arbitration, noting again that individualized arbitration was “the form of arbitration envisioned by the FAA.”[16] According to the Court, class arbitration “sacrifices the principal advantage of arbitration—its informality—and makes the process slower, more costly, and more likely to generate procedural morass than final judgment.”[17] The Court also suggested, as it had previously, that class arbitration might be constitutionally impermissible.[18] Given the differences between class and individual arbitration that “undermine” central benefits of traditional arbitration,[19] the Court found that *Stolt-Nielsen’s* reasoning controlled and required that “[l]ike silence, ambiguity does not provide a sufficient basis to conclude that the parties to an arbitration agreement agreed to “sacrifice[ ] the principal advantage of arbitration”.[20] Indeed, it viewed that conclusion as consistent with its refusal to infer consent to other “fundamental arbitration questions”, such as whether there was a valid arbitration agreement, whether a certain type of dispute was covered by the agreement, and whether an arbitrator, rather than a judge, should resolve such questions.[21] Thus, neither silence nor ambiguity would be enough to find that the parties had “agreed to undermine the central benefits of arbitration itself” by agreeing to class arbitration.[22]

Since the Ninth Circuit’s ruling on the contractual issue was based on the rule of construction against the drafter (known as *contra proferentem*), the Court also dealt with that rule. It observed that unlike rules of construction that help uncover the parties’ intent, *contra proferentem* applied as a last resort only after a court determined “that it *cannot* discern the intent of the parties” and that such rule “provides a default rule based on public policy considerations” rather than determining the meanings that the parties intended.[23] Since the rule did not enforce the intention of the parties, it was preempted by the FAA’s requirement that the class arbitration was a matter of consent.[24] The Court’s opinion dispensed a dissent’s objection that *contra proferentem* does not discriminate against arbitration by stating that the equal treatment rule “cannot save from preemption general rules “that target arbitration either by name or by more subtle methods, such as ‘interfer[ing] with fundamental attributes of arbitration’”.[25] Hence, the FAA preempted the California rule because it would impose class arbitration in the absence of the consent required by the FAA.

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[13] *Id.* at 1415.
[14] *Id.* at 1415.
[15] *Id.*
[16] *Id.* at 1416. The Court has drawn stark differences between class and individualized arbitration before. See, *Epic Systems Corp. v. Lewis,* 584 U.S. ___, 138 S.Ct. 1612, 1622-23 (2018); *Stolt-Nielsen,* 559 U.S. at 685-7; *AT&T Mobility LLC v. Concepcion,* 563 U.S. 333, 348-351 (2011).
[17] *Id.* at 1416.
[18] *Id.*
[19] *Id.* at 1417 & 1415.
[20] *Id.* at 1416.
[21] *Id.* at 1416-17.
[22] *Id.* at 1417.
[23] *Id.*
[24] *Id.* at 1417-18.
[25] *Id.* at 1418 (citing *Epic Systems,* 584 U.S.___, 138 S.Ct. at 1622 (quoting *Concepcion,* 563 U.S. at 344)).

III. The Upshot

While *Lamps* certainly restricts class arbitrations to some extent, its effect may be limited to those arbitration agreements whose meaning a court or arbitrator is unable to divine from its language. Although Justice Kagan saw ambiguity about the extent to which the Court's opinion "extends beyond the anti-drafter rule to other background principles that serve to discern the meaning of ambiguous contract language",[26] the Court's observation that its opinion "is far from [a] watershed" seems correct.[27] Certainly, the Court chose not to announce a new FAA rule of interpretation and instead ruled based upon the Ninth Circuit's finding of ambiguity under state law. It noted that enforcement of arbitration agreements may ordinarily be accomplished "by relying on state contract principles".[28] And, it framed the issue as "the interaction between a state contract principle for addressing ambiguity and a "rule [ ] of fundamental importance" under the FAA, namely, that arbitration "is a matter of consent."[29] Further, *Lamps'* preemption holding seems limited to those contract interpretation rules that do not seek to uncover the intent of the parties; and, the Court distinguished the *contra proferentem* rule as being "[u]nlike contract rules that help to interpret the meaning of a term, and thereby uncover the intent of the parties".[30] Finally, and perhaps most importantly, the various opinions in *Lamps* revealed that five Supreme Court Justices reached three different opinions as to the meaning of the arbitration agreement before them.[31] Given the diversity of opinion of five Justices on the same contractual language, one must wonder how many agreements will fall within the ambiguity rule of *Lamps* as opposed to being interpreted, rightly or wrongly, based upon the language used. Finally, the suggestion that class arbitration might be constitutionally suspect is nothing new and not a holding. On the whole, *Lamps* may be merely a limited extension on when consent may be inferred under the governing rule that a party cannot be "compelled under the FAA to submit to class arbitration unless there is a contractual basis for concluding that the party *agreed* to do so."[32]

As for careful contract drafters, after *Lamps,* a class action waiver provision[33] still seems essential for a party desiring certainty that there will not be class arbitration. That is so for several reasons. First, as *Lamps* illustrates, it is impossible to determine in advance how a given arbitration agreement will be interpreted or if one's understanding of its meaning will be shared by the decision-maker. Moreover, if the issue of class arbitration is found to have been delegated to the arbitrator(s), there is a limited ability to review any decision on the issue.[34] Finally, class action waivers may provide protection in instances where the FAA does not apply. Thus, *Lamps* probably changed nothing about the drafting decisions of careful counsel seeking to avoid class arbitration.

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[26] *Id.* at 1433, n. 7 (Kagan dissenting).
[27] *Id.* at 1418.
[28] *Id.* at 1415.
[29] *Id.*
[30] *Id.* at 1417.
[31] Three justices read the agreement to provide for class arbitration (*id.* at 1428-29 (Kagan dissenting)), one may have viewed it as allowing only bilateral arbitration (*id.* at 1419-20 (Thomas concurring)), and one found the agreement was ambiguous. *Id.* at 1427 (Sotomayor dissenting). Also, Lamps' counsel reportedly conceded at oral argument that slightly different wording would have allowed class arbitration. *Id.* at 1429 n.2 (Kagan dissenting).
[32] *Id.* at 1412 (quoting *Stolt-Nielson*, 559 U.S. at 684).
[33] A class action waiver provision is a term in an arbitration agreement that provides, preferably in clear and express terms, that class arbitration is not allowed. Such provisions are permitted under the FAA. See, *Concepcion,* 563 U.S. 333 (2011).
[34] *Oxford Health Plans LLC v. Sutter*, 569 U.S. 564 (2013) (upholding arbitrator's decision on class arbitration under the FAA's limited review).

Court Holds that President Cannot Revoke a Prior Executive Order Withdrawing Certain Offshore Areas from Mineral Leasing

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The Outer Continental Shelf Lands Act[1] authorizes the U.S. Secretary of Interior to grant oil and gas leases for areas on the federal portion of the Outer Continental Shelf. On the other hand, a section of OCSLA states, "The President of the United States may, from time to time, withdraw from disposition any of the unleased lands of the outer Continental Shelf."[2] Such a withdrawal would preclude leasing.

