

BEFORE THE WEST VIRGINIA SUPREME COURT OF APPEALS

**ESTATE OF GARRISON G. TAWNEY, by
LELA ANN GOFF, Executrix, LELA ANN
GOFF and VERNON B. GOFF, husband and
wife, JANICE E. COOPER and CLIFFORD R.
COOPER, husband and wife, LARRY G.
PARKER, JOHN W. PARKER, RICHARD L.
ASHLEY, MYRTLE JONES, by her
Attorney-in-Fact, ORTON A. JONES**

Plaintiffs,

v.

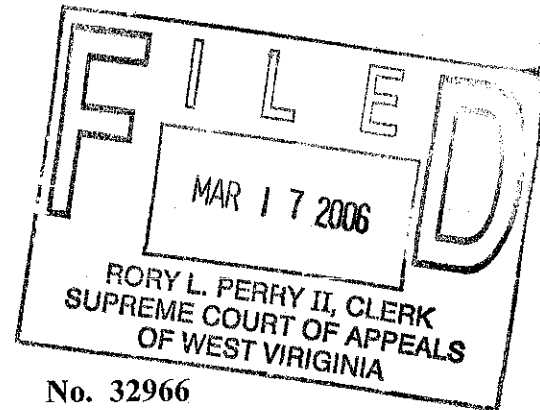
**COLUMBIA NATURAL RESOURCES,
LLC, f/k/a COLUMBIA NATURAL
RESOURCES, INC., a Texas corporation.**

Defendants.

**BRIEF OF DEFENDANT
COLUMBIA NATURAL RESOURCES, LLC,
ON CERTIFIED QUESTIONS**

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No. 32966

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I. KIND OF PROCEEDING AND NATURE OF RULING

The proceeding below is a class action suit commenced nearly three years ago in the Circuit Court of Roane County, West Virginia, on behalf of all persons who are or who have been royalty owners under West Virginia oil and gas leases with CNR or who are or have been beneficiaries of such leases since 1990. There are approximately 8,000 royalty owners who may have claims in the pending action ("Plaintiffs"). In their February 3, 2003, Complaint, December 22, 2004, Amended Complaint, and April 8, 2005, Second Amended Complaint, Plaintiffs sought class certification and alleged, among other things, that CNR's deductions from royalty payments for gathering, processing, line loss, and fuel use were improper. The parties have been engaged in extensive discovery, which has included the production and review of approximately 2,258 West Virginia leases of varying forms and types. Based on CNR's lease review, approximately 651 are flat-rate leases, 508 are proceeds leases, 100 are market price leases, 702 are market value leases, and 297 are leases that are formula, special or other forms which are not easily categorized. Of the total number of leases, at least 1,382 have language stating that the royalty is to be calculated "at the well" or "at the wellhead," or specifying that the royalty is to be calculated "net of all costs beyond the wellhead," or specifying that the royalty is to be "less all taxes, assessments, and adjustments."

The nature of the lower court's ruling involves interpretation of the language of Plaintiffs' leases. Leases with the named Plaintiffs, including Lease No. 1203122, dated October 27, 1989, and Leases Nos. 1204255, 1204256, 1204257, dated August 1, 1990, include the following royalty clause:

To pay Lessor an amount equal to 1/8 of the price, **net of all costs beyond the well head**, received by lessee for all gas and the constituents thereof produced and marketed from the Leasehold during the preceding month. The time and method

of marketing (g)as produced from any well on the Leasehold and the amount thereof that shall be used or marketed shall be within the sole discretion of Lessee.

Another example is a lease dated January 31, 1956, Lease No. 1013795 between Josephine H. Sutherland, et al. and United Fuel Gas Company, which provides:

. . . to pay for each gas well other than Well 1491, from the time and while gas is marketed, at the rate of their proportionate part of one-eighth (1/8) of the wholesale market value thereof **at the well** based on the usual price paid therefor in the general vicinity. . . .

Lease No. 1026481 between Nighbert Land Company and United Fuel Gas Company dated November 15, 1928, provides:

To pay for one-eighth (1/8) of the gas produced from each well their proportionate part thereof from the time and while gas is marketed, at the rate paid for gas **at the well or wells** on adjacent or neighboring lands or in the immediate vicinity....

Lease No. 1183376 dated November 10, 1988, provides:

To pay Lessor, an amount equal to one-eighth of the price, **net of all costs beyond the well head**, received by Lessee for all gas and the constituents thereof produced and marketed from the Leasehold, . . . The time and method of marketing gas produced from any well on the Leasehold and the amount thereof that shall be used or marketed shall be within the sole discretion of Lessee. . . .

And Lease No. 1213690, dated June 26, 1999, includes a royalty clause that provides:

ROYALTY: To Pay Lessor a Royalty, less all taxes, assessments, and adjustments on production from the Leasehold as follows:

2. **GAS:** To pay Lessor an amount equal to one-eighth of the revenue realized by Lessee for all gas and the constituents thereof produced and marketed from the Leasehold. . . .

While these sample leases appear in different forms and over different time periods, they all contain provisions explicitly providing that the point of valuation of the gas for purposes of the payment of royalty is at the well, not at a downstream delivery point where the sale occurs at interconnection points of gathering systems with the major interstate transmission pipelines.

The parties filed cross-motions for summary judgment regarding whether, as a matter of law, CNR could take deductions for "post-production" expenses. CNR sought summary judgment only with respect to leases containing "at the well" or similar royalty language. In contrast, Plaintiffs' Motion for Summary Judgment focused on *all* leases. On September 19, 2005, the Circuit Court heard argument on both motions. The Circuit Court then denied CNR's motion for summary judgment regarding the deductibility of post-production expenses where "at the well," "net of all costs beyond the well," or similar language is used and granted the Plaintiffs' motion for summary judgment regarding all leases, holding that, as a matter of law, "at the well," "at the wellhead," "net of all costs beyond the wellhead" and all other lease language as set forth in Exhibit A to the Order of Certification (see, Plaintiffs' Designation of Record, Exhibit 1) is ambiguous with regard to the allocation of post-production costs, and that, therefore, no deductions could be taken.