In 2015 and 2016, President Barack Obama issued three memoranda and an executive order withdrawing certain areas from oil and gas leasing, including areas off the Atlantic coast and certain areas off the coast of Alaska.[3] A few weeks after Donald Trump became President in 2017, he issued Executive Order 13795, which purports to revoke the withdrawals made by President Obama.[4] Five days after President Trump issued the executive order, several environmental groups filed *League of Conservation Voters v. Trump* in the United States District Court for the District of Alaska, asserting that a President has no authority to revoke a prior withdrawal.[5] The State of Alaska and the American Petroleum Institute intervened, joining the Department of Justice in defending the right of a President to revoke a prior withdrawal.[6]

The court rejected various procedural arguments raised by the defendants, including arguments based on standing, ripeness, and sovereign immunity.[7] The defendants also asserted various arguments that went to the merits of the dispute. For example, they asserted that the phrase "may, from time to time" implied that the President can revoke a prior withdrawal.[8] They argued that, if a President cannot revoke a prior withdrawal, then one President "may perform a *de facto* repeal of OCSLA" and tie future Presidents' hands by withdrawing areas from leasing, and that a statutory interpretation that allowed such a result would not make sense.[9] They also noted that, on two prior occasions, a President had reduced the area covered by a prior withdrawal and the Congress had not objected.[10] Ultimately, however, the court rejected these arguments and entered a judgment holding that the purported revocation of President Obama's prior withdrawal was unlawful and invalid.[11]

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[1] 43 U.S.C. §§ 1331 *et seq.* OCSLA was enacted in 1953.
[2] This is found in Section 12(a) of OCSLA, which is codified at 43 U.S.C. § 1341(a).
[3] League of Conservation Voters v. Trump, 363 F. Supp. 3d 1013, 1016 (D. Alaska 2019).
[4] *Id.* at 1016-7.
[5] *Id.* at 1017.
[6] *League of Conservation Voters*, 363 F. Supp. 3d at 1016.
[7] *Id.* at 1019.
[8] *Id.* at 1022.
[9] *Id.* at 1029.
[10] *Id.* at 1029-30.
[11] *League of Conservation Voters*, 363 F. Supp. 3d at 1030.

A New Well Control Rule for OCS Operations

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On May 2, the Bureau of Safety and Environmental Enforcement (BSEE) issued the 2019 Well Control Rule (Rule), a long-awaited, revised (and final) well control and blowout preventer rule governing Outer Continental Shelf (OCS) activities. This Rule represents a groundbreaking development for the offshore industry in the aftermath of the Deepwater Horizon incident in 2010. It is the first time that BSEE has provided more learned guidance for oil and gas companies regarding well control and blowout preventer systems since the well control rules issued in April 2016 (2016 WCR).

The new Rule revises current regulations impacting offshore oil and gas drilling, completions, workovers, and decommissioning activities. Specifically, the new final Rule addresses six areas of offshore operations: (1) well design, (2) well control, (3) casing, (4) cementing, (5) real-time monitoring (RTM), and (6) subsea containment. Recognizing that blowout preventer technology and well control systems continue to evolve and improve, BSEE decided that it was time to review and revamp its well control rules so that they not only incorporate the lessons learned from Deepwater Horizon, but also take into account OCS stakeholders' concerns about the implementation and application of the 2016 WCR. Since 2016, offshore operators have raised concerns that the 2016 WCR – although designed to enhance worker safety and environmental protection – instead created regulatory headaches for the industry and, in some cases, did nothing to improve worker safety or protect the environment. For example, some OCS stakeholders voiced concerns that the requirements for certain BSEE approvals during cementing operations generally resulted in unnecessary delay and did not actually protect workers and/or the environment. It was this type of concern that BSEE sought to allay with the revisions set forth in the 2019 Well Control Rule.

The 2019 Well Control Rule affects Part 250, Subparts A, B, D, E, F, G and Q of Title 30, Code of Federal Regulations. In creating the new Rule, BSEE received and reviewed more than 265 sets of comments from individual companies and industry organizations, among others, totaling 118,000 submissions. The new Rule revises/adds to 71 provisions of the 2016 WCR. The new Rule also embraces the recommendations set forth in a number of investigative reports following Deepwater Horizon and maintains the core safety and environmental protective provisions of the 2016 WCR, with a more tailored approach focused on reducing regulatory burdens on the industry. The new Rule does not alter the following: (i) the Drilling Safety Rule of 2010, (ii) SEMS I (2010) or (iii) SEMS II (2013). The 2019 Well Control Rule will go into effect 60 days after publication in the Federal Register. The Rule was published in the Federal Register on May 15, 2019 (84 Fed. Reg. 21,908 (May 15, 2019)).

Key Takeaways

This new Rule makes sure that blowout preventer rules are no longer a one-size-fits-all set of regulations. The new Rule: (1) clarifies rig movement reporting requirements; (2) revises BSEE reporting requirements to eliminate redundant reporting; (3) clarifies drilling margin requirements; (4) revises Section 250.723 to remove references to "lift boats"; (5) removes certain prescriptive requirements for RTM; (6) replaces use of BSEE approved verification organization with an independent third party for certain certifications and verifications of BOP systems and components; (7) revises accumulator system requirements and accumulator bottle requirements to better align with API Standard 53; (8) revises control stations and pod testing scheduled to ensure component functionality without duplicative testing; (9) includes coiled tubing and snubbing requirements in Subpart G; (10) revises rules overall to ensure more uniformity and conformity in the application of the Rule; and (11) revises the regulations to include a 21-day BOP testing frequency.

Colorado Enacts Sweeping Regulatory Changes to Oil and Gas Industry

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The end of Colorado's legislative session last month marked the beginning of a new era of regulation for the State's oil and gas industry. On April 16, 2019, Colorado Governor Jared Polis signed Senate Bill 19-181, also known as the Protect Public Welfare Oil and Gas Operations Act ("Act"), officially revamping the Colorado Oil and Gas Conservation Commission ("Commission"). Some of the most significant changes resulting from the bill's passage include: (1) the restructuring and repurposing of the Commission; (2) an increase in local government authority to regulate oil and gas matters; (3) an increase in partnerships with other agencies; and (4) the adoption of more stringent forced pooling requirements.

Colorado's legislative overhaul is not the State's first recent attempt to increase energy regulations. Last November, activists attempted to pass Proposition 112, which would have increased setback requirements for drilling from 500 feet to 2,500 feet from certain vulnerable areas like neighborhoods and schools.[1] While the proposition ultimately failed 57 percent to 43 percent, the Commission subsequently adopted a 1,000 feet setback rule from school properties.[2]

I. A New Mission

One of the most substantial changes to the Commission relates to its mission. Prior to the SB 19-181, the Commission's purpose was to foster the development of Colorado's natural resources in a manner consistent with the protection of the public and the environment.[3] This type of mission statement required the Commission to make decisions using a balancing scale, weighing the need to mitigate significant adverse effects against cost-effectiveness and technological feasibility.[4]

Back in January, in *COGCC v. Martinez*, the California Supreme Court relied on this balancing test to determine whether the Commission properly declined to adopt a proposed rule.[5] A group of teenagers sued the Commission after it refused to adopt a proposed rule requiring the Commission to refrain from issuing drilling permits "unless the best available science demonstrates, and an independent, third-party organization confirms, that drilling can occur in a manner that does not cumulatively, with other actions, impair Colorado's atmosphere, water, wildlife, and land resources, does not adversely impact human health, and does not contribute to climate change."[6] In deciding for the Commission, the Court reasoned that, under the balancing test, the Commission was not required to "condition all new oil and gas development on a finding of no cumulative adverse impacts to public health and the environment."[7]

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[1]John Aguilar, *"Let's get real, guys": Oil and gas rules front and center for Colorado lawmakers following Prop 112's defeat*, THE DENVER POST (Nov. 12, 2018), https://www.denverpost.com/2018/11/12/oil-gas-setback-legislature-regulation-prop-112/
[2]*Id.*
[3]Protect Public Welfare Oil and Gas Operations Act, S.B. 19-181 77 General Assembly, 1st Session, § 6 (Colo. 2019).
[4]*Id.*
[5]Colorado Oil and Gas Commission v. Martinez, 433 P.3d 22, 24 (Colo. 2019).
[6]*Id.*
[7]*Id.* at 25. The Court further considered the fact the Commission was already working with the Colorado Department of Public Health and Environment to reduce the concerns addressed by the proposed rule.

Now, the Commission has a new mission: to regulate the oil and gas industry and to protect the public's health and safety and the environment.[8] Under its new requirements, the Commission need not consider factors like cost effectiveness or technical feasibility.[9] The nine-member panel charged with carrying out this mission will also contain a more diverse array of experts from various scientific fields, not just the energy industry.[10] SB 19-181 reduces the required number of members with "substantial experience in the oil and gas industry" from three to one.[11]

The regulations pose additional panel changes to take place the earlier of July 1, 2020 or the date on which all rules become effective.[12] The future panel will also include individuals with experience in planning or land use, environmental protection, wildlife protection or reclamation, and public health.[13]

II. Increased Local Governance

Previously, local governments had minimal regulatory authority over the oil and gas industry.[14] Under the old regulatory scheme, an oil and gas operator would first obtain a permit from the Commission before notifying local authorities.[15] Now, under the new regulations, local governments[16] are the predominate regulators of fracking activity within their jurisdictions.[17] Instead of first filing with the Commission, the operator must instead file an application with, and obtain approval from, the local government.[18] The local government has the authority to regulate the siting of oil and gas developments.[19] If the local authority chooses not to regulate oil and gas development, then the operator must submit proof to the Commission that it need not comply with any local regulations.[20]

If the local government chooses to regulate development, it may ask the Commission to appoint a technical review board to study the local government's preliminary or final determination regarding the proposed siting of an oil or gas facility within the local jurisdiciton.[21] Technical review board members are made up of energy industry, environmental, and public health experts.[22] The board members must then issue a report sixty (60) days after their appointment. [23] The report must consider technological feasibility and the operator's management practices, but it may not consider the economic effects of the determination.[24] Ultimately, the local government has the freedom to adopt or ignore any changes proposed by the technical review board.[25]

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[8]Protect Public Welfare Oil and Gas Operations Act, S.B. 19-181 77 General Assembly, 1st Session, § 12 (Colo. 2019).
[9]*Id.* § 10
[10]*Id.* § 8.
[11]*Id.* § 9.
[12]*Id.*
[13]*Id.*
[14]*Id.* §§ 1, 2.
[15]*Id.* § 4.
[16]*Id.* § 7 (Local government means a "(a) municipality or city and county within whose boundaries an oil and gas location is sited or proposed to be sited; or (b) county, if an oil and gas location is sited or proposed to be sited within the boundaries of the county but is not located within a municipality or city and county.")
[17]*Id.* §§ 1, 2, 4, 11, & 15.
[18]*Id.* § 12.
[19]*Id.* § 4.
[20]*Id.*
[21]*Id.*
[22]*Id.*
[23]*Id.* § 10.
[24]*Id.* § 10.
[25]*Id.* § 4.

In addition to creating a new local administrative process for the issuance of permits, the Act also grants local authorities with the power to regulate "water quality, vibration, noise[26] odor, light, dust, air emission and air quality, land disturbance, reclamation procedures, cultural resources, emergency preparedness and coordination with first responders, security, and track and transportation impact."[27] Local authorities can inspect all facilities, impose fines for leaks, spills, and emissions, and charge fees for costs incurred in enforcing the regulations. [28]

The legal effects of Colorado's change in preemption law will largely depend on how Colorado communities wield their new power. In Weld County—the county responsible for 89% percent of the State's crude oil production— county commissioners have already announced plans to use their new authority to maintain a "working relationship" with the energy industry.[29] Still other cities are expected to attempt to revive previously-thought-dead fracking bans. In 2016, the Colorado Supreme Court struck down fracking bans imposed by Boulder and Longmont based on state-preemption law.[30] Now, these bans are likely permissible.

III. Partnership with Other Commissions

Under the old regulatory scheme, the Commission had exclusive authority to regulate oil and gas activities. Now, the Act not only grants regulatory authority to local governments, but also "no longer alters, impairs, or negates" the authority of the Air Quality Control Commission, Water Quality Control Commission, Board of Health, and Solid and Hazardous Waste Commission to regulate certain oil and gas operations.[31] These agencies can establish additional oil and gas specific regulations for everything from air and water pollution to disposal of hazardous waste and radioactive materials.[32] Further, the Act expressly directs the Air Quality Control Commission to consider adopting more stringent provisions regarding leak detection, inspection of transmission pipelines and compressor stations, and emissions output and monitoring.[33]

IV. Enhanced Requirements for Forced Pooling

The Act also makes three major changes to the State's forced pooling[34] provisions.[35] First, the Act now requires more than 45% of mineral interest owners to join in an application for pooling.[36] Before, any interested person could apply for a forced pooling order.[37] The pooling application must include proof of the filing of the siting application with the local government (or proof no local