In rendering its decision, the Circuit Court stated that certain portions of the opinion of this Court in Wellman v. Energy Resources, Inc., 210 W. Va. 200, 557 S.E.2d 254 (2001), which would allow such deductions, provided that the lessee could prove such expenses were actual and reasonable, were simply non-binding dicta and were not the law of West Virginia. The Circuit Court also stated that it believed that this Court would follow the Colorado decision of Rogers v. Westerman Farm Co., 29 P.3d 887 (Colo. 2001), a case not considered in Wellman, which held that "at the well" and similar language is silent with regard to the allocation of post-

production expenses. However, the Circuit Court also recognized that whether this Court would do so was not clear and ordered that questions be certified to this Court.

On January 11, 2006, this Court agreed to review the certified questions. CNR now asks this Court to reverse the trial court on the basis that the “deductibility” language in the leases is clear and unambiguous and, as a matter of law, those leases which contain express deductibility language allow the lessee to deduct the royalty owners’ proportionate share of post-production expenses, provided CNR can prove as if in an action for an accounting that such expenses are actual and reasonable. Wellman, 210 W. Va. at 211, 557 S.E.2d at 265.

It is clear that the lower court’s adoption of Rogers is a radical departure from existing law in West Virginia as to the deduction of post-production expenses and, as acknowledged by the Circuit Court, constitutes the adoption of a minority rule which has been roundly criticized by legal scholars throughout the country. Because the Circuit Court’s adoption of this radical minority rule has the potential to affect not only the several thousand leases involved in this case, but also to drastically alter royalty payment methodology for all oil and gas producers in the state, CNR urges this Court to answer the questions certified to it in the manner requested by CNR.

II. STATEMENT OF THE FACTS

The Plaintiffs’ claims relate to gas wells located in Roane County, West Virginia, and elsewhere throughout the state. These wells were drilled pursuant to leases executed by the parties. In addition to the leases described above, those leases believed to be relevant are represented in the class action by the leases of the named plaintiffs, which are summarized as follows:

LEASE NO.	LEASE DATE	LESSOR	ROYALTY PROVISION
1203122-000	10/27/1989	Frieda V. Tawney and Garrison V. Tawney	Gas: To pay lessor an amount equal to 1/8 of the price, net of all costs beyond the wellhead,

LEASE NO.	LEASE DATE	LESSOR	ROYALTY PROVISION
			received by lessee for all gas and the constituents thereof produced and marketed from the Leasehold during the preceding month. The time and method of marketing gas produced from any well on the Leasehold and the amount thereof that shall be used or marketed shall be within the sole discretion of Lessee.
1204255-002	08/01/1990	Frederick Clyde Parker and Beatrice A. Parker, his wife, by Fredrick Lee Parker, their Attorney-in-Fact; Georgie E. Shafer, widow; Eva Jane Parker, widow; Ronald L. Parker, single; Donald W. Parker and Rita C. Parker, his wife	Gas: To pay lessor an amount equal to 1/8 of the price, net of all costs beyond the wellhead, received by lessee for all gas and the constituents thereof produced and marketed from the Leasehold during the preceding month, but no royalty will be paid for stored gas and gas produced from storage horizons. The time and method of marketing gas produced from any well on the Leasehold and the amount thereof that shall be used or marketed shall be within the sole discretion of Lessee.
1204256-000	08/01/1990	Frederick Clyde Parker and Beatrice A. Parker, his wife, by Fredrick Lee Parker, their Attorney-in-Fact; Georgie E. Shafer, a widow; Eva Jane Parker, a widow; Ronald L. Parker, single; Donald W. Parker and Rita C. Parker, his wife	Gas: To pay Lessor an amount equal to 1/8 of the price, net of all costs beyond the wellhead, received by Lessee for all gas and the constituents thereof produced and marketed from the Leasehold during the preceding month, but no royalty will be paid for stored gas and gas produced from storage horizons. The time and method of marketing gas produced from any well on the Leasehold and the amount thereof that shall be used or marketed shall be within the sole discretion of Lessee.
1204257-000	08/01/1990	Frederick Clyde Parker and Beatrice Parker, his wife; by Fredrick Lee Parker, their Attorney-in-Fact; Georgie E. Shafer, widow; Eva Jane Parker, widow; Ronald L. Parker, single; Donald W. Parker and Rita C. Parker, his wife	Gas: To pay lessor an amount equal to 1/8 of the price, net of all costs beyond the wellhead, received by lessee for all gas and the constituents thereof produced and marketed from the Leasehold during the preceding month, but no royalty will be paid for stored gas and gas produced from storage horizons. The time and method of marketing gas produced from any well on the Leasehold and the amount thereof that shall be used or marketed shall be within the sole discretion of Lessee.

Despite the plain and unambiguous terms of the above-quoted leases as they relate to the payment of royalties on gas production, the Plaintiffs have essentially alleged (1) that they were entitled to be paid royalties based upon "fair market value" of the gas produced, (2) that "improper deductions" were made for costs incurred downstream of the wellhead, and (3) that they were somehow misled or deceived because the stubs provided with their royalty payment checks did not include an explanation of the manner in which royalties were calculated.

Plaintiffs make these allegations despite the fact that they cannot cite any lease language which entitles them to be paid on a fair market value basis. They fail to acknowledge the plain and unambiguous language in the leases which expressly authorizes the deduction of costs incurred downstream of the wellhead. They do not mention that the above-quoted leases involving the named Plaintiffs have express language defining the place where the royalty is to be computed, and contain marketing clauses, i.e., express provisions that the “time and method of marketing . . . shall be within the sole discretion of lessee.” Plaintiffs also fail to cite any provision of their leases prescribing any particular method, manner or format required in documentation of their royalty payments.