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[26] *Id.*
[27] *Id.*
[28] *Id.*
[29] Weld County Colorado, Planning and Zoning Oil and Gas, (last visited May 24, 2019) https://www.weldgov.com/departments/planning_and_zoning/oil_gas; John Aguilar, *In "new era" of oil and gas regulation, Colorado communities waste no time writing own rules*, THE DENVER POST (May 6, 2019), https://www.weldgov.com/departments/planning_and_zoning/oil_gas
[30] City of Longmont v. Colorado Oil and Gas Association, 369 P.3d 573, 585 (Colo. 2016); City of Fort Collins v. Colorado Oil and Gas Association, 369 P.3d 586, 589 (Colo. 2016).
[31] Protect Public Welfare Oil and Gas Operations Act, S.B. 19-181 77 General Assembly, 1st Session, § 11 (Colo. 2019).
[32] *Id.* § 11
[33] *Id.* § 3.
[34] Curtis Talley, *Oil and gas leasing: what is pooling?*, MICHIGAN STATE UNIVERSITY EXTENSION, (Apr. 8, 2011), https://www.canr.msu.edu/news/oil_and_gas_leasing_what_is_pooling. Force pooling is a term used to describe the means by which a government can force nonconsenting owners to combining oil and gas leases to form a single drilling unit.
[35] *Id.* ("[t]he reason for establishing such pools is to unite all the landowners having an interest in a common underground reservoir under one operator. Sometimes pooling arrangements are necessary to meet the minimum acreage requirement for a drilling permit under state regulations.")
[36] Protect Public Welfare Oil and Gas Operations Act, S.B. 19-181 77 General Assembly, 1st Session, § 14 (Colo. 2019).
[37] *Id.* § 12.

government requirements exist).[38] Second, an operator must obtain permission from a non-consenting owner before using the nonconsenting owner's surface estate.[39] Third, the Act raises the royalty rates for nonconsenting owners from 12.5% to 13%, until the consenting owners recover their costs.[40]

V. More to Come

Colorado's legislative overhaul is just one example of a growing movement to increase oil and gas regulations to protect public health and safety and the environment. While the Act already contemplates many significant changes, over the next year, the Commission is expected to unveil additional regulations designed to carry out its freshly-minted mission. For example, the Act states that the Commission must develop, among other things, rules regarding: (1) permitting, construction, operation, and closure of wells; (2) safety and environmental protections; (3) regulatory integrity assessments; (4) worker certification requirements; (5) disclosure of flow information to the public; and (6) inspection requirements for inactive, temporarily abandoned, or shut in wells.[41]

Ultimately, the force of these changes will largely depend on how local governments respond. Regardless, the current changes, as well as the changes to come, will present new legal risks and challenges for landowners, developers, and local governments.

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[38] *Id.*
[39] *Id.* § 14.
[40] *Id.*
[41] *Id.* § 11.

Louisiana Appellate Court Upholds Grant of Coastal Use Permit for Crude Oil Pipeline

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In *Joseph v. Department of Natural Resources*, 265 So. 3d 945 (La. App. 5th Cir. 2019), several persons challenged the Department of Natural Resources's grant of a Coastal Use Permit to Bayou Bridge Pipeline, LLC to construct and operate a pipeline. The pipeline is designed to carry 280,000 barrels of crude oil per day from a terminal in Lake Charles, Louisiana to a terminal in St. James, Louisiana. Although most of the pipeline's proposed route is outside Louisiana's Coastal Zone, the terminal in St. James is within the Coastal Zone.

The persons challenging the permit filed a petition in the Twenty Third Judicial District Court for the Parish of St. James, pursuant to Louisiana Revised Statutes 49:214.35D, which allows certain persons to appeal Coastal Use Permit decisions, and pursuant to 49:214.35E, which authorizes venue for such an appeal "in the district court of the parish in which the proposed use is to be situated." A district court's review of a permit in such cases is an appellate review.[1] The district court rendered judgment in favor of the plaintiffs challenging DNR's grant of the Coastal Use Permit and remanded the matter to DNR. The district court stated in its reasons for judgment that Coastal Use Guidelines 711(A) and 719(K) applied and that DNR had not complied with the requirements contained in those Guidelines. Bayou Bridge and DNR appealed the trial court's judgment to the Louisiana Fifth Circuit Court of Appeal. They argued that the trial court erred by failing to give deference to DNR's conclusion that the Guidelines did not apply. They also argued that DNR had complied with the Guidelines.

After describing the basis for its jurisdiction, the Fifth Circuit[2] began is analysis of the merits of the dispute by noting that Louisiana law generally requires a reviewing court to give "considerable weight to an administrative agency's construction and interpretation of its rules and regulations adopted under a statutory scheme that the agency is entrusted to administer." Indeed, such an agency's "construction and interpretation should control unless the court finds it to be arbitrary, capricious, or manifestly contrary to its rules and regulations."[3]

One of the Guidelines at issue was Guideline 711(A), the first subsection of Guideline 711, which is entitled "Guidelines for Surface Alterations." This Guideline applies to surface alterations, which are defined by the Louisiana Administrative Code to be "uses and activities which change the surface or usability of a land area or water bottom."[4] DNR concluded that Guideline 711 did not apply. In part, DNR reasoned that the Guideline did not apply because the pipeline would be buried and, after construction of the pipeline was complete, the land would be restored to its original condition. Thus, any surface alteration was temporary. As for "usability" of the land, the appellate court noted that the proposed route for the pipeline ran primarily through an existing utility right-of-way, and DNR

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[1] La. Const. art. V, sec. 16 authorizes district courts to exercise appellate jurisdiction "as provided by law."
[2] Judge Stephen J. Windhorst wrote for a panel that included Susan M. Chehardy, Robert A Chaisson, Hans J. Liljeberg, and Marc E. Johnson. Judge Johnson dissented.
[3] 265 So. 3d at 950 (citing prior Louisiana First Circuit and Fourth Circuit cases). This deference seems similar to the *Auer* deference that the U.S. Supreme Court has said is due to federal agencies' interpretation of their own regulations. *See, e.g.*, Decker v. Northwest Environmental Defense Center, 133 S. Ct. 1326, 1337 (2013); Auer v. Robbins, 117 S. Ct. 905, 911 (1997).
[4] La. Admin. Code 43:I.700.

had concluded that the proposed route used existing corridors to the maximum extent practicable. Under these circumstances, DNR's conclusion that Guideline 711(A) did not apply was reasonable.[5]

Another Guideline at issue was Guideline 711(K), which applies to "uses and activities which are directly involved in the exploration, production, and refining of oil, gas, and other minerals."[6] The Fifth Circuit noted that the transportation of crude oil between terminals is not directly involved in the exploration or production of oil and gas. Further, such transportation is not "directly" related to refining of oil, and at most, is indirectly related to refining.[7] Therefore, DNR's conclusion that Guideline 719(K) does not apply was reasonable.[8]

The appellees also had argued at the trial court level—and renewed those arguments before the Fifth Circuit—that DNR had not required effective environmental and emergency response plans and that DNR had not complied with its public trust obligations under Article IX, section 1 of the Louisiana Constitution, as interpreted in the *Save Ourselves* decision.[9] The Fifth Circuit rejected both of those arguments. The appellate court noted that DNR had made certain findings regarding the adequacy of the proposed pipeline's spill and response plans. Further, the primary responsibility to develop such plans is vested in the Louisiana Oil Spill Coordinator's Office, not DNR. The Fifth Circuit concluded that, "within the permissible scope of its authority," DNR made a reasonable determination that the emergency response and contingency plans submitted by Bayou Bridge were sufficient. Finally, the court concluded that DNR had thoroughly and carefully considered Bayou Bridge's application, and that this review satisfied its public trust obligations.