The Plaintiffs also assert that “at the well” lease language should be interpreted as silent with regard to post-production expenses in light of a rule favoring strict construction against the gas lessee. Ironically, the named Plaintiffs in this action are not individuals in need of the protection of such a rule because (1) the named Plaintiffs received the advice of legal counsel regarding the leases at issue and made changes to their leases; and (2) a whole sub-class of Plaintiffs are sophisticated business entities who cannot be said to have unequal bargaining power.

Named Plaintiff Larry Parker testified at deposition that he received the advice of an attorney before signing his lease:

Q: Do you recall any specific paragraphs of this lease that caused you to call Mr. Brumbaugh or Mr. Gaston and ask a question about –

A: Well, yeah, I’m sure I just asked their best – I asked for their advice, I am sure, and not Gaston but probably Brumbaugh and probably my father-in-law.

(Parker Depo., CNR’s Designation of Record, Doc. No. 24, 63:14-21). Named Plaintiff Garrison Tawney also testified that he received the advice of counsel prior to signing his lease. He even

testified that his counsel made revisions to the document. (Tawney Depo., CNR's Designation of Record, Doc. No. 23, 92:19-23, 93:1-23, 94:1-23, 95:1-23, 96:1). The large landowner subclass boasts a long list of businesses who negotiated and entered into oil and gas leases freely. This list includes Boone East Development Company, Cole & Crane Real Estate Trust, Cotiga Development Company, and Kanawha Gauley Coal & Coke Company to name a few.

A. HOW GAS IS PRODUCED AND MARKETED.

Natural gas that is produced from the Plaintiffs' leaseholds comes to the surface at the "wellhead." From the wellhead, the gas passes through small diameter field lines until such time as it connects to "gathering lines" or "gathering systems."¹ Once the gas enters the gathering system it is marketable, but some of the gas produced is not in a state in which it can be delivered to the major interstate pipelines. The gas is "wet" or otherwise contains natural gas liquids ("NGLs"). Accordingly, for those wells that produce wet gas, the gas is gathered and delivered to a downstream "processing plant," which, during the relevant time period, has been operated by Columbia Gas Transmission Corporation ("TCO"), which was a CNR affiliate until 2003, or by an unaffiliated third party, MarkWest. (See, Warnick Deposition, Plaintiffs' Designation of Record, Exhibit 2(a) at 80-83). The processing plant removes the NGLs so that the gas is pipeline quality and, therefore, can be delivered to the major interstate pipeline interconnections. When MarkWest removes the NGLs, pursuant to contract with CNR, CNR pays to MarkWest a 3 cent per dekatherm "processing fee." MarkWest, in turn, in recognition of the btu content of the NGLs that are removed, contracts to deliver back an equivalent quantity of replacement gas to CNR on a btu basis so that CNR has the same equivalent of gas to sell after

¹ Some of the gathering systems in question were, until 1997, owned and operated by Columbia Gas Transmission Corporation. After 1997, these gathering lines were sold to CNR pursuant to proceedings before the Federal Energy Regulatory Commission.

processing as it had before processing. Accordingly, CNR, as seven-eighths owner of the NGLs, and the royalty owner, as a one-eighth owner of the NGLs, are compensated with an equivalent volume of gas and btus, which is the basis on which gas is sold.

Gas produced by CNR throughout the State of West Virginia travels through hundreds of gathering lines that look like “spaghetti” on a map. (See, Chandler Deposition, Plaintiffs’ Designation of Record, Exhibit 2(b) at 30, 51). These lines interconnect and join with other gathering lines to gather, ship and transport gas to major interconnection points on the interstate pipelines. Gas that is so gathered and delivered at various points into the interstate lines is considered the “pooled gas.”

CNR, when marketing and selling gas delivered to – for example – the TCO pool, contracts with purchasers to buy gas from the TCO pool at interconnections on the TCO pipelines. Since no molecule of gas from a particular well can be traced to a particular end user or purchaser of gas, all gas which is commingled and delivered into the TCO pool is sold under various contracts at various interconnection points at which gas is delivered to the TCO lines. In order to treat all lessors equitably, CNR pays royalty based upon the weighted average sales price of gas for gas sales from the TCO pool. That is, all contracts for purchases of gas from the TCO pool are combined and averaged based upon the volume of gas sold under each contract and the price negotiated for each contract, so that each royalty owner and CNR are paid based upon the weighted average proceeds from the sale of gas. This weighted average price is for the value of gas in the TCO pool downstream of the wellhead.

Once this weighted average proceeds price of gas is determined, calculations are made in order to arrive at the price “at the wellhead.” In the present case, the leases under which the Plaintiffs are claiming entitlement expressly provide that they are to be paid “net of all costs

beyond the wellhead” or “at the well” and based upon the price received by the lessee for all gas, not fair market value. Accordingly, when calculating and paying royalties to the named Plaintiffs, CNR starts with the weighted average price of gas sold from the TCO pool, then deducts the cost incurred between the TCO pool and the wellhead for gathering, processing, compression and line loss in order to compute the net proceeds price at the well.

B. GATHERING CHARGES.

A large component of the deductions downstream of the wellhead is the cost of shipping the gas from the well on the gathering lines to the interstate pipeline interconnection points. The amount that is charged has changed over time, but in all cases has been determined in rate proceedings subject to the exclusive jurisdiction and authority of the Federal Energy Regulatory Commission (“FERC”) or pursuant to a negotiated contract with various third party, independent producers of gas in West Virginia, as explained below.

Up to 1997, many of the gathering systems in question were owned and operated by TCO.² During TCO’s ownership, the lines, for rate purposes, were subject to the exclusive jurisdiction of FERC. CNR has produced in discovery various documents which demonstrate that this rate developed and changed over time as the result of FERC policy requirements and individual rate settlements.