For these reasons, the Louisiana Fifth Circuit reversed the district court's decision and upheld the validity of the Coastal Use Permit that DNR granted to Bayou Bridge.

[5] Because the appellate court concluded that DNR's conclusion regarding the inapplicability of 711(A) was reasonable, the court did not reach the appellants' argument that DNR's review of the Coastal Use Permit application satisfied 711(A). 265 So. 3d at 952-3.
[6] 265 So. 3d at 952; *see also* La. Admin. Code 43:I.700.
[7] 265 So. 3d at 952.
[8] Because the appellate court concluded that DNR's conclusion regarding the inapplicability of 711(A) was reasonable, the court did not reach the appellants' argument that DNR's review of the Coastal Use Permit application satisfied 719(K). 265 So. 3d at 952-3.
[9] *See* Save Ourselves, Inc. v. Louisiana Environmental Quality Comm., 452 So. 2d 1152 (La. 1984).

Louisiana Appellate Court Upholds Sufficiency of Omnibus Description

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Sons of legendary Texas oilman H.L. Hunt tried to corner the silver market in late 1979 and early 1980. They used much of their money to purchase silver and borrowed additional money to acquire yet more silver. The price of silver rose dramatically, and, by some accounts, the brothers were close to gaining control of the world silver market. But the U.S. government changed certain rules regarding commodities trading in an effort to thwart the brothers' scheme. The brothers' effort stalled, and on March 27, 1980—dubbed "Silver Thursday"—they missed a margin call. Silver prices tumbled, lawsuits followed, and the brothers eventually were forced into bankruptcy. A recently decided case revives memories of those events.

Compass Energy Operating LLC v. Robena Property & Royalty Co., Ltd., 265 So. 3d 1160 (La. App 2nd Cir. 2019) was a concursus proceeding[1] filed by Compass, a unit operator, asserting that there was a dispute regarding ownership of certain interests that would entitle the owner to a share of production from a unit in Jackson Parish. The rival claimants asserted rights based on competing chains of title. One side based its claim on transfers made during the bankruptcy of Nelson Bunker Hunt and his wife, following Nelson's and his brother's unsuccessful attempt to corner the silver market. The other side in this litigation traced their title to a quitclaim executed later, outside the bankruptcy, by Nelson's wife.

The parties who based their claim on the quitclaim made two arguments. First, in the Hunt bankruptcy, a trust had been established to administer the property being received from the Hunts by the bankruptcy trustee. Pursuant to the agreement and a bankruptcy court order, a deed was prepared that listed the property that was being conveyed to R. Carter Pate, the trustee. This "Pate Deed" was recorded in Jackson Parish, but the trust agreement was not recorded. The parties relying on the quitclaim asserted that recordation of the Pate Deed was not sufficient to make the transfers of property to the trustee effective against third parties because the trust agreement itself was not recorded. The trial court accepted that argument. On appeal, the Louisiana Second rejected it.

The parties who based their claim on the quitclaim also argued that the Pate Deed was not sufficient to put third parties on notice of the transfer of the oil and gas lease relevant to this case because no leases were listed in the Pate Deed. The trial court agreed. On appeal, the Second Circuit disagreed. The Second Circuit noted that an omnibus clause in the deed stated that all leases and mineral interests associated with the listed properties were being transferred to the trustee. The lease relevant to this case was associated with one of the properties listed in the deed, and the deed provided a legal description of the property. The Second Circuit reasoned that this was sufficient, even though the deed did not list individual oil and gas leases.

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[1] A concursus proceeding is an action authorized by the Louisiana Code of Civil Procedure that is analogous to an interpleader action under the Federal Rules of Civil Procedure and federal statutes. See La. Code Civ. Proc. arts. 3651-3662; Fed. R. Civ. Proc. 22 ("rule interpleader"); 28 U.S.C. § 1335 ("statutory interpleader"). *See* also 28 U.S.C. §§ 1397 (venue for statutory interpleader actions), 2361 (process and procedure in statutory interpleader action).

Unleased Owner Not Responsible for Post-Production Costs

Keith B. Hall
LSU Law Center

In *Johnson v. Chesapeake Louisiana LP*, 2019 WL 1301985 (W.D. La.), parties disputed whether the operator of a compulsory drilling unit in Louisiana can charge an unleased owner with a proportionate share of post-production costs. The United States District Court for the Western District of Louisiana (Hicks, J.) held that such an operator cannot.

In Louisiana, compulsory pooling is used more often than voluntary pooling. Indeed, Louisiana Revised Statute 30:10(A)(1) provides that, if "two or more separately owned tracts of land are embraced within a drilling unit which has been established by the" Commissioner of Conservation, and those owners have not agreed "to pool, drill, and produce their interests and to develop their lands as a drilling unit," 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."

Louisiana Revised Statute Section 30:10(A)(2) states that, "In the event pooling is required, the cost of development and operation of the pooled unit chargeable to the owners therein shall be determined and recovered as provided herein." Section 30:10(A)(3) provides that owners of unleased mineral rights in a tract in a unit are liable, out of production, for their "tract's allocated share of the actual reasonable expenditures" incurred by the unit operator in drilling the well and producing oil or gas. The statute does not expressly address post-production costs that the operator may incur in handling and transporting oil or gas prior to selling it.

Nevertheless, unit operators often incur such post-production costs in handling and arranging the sale of hydrocarbons attributable to unleased mineral interests, particularly if a unit well produces natural gas. This occurs because many owners of unleased interests do not make their own arrangements to sell the portion of gas attributable to the tracts in which they own interests. In such circumstances, the operator has authority to sell the gas attributable to the unleased interests, subject to an obligation to account to the owners of the interests. Typically, operators choose to exercise that authority because the alternative of letting an unleased owner's share of gas accumulate is not practical.

Post-production costs that operators commonly incur include expenses for treating and compressing gas, then transporting it to the place of sale. This leads to the question disputed in *Johnson*. Namely, if the unit operator sells natural gas attributable to an unleased interest, is the owner of that unleased interest responsible for a proportionate share of the post-production costs reasonably incurred by the operator in handling the gas. In *Johnson*, the operator (Chesapeake) argued that it was entitled to charge the unleased owner with a proportionate share of these costs. Otherwise, the unleased owners would be unjustly enriched at Chesapeake's expense.