Pursuant to deregulation of the natural gas industry and various Orders issued by FERC in the 1980s and 1990s, FERC required the “unbundling” of services rendered by the interstate pipeline companies. As a result of the FERC Orders, TCO sold various gathering systems, including gathering systems throughout West Virginia. CNR’s purchase of these lines (called a “spindown”) was subject to adversary proceedings before FERC and was ultimately approved by

² Other gathering systems, such as the “Cottontree” system, were constructed by CNR after 1997.

that body. When the lines were sold to CNR, the rate for gathering charges was based upon a cost of service³ and was negotiated and set for a period of time in order to protect third-party producers. Pursuant to FERC Certification of Uncontested Settlement issued on January 15, 1997, once facilities were sold to CNR, it was obligated to transport gas on the CNR gathering system at a gradually increasing rate starting at 25 cents and rising to 32 cents for the final period of February 1, 2000, to February 1, 2001.⁴ This 32-cent rate was extended by agreement for one year to February 1, 2002. After February 1, 2002, the gathering rate was again negotiated with unaffiliated third party producers through their industry representatives including the Independent Oil and Gas Association of West Virginia. Pursuant to exchanges and analyses of accounting data by experts on both sides, CNR has negotiated rates which are deemed by unaffiliated third party producers as fair and reasonable rates representative of the actual costs incurred by CNR for the operation of said lines in West Virginia. Thus, in summary, the gathering rates in question either have been established by and subject to the sole and exclusive jurisdiction of FERC or, after the "spin down," have been subject to negotiated contract rates acknowledged as fair and reasonable with unaffiliated third party producers and shippers in West Virginia.

³ The determination of gathering rates is based upon FERC or Public Service Commission specified accounting procedures that designate the "cost of service" for operation of a gathering system. (See, Chandler Deposition, Plaintiffs' Designation of Record, Exhibit 2(b) at 27-28.) Thus, in analyzing the cost of operation of the gathering systems, standard utility accounting formulas are used for purposes of calculating the cost of service, and then the rate is negotiated with unaffiliated third-party producers.

⁴ TCO agreed to charge the same rates for gathering through February 1, 2000, for gathering systems it retained, which would be the rates applicable to the named plaintiffs through 1999 when CNR acquired the TCO gathering assets in Roane County.

C. THE PROCESSING FEE.

The processing fee paid to MarkWest by CNR is subject to a negotiated contract rate which is currently 3 cents per dekatherm, but for portions of the period relevant to this litigation was 6 cents per dekatherm. (See McCracken Deposition, Plaintiffs' Designation of Record, Exhibit 2(c) at 48-50.) The MarkWest contract further provides that because the NGLs are stripped out of the gas, MarkWest returns an equivalent btu volume of gas into the lines so CNR and its royalty owners have the same volume and btu quantity to sell that they possessed prior to processing. (See Chandler Deposition, Plaintiffs' Designation of Record, Exhibit 2(b) at 53-57; McCracken Deposition, Plaintiffs' Designation of Record, Exhibit 2(c) at 108-11.)

D. COMPRESSION AND LINE LOSS.

Certain gas produced at the well is not under sufficient pressure in pounds per square inch to enter into downstream gathering and/or interstate pipelines. Accordingly, the gas must go through various compressor facilities to increase the pressure in the pipelines to enable the gas to flow into the downstream pipelines. These compressor facilities, downstream of the wellhead, generally use natural gas as fuel to operate and run the compressor engines. (See Chandler Deposition, Plaintiffs' Designation of Record, Exhibit 2(b) at 51.) Further, as is standard and normal in the industry, a certain amount of gas is lost during the process of gathering, compression, and transportation. This "line loss" represents a "shrinkage," or lost and unaccounted for gas that is not sold by CNR and is a reduction of the gross volume produced by each well. (See Chandler Deposition, Plaintiffs' Designation of Record, Exhibit 2(b) at 51.) Accordingly, no gas revenue is obtained by CNR for such lost gas or gas used as fuel. Because no revenue is obtained, no royalty is paid.

III. POINTS AND AUTHORITIES

1. “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.” Syl. pt. 4, Wellman v. Energy Resources, Inc., 210 W. Va. 200, 557 S.E.2d 254 (2001) (emphasis added).

2. “If an oil and gas lease provides that the lessor shall bear some part of the costs incurred between the wellhead and the point of sale, the lessee shall be entitled to credit for those costs to the extent that they were actually incurred and they were reasonable. Before being entitled to such credit, however, the lessee must prove, by evidence of the type normally developed in legal proceedings requiring an accounting, that he, the lessee, actually incurred such costs and that they were reasonable.” Id. at Syl. pt. 5.

3. “[T]his Court believes that the language of the leases in the present case indicating that the ‘proceeds’ shall be from the ‘sale of gas as such at the mouth of the well where gas ... is found’ might be language indicating that the parties intended that the ... lessors, would bear part of the costs of transporting the gas from the wellhead to the point of sale.” Id. at 211, 265.

4. “[W]hen a certified question is framed so that this Court is not able to fully address the law which is involved in the question, then this Court retains the power to reformulate the questions certified to it.” Kincaid v. Mangum, 189 W. Va. 404, 432 S.E.2d 74 (1993). See, also, Ferrell v. Nationwide Mut. Ins. Co., 217 W. Va. 243, 617 S.E.2d 790 (2005).

5. A covenant will be implied in a contract only where the contract contains no express provisions with regard to the subject matter of the implied covenant. Croston v. Emax Oil Co., 195 W. Va. 86, 464 S.E.2d 728 (1995); Thompson Dev., Inc. v. Kroger Co., 186 W. Va.

482, 413 S.E.2d 137 (1991); De Stubner v. Microid Process, 124 W. Va. 591, 21 S.E.2d 154 (1942); Berry v. Humphreys, 76 W. Va. 668, 669, 86 S.E. 568, 569 (1915).

6. Where contract terms are clear and unambiguous, they must be applied by the court and not construed. Syl. pt. 3, Waddy v. Riggleman, 216 W. Va. 250, 606 S.E.2d 222 (W. Va. 2004); Syl. pt. 2, Orteza v. Monongalia County General Hosp., 173 W. Va. 461, 318 S.E.2d 40 (1984); Syl. pt. 2, Bethlehem Mines Corp. v. Haden, 153 W. Va. 721, 172 S.E.2d 126 (1969).

7. “[A]n oil and gas lease which [sic] is clear in its provisions and free from ambiguity, either latent or patent, should be considered on the basis of its express provisions and it is not subject to a practical construction by the parties.” Cotiga Dev. Co. v. United Fuel Gas Co., 147 W. Va. 484, 495, 128 S.E.2d 626, 634 (1962).

8. It “is not the right or province of the court to alter, pervert or destroy the clear meaning and intent of parties as plainly expressed in their written contract or to make a new and different contract for them.” Id.

9. It is a basic tenet of contract construction that each and every word is to be given meaning, and that the court cannot create or impose an implied covenant or construction that is inconsistent with the express terms of the contract. Barn-Chestnut, Inc. v. CFM Dev. Corp., 193 W. Va. 565, 572, 457 S.E.2d 502, 509 (1995).

10. Individual terms in a contract provision are not to be interpreted separately, but are to be read together with all other words in that contract provision so that all words are given meaning. See, e.g., Moore v. Johnson Serv. Co., 158 W. Va. 808, 814, 219 S.E.2d 315, 320 (1975); Chambers v. Simmons, 76 W. Va. 174, 179, 85 S.E. 182, 184 (1915).

11. “This and all other courts of this land have laid down certain rules for ascertaining the intent of parties to any written instrument. If the language used be clear and unambiguous, it

simply 'applies' the language used to the factual situation. If it is found to be ambiguous, the rules applicable to that type of instrument are used to ascertain the meaning of the parties and if the instrument contains irreconcilable provisions the rules are equally well established for determining the dominant intent in the circumstances." Lewis v. Dils Motor Co., 148 W. Va. 515, 523-24, 135 S.E.2d 597, 601-02 (1964).

12. The purpose of the rule of construction directing that oil and gas leases, if ambiguous, should be interpreted strictly against the lessee is to protect individuals with little knowledge regarding the oil and gas industry from aggressive agents who convince them to sign form leases without the benefit of legal advice. Bettman v. Harness, 42 W. Va. 433, 438, 26 S.E. 271, 276 (1896) (overruled on other grounds).

IV. CERTIFIED QUESTIONS AND REQUEST FOR REFORMULATION

The Circuit Court ordered that the following questions be certified to this Court.⁵

Question 1: Where the royalty language is as set out in Exhibit A, may a lessee of oil and gas in West Virginia deduct money and/or volume from the lessor's 1/8 royalty payments where the lease does not provide specifically that the lessee may take the deductions?

Question 2: Where in an oil and gas lease there is no specific provision allowing for deduction of post-production expenses does language such as "wholesale market at the well," "amount realized at the well," "net revenue realized," "1/8 of the price," "net of all costs beyond the wellhead," and other language as set forth in Exhibit A, grant to the lessee the right to deduct post-production expenses from the lessor's royalty?

⁵ CNR and the Plaintiffs could not come to an agreement as to the proper wording of the certified questions, so CNR and the Plaintiffs individually submitted to the Circuit Court proposed certified questions. The Circuit Court chose to use the Plaintiffs' proposed certified questions without revision.

CNR again asks that this Court utilize its power to reformulate certified questions because such questions, as currently drafted, (1) go beyond the scope of CNR's motion for summary judgment, and (2) do not allow the Court to fully consider the relevant law before it. "[W]hen a certified question is framed so that this Court is not able to fully address the law which is involved in the question, then this Court retains the power to reformulate the questions certified to it." Kincaid v. Mangum, 189 W. Va. 404, 405, 432 S.E.2d 74, 75 (1993). See, also, Ferrell v. Nationwide Mut. Ins. Co., 217 W. Va. 243, 617 S.E.2d 790 (2005).

First, the certified questions, as drafted, ask this Court to decide not only the sufficiency of "at the well" and similar royalty language, but also to decide the propriety of taking deductions for post-production expenses on lease provisions for which CNR never asked for summary judgment. Under W. Va. Code § 58-5-2 (1996), questions may be certified only for questions arising from the following:

1. the sufficiency of a summons or return of service;
2. a challenge of the sufficiency of a pleading or the venue of the circuit court;
3. *the sufficiency of a motion for summary judgment where such motion is denied*;
4. a motion for judgment on the pleadings;
5. the jurisdiction of the circuit court of a person or subject matter; or
6. failure to join an indispensable party.

(emphasis added).

Here, the Circuit Court bases its grounds for certification upon the third permissible action giving rise to a certified question – the sufficiency of a motion for summary judgment where such motion is *denied*. Confusion has apparently resulted from the fact that the Court was considering at the same time both CNR's motion for summary judgment regarding the

sufficiency of “at the well” and similar royalty language and the Plaintiffs’ motion for summary judgment, which covered all leases, not just those containing “at the well,” “at the wellhead,” “beyond the well,” and similar language. (See CNR’s Memorandum In Support Of Motion For Partial Summary Judgment Regarding Deductibility Of Post-Production Expenses, CNR’s Designation Of Record, Exhibit 1.) Both questions certified by the trial court incorporate Exhibit A (See Plaintiffs’ Designation of Record, Exhibit 1), which outlines what the Plaintiffs assert is all lease language contained in gas leases between the Plaintiffs and CNR. In fact, Exhibit A was prepared by the Plaintiffs in support of *their* motion for summary judgment, not in connection with CNR’s motion for partial summary judgment – the motion that was denied.

Exhibit A includes lease provisions not addressed by CNR in its motion for summary judgment. For example, Exhibit A includes “based upon the usual price,” “gas produced and sold” and other language not made part of CNR’s motion. By incorporating Plaintiffs’ Exhibit, the lower court inadvertently certified questions involving leases where deductions are not at issue! For example, in a separate motion, CNR moved for summary judgment on flat-rate leases, under which royalty holders are entitled to a fixed royalty rather than one based on the volume of gas produced. The Circuit Court has not ruled on that motion. Flat-rate leases from which deductions are not taken are, nevertheless, included as lease type W of Exhibit A. Because certified questions must arise from the Circuit Court’s denial of CNR’s motion for partial summary judgment, the inclusion of such lease provisions is clearly improper.