The court rejected that argument, noting that 30:10(A)(3) states:

> If there is included in any unit created by the commissioner of conservation one or more unleased interests for which the party or parties entitled to market production therefrom have not made arrangements to separately dispose of the share of such production attributable to such tract, and the unit operator proceeds with the sale of 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 of production within one hundred eighty days of such sale.

Chesapeake argued that the only purpose of 30:10(A)(3) is to set a deadline for payment, not to govern liability for post-production costs. The court held otherwise. Section 30:10 does not define “pro rata share,” but the court concluded that it means a pro rata portion of gross proceeds, from which the operator may subtract only the costs that Section 30:10 expressly authorizes the operator to recover. The district court granted summary judgment in favor of the unleased owners, holding that Chesapeake may not charge them with a share of post-production costs.

Ohio's Seventh Appellate District Addresses Lease *Continuous Drilling Operations* Clause

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Many, if not most, lease provisions are drafted to manage the uncertainty that surrounds oil and gas development, and the *continuous drilling operations* (or, more simply, a *continuous operations*) clause is no different. Simply stated, it is a savings clause designed to maintain the lease past the expiration of the primary term despite a lack of production as long as the lessee is then engaged in drilling (or other) operations. In *Shutway v. Chesapeake Expl., LLC*, the Court of Appeals for the Seventh Appellate District upheld the trial court's grant of summary judgment in favor of the lessee, finding that it had engaged in sufficient operations prior to the primary term's expiration to maintain the lease into the secondary term.

The facts were straightforward. Plaintiffs executed an oil and gas lease containing a fairly standard habendum clause and the following operations language: "If at the expiration of the primary term of this lease, oil or gas is not being produced on the leased premises or acreage pooled therewith, **but lessee is engaged in drilling** … **operations thereon** … this lease shall remain **in force so long as operations on said well** or drilling … of any additional well **are prosecuted** with no cessation of more than ninety (90) consecutive days …" While there was no production at the end of the primary term, months earlier the lessee had contacted the plaintiffs to negotiate a surface use agreement and identify a suitable pad location; prepared a plan for erosion and sediment control; surveyed and staked the location; applied for and received drilling permits from the Ohio Department of Natural Resources; and applied for a needed road access permit from the Ohio Department of Transportation. The lessee had also engaged contractors, who near the end of the primary term used heavy equipment to extend the dirt access road, install a culvert, and excavate the well pad location (by clearing, leveling, constructing berms, and stabilizing the location).

To support their argument that these activities were insufficient to hold the lease into its secondary term, plaintiffs were forced to distinguish existing Ohio case law finding the phrase *drilling operations* to be unambiguous and that it encompasses substantially less conduct than that which occurred in this case. See, e.g., *Duffield v. Russell*, 10 Ohio C.D. 472 (1899) (stating that it can consist of fairly trivial and insignificant activities). Plaintiffs argued that the lease language here required the lessee to be "engaged in" drilling operations at the end of the primary term, as opposed to the language at issue in earlier case law – i.e., requiring "commencement" of those operations. The court of appeals quickly disposed of that argument, stating, "[As] the word 'commence' means to begin, a lessee who 'is engaged in drilling … operations' has necessarily commenced drilling operations, and a lessee who has commenced drilling operations is necessarily engaged in them."

Next, the court of appeals addressed plaintiffs' argument that the operations clause required that the well pad actually be completed and a rig actively engaged in the drilling process in order to maintain the lease beyond its primary term. "[Plaintiffs] suggest that Chesapeake could not have been engaged in drilling operations at the end of the primary term if the drill bit was not predicted to penetrate the surface until after the primary term expired, concluding that Chesapeake thus lacked 'said well' on which it could be said they 'prosecuted' operations." The court rightly recognized that the use of the term "said well" simply referred to the intended well for which the operations had been commenced. "In other words, when the clause allows the lease to continue ‘so long as operations on said well … are prosecuted …,’ it is referring to the well in the process of being developed by the lessee via the drilling operations the lessee is engaged in at the expiration of the primary term. The phrase merely reinforces that the drilling operations are being engaged in with intent for these operations to culminate in a well (which is needed for production).”

Last, the court of appeals addressed plaintiffs’ “too little, too late” argument (*i.e.*, that the well pad excavation and road work that took place less than a week before the end of the primary term was insufficient to maintain the lease—insinuating that it was done for illegitimate reasons). Reviewing the activities engaged in by Chesapeake, the court observed: “There is no indication these acts were engaged in with any intent other than carrying out the rights of the lessee under the lease; the mere fact the intent to carry out the lease means there is an intent to utilize the drilling operations clause to extend the lease … does not corrupt the intent. **Whether Chesapeake ‘scrambled’ because the lease was about to expire in order to try to extend the lease past the primary term** and whether Chesapeake intended to have a completed well capable of production before the end of the primary term **are not pertinent to whether the drilling operations clause operated to save the lease**.”

Tenth Circuit Court of Appeals Affirms Decision of the United States District Court for the Western District of Oklahoma Certifying a Modified Royalty Owner Class

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In *Naylor Farms, Inc. v. Chaparral Energy, LLC,*[1] the plaintiff royalty owners (collectively, Naylor Farms) contended that Chaparral systematically underpaid royalties on production from approximately 2,500 Oklahoma oil and gas wells by improperly deducting from royalty payments certain costs that the plaintiffs contended should have been borne solely by Chaparral under Oklahoma law. The district court granted Naylor Farms' motion seeking certification of a class of royalty owners under Rule 23 of the Federal Rules of Civil Procedure.[2] In the present proceedings, Chaparral appealed the district court's order granting class certification.[3]

Naylor Farms brought this suit alleging "claims for breach of contract, breach of fiduciary duty, fraud, unjust enrichment, and failure to produce in paying quantities."[4] Naylor Farms asserted that Chaparral breached what was described by the court as the "implied duty of marketability (IDM)"[5] by improperly deducting what were described as "GCDTP-service costs"[6] from the royalty payments Chaparral made to Naylor Farms and to other similarly-situated royalty owners. More specifically, certain midstream companies acquired title to or possession of the gas and natural gas liquids (NGLs) at or near the wellhead, and then performed certain GCDTP services and sold the treated gas to downstream purchasers. The midstream companies, in turn, deducted from the gross proceeds they received from the downstream sales of production the costs and fees associated with performing the GCDTP services. They paid Chaparral the resulting net proceeds. Chaparral then computed royalty payments "based on the *net proceeds* it receives from the midstream companies, rather than . . . based on the gross proceeds the midstream companies receive from the downstream sales."[7] Naylor Farms asserted that this approach to calculating royalty payments "requires royalty owners to bear the costs of transforming unprocessed gas into a marketable product" in breach of the IDM.[8]

Naylor Farms moved the court to certify a class of similarly situated royalty owners.[9] In opposition to that request, Chaparral argued that a determination of whether it breached the IDM would require an assessment of "individual issues, including the obligation created by each"

[1] No. 17-6146 (10th Cir. May 3, 2019).
[2] The class definition proposed by Naylor Farms in its motion for class certification is quoted in the ruling of the district court granting certification of a modified class. *Naylor Farms, Inc. v. Chaparral Energy, LLC,* 2017 WL 187542 (W.D. Okla. Jan. 17, 2017), at *2. The district court ruled: "[P]laintiffs' motion for class certification [Doc. #134], with the stated modifications, is granted. Plaintiffs' fraud claim will be excluded and the class will be limited to include those leases with "Mittelstaedt Clauses" listed on plaintiffs' Exhibit 29." 2017 WL 187542 at *9. By later proceedings, the class definition was further revised to specify June 1, 2006, as the commencement date of the class period. Naylor Farms filed its Amended Class Definition (including the incorporation of the revisions referred to in the district court's Order of January 17, 2017) with the clerk of the district court. See Doc. 175, filed April 17, 2017, and Doc. 176, filed April 18, 2017.
[3] Certain of the class certification proceedings in this case occurred *after* Chaparral filed for bankruptcy. The bankruptcy court lifted the automatic stay on the underlying proceedings so that the district court could rule on Naylor Farms' motion for class certification.
[4] *Id.* at 3.
[5] *Id.* at 2-3. The court stated that the IDM "imposes upon lessees 'a duty to provide a marketable product available to market.'" (citing *Mittelstaedt v. Santa Fe Minerals, Inc.*, 954 P.2d 1203, 1206 (Okla. 1998)).
[6] *Id.* at 3. The term "GCDTP services" was used by the Tenth Circuit early in its opinion to refer to the "gathering, compressing, dehydrating, transporting, and producing" of raw or unprocessed gas. *Id.*
[7] *Id.* at 4.
[8] *Id.*
[9] *See* footnote 2, *supra*.

individual oil and gas lease "and the gas produced from each" individual well,[10] and would raise individual questions as to damages. Chaparral urged that those issues would predominate over any common questions. The district court disagreed and found that class certification was appropriate, except that it excluded Naylor Farms' fraud claim from the class certification order.[11]

Chaparral appealed. It asserted three primary arguments in support of its effort to obtain a reversal of the class certification order. First, Chaparral contended that *marketability* constitutes an individual question that predominates over any common questions. Second, it argued that distinctions in lease language also give rise to individual questions that likewise predominate in this case. Finally, Chaparral contended that there is a lack of evidence showing that it employs a uniform payment methodology to support certification. The Tenth Circuit proceeded to address "whether the district court abused its discretion in concluding that Naylor Farms satisfied Rule 23's certification requirements."[12]

The court first addressed the issue of marketability. The Tenth Circuit stated that "[i]t has been more than two decades since the Oklahoma Supreme Court (OSC) has said anything meaningful about marketability,"[13] citing *Mittelstaedt v. Santa Fe Minerals, Inc, supra.* However, finding that *Mittelstaedt* did not provide guidance on the specific marketability questions presented in this appeal, the court stated that its "task is **'to predict how [the OSC] would rule'** if it were to answer those questions."[14] The court then reviewed the principles and reasoning applied by the Oklahoma Supreme Court in *Mittelstaedt*, and in the more recent Oklahoma Court of Appeals decisions in *Whisenant v. Strat Land Expl. Co.,*[15] and *Pummill v. Hancock Expl. LLC*.[16]

Chaparral contended that the district court erred in ruling "that (1) the question of when the gas became marketable can be answered via generalized, classwide proof and (2) as a result, the marketability question doesn't defeat predominance."[17] Chaparral additionally argued that the district court erred in treating marketability as a question of law, rather than as a question of fact. It asserted that a determination of the marketability question and whether Chaparral breached the IDM requires a "well-by-well analysis to determine whether any of the gas at issue was marketable at the wellhead."[18] Thus, the marketability question would defeat commonality and predominance.

However, the Tenth Circuit found that "the district court's ruling that marketability is subject to classwide proof under the specific facts of this case is entirely consistent with the [Oklahoma Court of Civil Appeals'] decision in *Pummill*."[19] With regard to Chaparral's reliance on the *Whisenant* decision, the court noted Chaparral's insistence that "marketability can *never* be susceptible to classwide proof because it will always require an individualized assessment of the gas produced by each well."[20] The court emphasized, however, that *Whisenant's* finding that certain of the factual issues were not susceptible to generalized proof was with reference to *that particular case*. "[T]he *Whisenant* court recognized that the OSC has declined to adopt a uniform test for determining when

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[10] *Id.*at 5.
[11] See footnote 5 in the *Naylor Farms* opinion.
[12] *Id.* at 7.
[13] *Id.* at 8.
[14] *Id.* [Emphasis added]
[15] 429 P.3d 703, 2018 OK CIV APP 65.
[16] 419 P.3d 1278, 2018 OK CIV APP 48.
[17] *Naylor Farms,* at 20.
[18] *Id.* at 23.
[19] *Id.* at 26.
[20] *Id.*

gas becomes marketable [and instead] left the issue open to resolution on a case-by-case basis."[21] The court left open the possibility that, in some cases, a determination might be made as to "when gas became marketable without undertaking an individualized inquiry into the quality of that gas."[22]

The court then found that "the facts in *Pummill* (and, by extension, the facts in this [Chaparral] case) fit comfortably in the space 'left … open' by *Whisenant*."[23] In light of the court's reading of *Pummill* and *Whisenant*, the Tenth Circuit predicted that the Oklahoma Supreme Court would hold:

> under the facts of this case, a jury could determine when the gas at issue became marketable without individually assessing the quality of that gas; instead, a jury could make this determination based solely on the expert testimony that all the gas at issue was required to undergo at least one GCDTP service before it could "reach" and be "sold into" the pipeline market.[24]

The district court in *Chaparral* was found to have not abused its discretion by concluding that the question of marketability "*in this particular case* is subject to common, classwide proof for purposes of satisfying Rule 23's commonality and predominance requirements."[25]

The court next turned to Chaparral's contention that distinctions in oil and gas lease language present individual questions that predominated over any common questions. The district court below rejected that argument and found that "its decision to limit the class to leases containing a *Mittelstaedt* Clause renders such an individualized analysis unnecessary."[26] Most of the Tenth Circuit's discussion addressing this particular area of the appellants' arguments focuses on which issues were presented and preserved below. The Tenth Circuit was not persuaded that the district court abused its discretion in certifying the class despite the existence of what the court characterized as *minor* variations in oil and gas lease language.