Quite simply, the certified questions as presented cover more than is permissible on certification, which is properly limited to the issues raised in CNR’s denied motion. The questions, therefore, must be reformulated to address only those lease types covered in CNR’s motion for summary judgment and the lower court’s decision denying that motion.

The lower court also assumed that this Court would adopt the holding of Rogers v. Westerman Farm Co., 29 P.3d 887 (Colo. 2001), that “at the well” and similar royalty language is *silent* as to the allocation of post-production expenses. Based on this assumption, the Circuit Court certified questions that assume that “at the well” and similar language does not expressly provide that post-production expense shall be deducted, a conclusion, CNR respectfully suggests, that is inconsistent with West Virginia law. As the questions are currently drafted, however, both specifically state that this Court must first agree that “at the well” and similar language is silent in stating that deductions can be taken. But the question of whether “at the well” and similar royalty language expresses an intent to allocate post-production costs between the gas lessor and gas lessee is precisely what the lower court stated at the September 19, 2005, hearing was to be certified to this Court.

Given the fact that there is no precedent in the state, the Court is going to order that the questions be certified. I’m going to direct that the lawyers get together and certify it and I’m asking that the trial Court’s answer to the question is does this sufficiently allocate between the lessor and the lessee. Does this language sufficiently allocate post-production costs and the trial court’s answer is no, the result of which, if the trial court is correct, these post-production expenses are not deductible.

See, Hearing Transcript at 100:18-24 and 101:1-3.

This is not the only discrepancy between the Circuit Court’s September 19, 2005, holdings and the Order containing certified questions and their answers entered on October 18, 2005. At the hearing on the parties’ motions for summary judgment, the lower court specifically held not that “at the well” and similar language was *silent*, but that such language was *ambiguous* with regard to whether the parties intended that post-production costs should be shared by the parties to the leases. At the hearing, the lower court stated:

There are ambiguities. Some of those ambiguities have been pointed out here. If, in fact, the drafter of the lease expected the lessor to pay for transportation,

gathering, dehydration, stripping of the constituents, then certainly the lessee could have put that into the lease so that the average person reading this lease would have an understanding of exactly what the rights and obligations of the parties are and the judgment of the court just doesn't do it and I'm persuaded that the rules established by the case of Rogers v. Westerman Farm Company, 29 P.3d 887 is well reasoned and consistent with the implied covenant to market that's placed upon the lessee and consistent with the rule requiring construction of ambiguous lease provisions most strongly against the lessee who prepares the lease.

See, Hearing Transcript at 100:3-17. However, in answer to the certified questions, the trial court stated in its Order that “ ‘at the well,’ ‘gross proceeds,’ ‘market price,’ ‘proceeds from sale,’ ‘proceeds received,’ or ‘net of all costs’ and other such language above is *silent* as to the right of the lessee to deduct post-production expenses.” Such discrepancies in the lower court's rationale shows that the questions, as drafted, do not adequately permit this Court to consider all relevant law regarding the issues submitted to it. Therefore, CNR proposes that this Court reformulate the certified questions as follows:

Question 1: Is an oil and gas lease that contains language providing for the payment of royalty “at the well” or “at the wellhead” or “net of all costs beyond the wellhead” clear and unambiguous in that it allows for the deduction of post-production expenses?

Question 2: Even if such language is ambiguous, is it proper for the trial court – relying solely on the implied covenant to market and the general rule of construction that ambiguities in an oil and gas lease are to be resolved against the lessee – to preclude the lessee from deducting a lessor's proportionate share of post-production expenses from the lessor's royalty as a matter of law, thereby denying the lessee its right to have the fact finder determine the intent of the parties?

As both of the certified questions drafted by the lower court assume – contrary to fact and to the lower court's actual ruling – that “at the well” and similar language is *silent* as to the

allocation of post-production costs, CNR will incorporate its arguments regarding the lower court's certified questions into its discussion of the questions as reformulated.

V. SUMMARY OF ARGUMENT

This Court should find that deductions from oil and gas royalties are provided for in an oil and gas lease where "at the well," "at the wellhead," "at the mouth of the well" and similar royalty language is used.

West Virginia has long held that implied covenants such as the implied covenant to market are not applicable where a contract contains express language addressing the subject matter. The Wellman opinion illustrates this Court's adherence to this fundamental principle of law. Wellman indicates that West Virginia is not in full agreement with the courts of Colorado, Arkansas, and Oklahoma on the applicability of the implied covenant to market. Rather, Syllabus Point 5 of Wellman shows that where royalty language such as "at the well" is used, deductions from royalty payments may be made so long as such deductions are actual and reasonable. Moreover, this Court specifically stated in Wellman that "at the mouth of the well" language "might be language indicating that the parties intended that the Wellmans, as lessors, would bear part of the costs of transporting gas from the wellhead to the point of sale." Wellman v. Energy Resources, Inc., 210 W. Va. 200, 211, 557 S.E.2d 254, 265 (2001).

"At the wellhead" and similar royalty language becomes meaningless where deductions for post-production expenses are not permitted. In fact, the effect of prohibiting deductions for post-production expenses where an "at the wellhead" royalty clause is used is to give such language a meaning contrary to the meaning that it has historically been given throughout the country. It is downstream of the wellhead that post-production expenses are incurred; therefore, the clear and express meaning of language calling for royalties to be calculated "at the wellhead"

unmistakably directs that royalty holders are not to receive the benefit of post-production activities without sharing in the costs incurred beyond the wellhead.