Finally, Chaparral urged on appeal that "Naylor Farms failed to demonstrate that Chaparral uses a uniform payment methodology to calculate royalty payments,"[27] and that such failure warranted the denial of class certification. However, while the existence of a uniform payment methodology, *alone*, was found by the court to be insufficient to meet the predominance requirement, the court rejected the notion that such a methodology is a necessary component for satisfying predominance. Moreover, the court noted that "[t]he fact that damages may have to be ascertained on an individual basis is not, standing alone, sufficient to defeat class certification."[28] Naylor Farms presented evidence that individualized evidence will not be needed because its expert can determine damages on a classwide basis through the use of a model. The Tenth Circuit further noted that the district court could also, if needed, divide the class into subclasses for purposes of determining damages.[29] The district court was found to have not abused its discretion in concluding that individual questions about damages do not defeat predominance.

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[21] *Id.* at 27.
[22] *Id.*
[23] *Id.*
[24] *Id.* at 28.
[25] *Id.*
[26] *Id.*
[27] *Id.* at 33.
[28] *Id.* at 34, citing *Menocal v. GEO Grp., Inc.,* 882 F.3d 905, 916-17 (10th Cir.), *cert. denied,* 139 S. Ct. 143 (2018).
[29] *Id.* at 34.

The Tenth Circuit Court of Appeals affirmed the district court's order granting Naylor Farms' motion for class certification subject to certain modifications of the class definition consistent with its opinion.

Owner of Executive Rights Breached Duty under Texas Law by Refusing to Grant Lease

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In *Texas Outfitters Limited, LLC v. Nicholson*, 2019 WL 1575018, _____ S.W.3d ____ (Tex. 2019), Texas Outfitters owned the surface of a 1,082-acre tract in Frio County, Texas. The company purchased the land to use for its hunting business and as a residence for its owner. Texas Outfitters also purchased a 4.16% mineral interest and the executive rights over a 45.84 % mineral interest owned by Dora Jo Carter and her children (the Carters). The Hindes family owned the other 50% mineral interest.

The Hindes family leased their mineral interest to El Paso Oil for a $1,750 per acre bonus and a 25% royalty. El Paso offered to lease the mineral interests owned by Texas Outfitters and the Carters on the same terms. The Carters wanted Texas Outfitters to accept El Paso's offer, but Texas Outfitters declined it. Another company later offered to take a lease on terms that included a $2000 per acre bonus, but that prospective lessee withdrew its offer when it learned that El Paso already had leased a 50% mineral interest. Yet another company offered to give a $1500 bonus to lease the property, but that company also withdrew its offer. Subsequently, the results of nearby drilling suggested that the 1,082-acre tract held less promise for oil and gas development than had been thought, and Texas Outfitters received no more offers to lease the land.

The Carters filed suit, alleging that Texas Outfitters, in its role as executive, had breached its duty to the non-executives (the Carters) by refusing to accept the lease from El Paso. At trial, the parties offered competing testimony regarding Texas Outfitters's motivation for declining El Paso's offer. Texas Outfitters presented testimony that it had declined the lease in hopes that drilling on nearby land would be successful and that the price for leases would increase. The Carters presented testimony that the owner of Texas Outfitters had previously asserted that he would not lease the land because oil and gas activity might interfere with his company's hunting business.

After a bench trial, the trial court entered judgment for the Carters, awarding them monetary damages in an amount equal the bonus they would have received if Texas Outfitters had accepted El Paso's offer. In its written reasons for judgment, the court seemed to suggest that Texas Outfitters's decision to decline the offer was motivated in part by its desire to have unfettered use of the surface for its hunting operation.

The court of appeals affirmed, concluding that the evidence supported a finding that, to the detriment of the Carters, Texas Outfitters had refused to grant a lease in order to protect its surface interests. In its written opinion, the appellate court suggested that the Texas Supreme Court's decision in *Lesley v. Veterans Land Board*, 352 S.W.3d 479 (Tex. 2011) set the standard for judging an executive's conduct when the executive declines to grant a lease, but that *KCM Financial LLC v. Bradshaw*, 457 S.W.3d 70 (Tex. 2015) sets the standard for judging an executive's conduct when the executive grants a lease.

The Texas Supreme Court agreed to hear the case. In its discussion of the executive's duty, the Texas Supreme Court first noted that the executive right—that is, the right to execute oil and gas leases—is one of the "bundle of sticks" inherent in mineral ownership. When the executive right is severed from other incidents of mineral ownership, the executive owes a duty to the non-executive.

The court stated that the parameters of the duty are difficult to describe, but that the court's jurisprudence provides "several guiding principles."

In this case, the Texas Supreme Court began its analysis of the executive's duty by rejecting the appellate court's suggestion that two different standards apply, depending on whether a non-executive complains about the executive's refusal to grant a lease or about the terms of a lease that the executive has granted. Instead, only one standard applies. Of course, different fact patterns may raise different issues. For example, the executive may violate his duty if he grants a lease (covering the non-executive's interest) to himself or to a relative at a below-market price.

Further, although the duty generally does not require the executive to subjugate his interests to those of the non-executive, the executive generally has a duty, when exercising his authority, to obtain for the non-executive every benefit that he obtains for himself with respect to any type of interest that both the executive and non-executive have. Thus, if the executive owns a mineral interest, so that both the executive and non-executive have a right to receive royalties, the executive probably violates his duty if he grants a lease that gives a higher royalty to himself than to the non-executive. The court referred to these parameters of the duty as the "non-subjugation" principle and the "equal benefits" principle.

The court went on to explain, however, that the equal benefits principle does not apply when the executive has a right to some benefit that the non-executive does not have. Thus, if only the executive has a right to lease bonuses or rentals, the executive does not breach his duty by negotiating for a lease that includes a lease bonus or delay rentals. Further, if the executive owns the surface, the executive does not necessarily breach his duty if he negotiates for a lease that provides some surface protection. However, the executive beaches his duty if, by obtaining a benefit for himself, he "unfairly" harms the non-executive's interest. Thus, an executive who owns the surface might violate his duty if he exercised his authority in a way that protected the surface, while "unfairly" harming the non-executive's interest.

The Texas Supreme Court noted that, because Texas Outfitters owned the surface estate, the "equal benefits" principle did not apply. That is, although the Carters would not share in any of the benefits associated with the acquisition of surface protections, Texas Outfitters would not "necessarily" violate its duty to the Carters merely by seeking to protect the surface. On the other hand, Texas Outfitters would breach its duty if it obtained surface protections in a way that "unfairly" harmed the Carters' interest. The court noted that the Carters had introduced evidence that it was "common" for surface owners who used their land for commercial hunting to enter oil and gas leases that accommodated the surface owner. Yet, Texas Outfitters had declined to grant a lease, thereby obtaining greater protection for surface. The court held that "legally sufficient evidence supports the trial court's finding that," under the facts of this case, Texas Outfitters' refusal to grant a lease "unfairly diminished the value of the Carters' mineral interest." On that basis, the Texas Supreme Court affirmed the judgment in favor of the Carters, while emphasizing that the resolution of disputes between executives and non-executives is very "fact-dependent."

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