This Court has previously acknowledged that the wellhead price is something different than the price received at the point of sale. Cotiga Dev. Co. v. United Fuel Gas Co., 147 W. Va. 484, 128 S.E.2d 626 (1962). Then, in Wellman, this Court noted that “at the mouth of the well” language might be language providing for the deduction of post-production expenses, and adopted Syllabus Point 5, directing that deductions are permissible where expressly provided for. The West Virginia Supreme Court’s holding in Wellman acknowledging the significance of “at the well” language is not without support. Courts in Texas, Louisiana, and California, to name a few, agree that royalty holders should bear a proportionate share of post-production expenses if the lease contains “at the well” or similar royalty language. See, Heritage Resources, Inc. v. Nations Bank, 939 S.W.2d 118, 121-23 (Tex. 1996) (holding that post-production expenses were deductible where the lower court had “disregarded the generally accepted meanings of ‘market value at the well’ and ‘royalty’ to determine that [lessee] wrongfully deducted post-production costs.”); Merritt v. Southwestern Elec. Power Co., 499 So. 2d 210, 213 (La. App. 2 Cir. 1986) (holding that “at the well” language “provides for a proportionate deduction of costs of gathering and delivering the gas to a pipeline system.”); Babin v. First Energy Corp., 693 So. 2d 813, 815 (La. App. 1 Cir. 1997) (stating that where “at the well” language is used, “the general rule is that a royalty owner is liable for a proportionate share of the costs incurred subsequent to production.”); Atlantic Richfield Co. v. State, 262 Cal. Rptr. 683, 688 (Cal. App. 2 Dist. 1989) (stating that “at the well” language means that “the lessor of an oil and gas lease...bears its proportionate share of processing costs incurred downstream of the well.”).

Moreover, the view adopted by the lower court represents an extreme minority view that was not considered by the Wellman Court. The argument that “at the well” and similar language is silent with respect to post-production expenses is based on the much-criticized opinion of the Colorado Supreme Court in Rogers v. Westerman Farm Co., 29 P.3d 887 (Colo. 2001). That opinion, in turn, was largely based upon the theories purportedly advanced by an expert in the area of oil and gas law, Professor Owen Anderson. In fact, after the Rogers opinion was issued, Professor Anderson quickly asked the court to modify its opinion because the court’s reasoning was directly contradictory to his theories. Owen L. Anderson, 2001: A Royalty Odyssey, Institute for Energy Law, 53rd Annual Institute (February 21, 2002).

Finally, even if “at the well” language is found to be ambiguous, the rules of interpretation and construction do not demand that courts automatically construe lease language against the lessee. Rather, the rules of interpretation require first that the intent of the parties be determined by a fact finder. The rule of law applied by the Circuit Court would require this Court to deny gas producers the right to have their evidence heard by a finder-of-fact before an interpretation tool of last resort is used. Furthermore, in this case, the rule should not apply at all because the individuals and businesses chosen to represent the Plaintiff class were not parties forced to sign form contracts without the advice of attorneys, but actually consulted counsel and made revisions to the leases.

Because “at the well” and similar royalty language is clear and unambiguous that deductions for post-production expenses are to be made, this Court should answer the certified questions in a manner that acknowledges the significance of such language. However, even if this Court believes that “at the well” and similar language is not clear and unambiguous, it should still answer the certified questions as suggested by CNR because West Virginia and a

majority of states have long recognized the significance of “at the well” and similar language⁶ and because defendant lessee must be afforded the opportunity to have the intent of the subject leases determined by a finder-of-fact.

VI. ARGUMENT

A. ISSUES NOT CERTIFIED TO THIS COURT MUST NOT BE DECIDED.

In their Brief in Support of Affirming Trial Court’s Rulings on Certified Questions, the Plaintiffs address several issues not certified to this Court for review. Such issues should not be decided by this Court on certification.

This Court has long held that it will not consider issues not having some bearing on certified questions when reviewing certified questions. Baier v. City of St. Albans, 128 W. Va. 630, 637, 39 S.E.2d 145, 150 (1946) (stating that the Supreme Court “confines itself to answering the specific questions certified”). The Plaintiffs nevertheless raise several issues not certified to this Court for review, including issues regarding the manner of calculating royalty deductions, what types of deductions are proper, an alleged non-disclosure of deductions from royalties, and the requirement that deductions must be actual and reasonable to be permissible.

Typical of the issues discussed by the Plaintiffs in their Brief on the certified questions is their discussion of CNR’s alleged deductions for line loss. An examination of this issue quickly

⁶ Failure to apply the clear meaning of the “at the wellhead” language would provide an obvious windfall to Plaintiffs to the detriment of CNR. The lease language permits the royalty owner to receive only 1/8 of the price received at the well or at the wellhead. Where gas is not sold at the wellhead, a determination of the wellhead price is necessary. For example, let us assume that the actual sale price of a quantity of gas at the downstream point of sale is \$100.00. If we further assume that the lessee was required to spend \$20.00 in post-production expenses to get the gas to the point of sale, then, working back from the point of sale, the price at the wellhead was \$80.00. Applying a 1/8 royalty to the price at the wellhead, the royalty owner would receive \$10.00. If, on the other hand, the 1/8 royalty is applied to the price at the point of sale, the royalty owner would receive \$12.50, all as a result of costs incurred by the lessee and with no commensurate benefit to the lessee.

reveals that it is not a topic properly before this Court in connection with the questions that have been certified. "Line loss" is a phrase used to describe an amount of gas lost between the wellhead and the point of sale due to leakage or differences in pressure throughout the pipeline system. Gas lost through line loss is not sold by producers such as CNR, and producers are not compensated for gas not sold because of line loss. Line loss does not involve a monetary deduction from the sales price of the gas, and it has no bearing on the physical condition of the gas. For these reasons, the Plaintiffs' arguments regarding post-production expenses and the marketable condition rule do not apply to line loss. Moreover, the lower court was not asked in CNR's motion for summary judgment to consider the issue of line loss. Accordingly, it is not an issue properly considered by this Court in determining certified questions regarding the significance of "at the well" and similar royalty language.

Line loss and the other issues discussed above have no bearing upon the Supreme Court's consideration of the certified questions before it, whether this Court accepts CNR's requested reformulation or the questions as certified by the lower court. The certified questions relate only to the permissibility of taking monetary deductions from royalty payments where "at the wellhead" and similar language is used in an oil and gas lease. Because issues raised by the Plaintiffs that were not raised in the certified questions have no bearing on the certified questions, case law directs that this Court should not address them.

B. "AT THE WELL," "AT THE WELLHEAD," "BEYOND THE WELL," AND OTHER SIMILAR ROYALTY LANGUAGE IS CLEAR AND UNAMBIGUOUS AND PROVIDES THAT POST-PRODUCTION COSTS MAY BE DEDUCTED.

The Supreme Court of Appeals should answer the reformulated certified questions in favor of CNR because "at the well" and similar royalty language is clear and unambiguous that deductions may be taken from royalties. Despite the Plaintiffs' argument to the contrary,

implied covenants such as the implied covenant to market only apply where a contract contains no express language governing the subject. "At the well" and similar royalty provisions are clear and unambiguous, thereby precluding application of the implied covenant to market. Moreover, as specifically recognized by the lower court, the Rogers opinion represents an extreme minority view regarding the deductibility of post-production expenses. This extreme minority view should not be adopted as the law of West Virginia.

1. Implied Covenants Operate Only Where Language To The Contrary Is Not Found In The Express Language Of A Contract.

The Plaintiffs contend that the implied covenant to market, which was recognized by this Court in Wellman v. Energy Resources, Inc., 210 W. Va. 200, 557 S.E.2d 254 (2001), operates in all leases, regardless of whether the lease contains express language addressing the lessee's obligation to market gas. An examination of West Virginia law shows that this is not true.

Under West Virginia law, a covenant will be implied in a contract only where the contract contains no express provision with regard to the subject matter of the implied covenant. Berry v. Humphreys, 76 W. Va. 668, 669, 86 S.E. 568, 569 (1915). See, also, Croston v. Emax Oil Co., 195 W. Va. 86, 464 S.E.2d 728 (1995) (stating that the implied duty of lessee to protect lessor's property against substantial drainage only applies where there is no express provision in the lease dealing with drainage); Thompson Dev., Inc. v. Kroger Co., 186 W. Va. 482, 413 S.E.2d 137 (1991) (stating that implied covenant of continuous operation must not be inconsistent with the express terms of the contract); De Stubner v. Microid Process, 124 W. Va. 591, 21 S.E.2d 154 (1942) (holding that an implied duty to exploit should be applied where there is no express contract provision to the contrary). This general rule has been applied by this Court to cases involving the implied covenant of marketability as well, as seen in the discussion of Wellman below.

It is a basic tenet of contract construction that each and every word is to be given meaning, and that the court cannot create or impose an implied covenant or construction that is inconsistent with the express terms of the contract. Barn-Chestnut, Inc. v. CFM Dev. Corp., 193 W. Va. 565, 572, 457 S.E.2d 502, 509 (1995), citing Bonanza Int'l, Inc., v. Restaurant Management Consultants, 625 F. Supp. 1431, 1448 (E.D. La. 1986) (“*where the express intention of contracting parties is clear, a contrary intent will not be created by implication.*” The implied covenant of good faith and fair dealing cannot give contracting parties rights which are inconsistent with those set out in the contract” (emphasis added)). Moreover, the Supreme Court of Appeals has recently acknowledged that “specific words or clauses of an agreement are not to be treated as meaningless, or to be discarded, if any reasonable meaning can be given them consistent with the whole contract.” Dunbar Fraternal Order of Police, Lodge #119 v. City of Dunbar, 624 S.E.2d 586, 591 (W. Va. 2005) (citation omitted).

In Wellman, the trial court had ruled in favor of the lessor on a summary judgment motion that was essentially unopposed because the defendant failed to produce any evidence in the record to justify or explain the deductions that had been taken. Wellman, 210 W. Va. at 204, 557 S.E.2d at 258. The Wellman Court noted that the deductions represented an extremely high percentage of the actual sale price of the gas without justification or explanation. Id. With this factual background, this Court reached certain general conclusions that relate to the issue of the deductibility of costs incurred downstream of the wellhead when the lease is silent or does not otherwise specify whether post-production expenses can be deducted. Id. at 210, 265. In doing so, this Court recognized the long-standing rule that implied covenants will not have force where express language to the contrary exists.

Syllabus Pt. 5 of Wellman provides that:

If an oil and gas lease provides that the lessor shall bear some part of the costs incurred between the wellhead and the point of sale, the lessee shall be entitled to credit for those costs to the extent that they were actually incurred and they were reasonable. Before being entitled to such credit, however, the lessee must prove, by evidence of the type normally developed in legal proceedings requiring an accounting, that he, the lessee, actually incurred such costs and they were reasonable.

The Wellman Court even went a step further – it recognized that “language ... indicating that the ‘proceeds’ shall be from the ‘sale of gas as such at the mouth of the well where gas is ... found” might be language indicating that the Wellmans, as lessors, would bear part of the costs of transporting the gas from the wellhead to the point of sale.” Wellman, 210 W. Va. at 211, 557 S.E.2d at 265. Thus, this Court recognized that “at the well” and similar language is likely sufficient to prevent operation of the implied covenant to market. In accordance with the limitations attached to the implied covenant of marketability, this Court acknowledged that where an oil and gas lease expressly provides for the allocation of post-production expenses between the lessor and the operator, the implied covenant of marketability cannot be invoked. As such, because “at the well,” “at the wellhead,” and other similar language sufficiently expresses the intent of the parties that post-production costs shall be shared, the implied covenant of marketability does not apply.

2. “At The Well” And Similar Language Must Be Given Meaning.

Because “at the well” and “net of all costs beyond the wellhead” language clearly and unambiguously indicates that post-production costs shall be shared, the lower court’s determination that such language is ambiguous must not stand. Generally, where contract terms are clear and unambiguous, they must be applied by the court and not construed. Syl. pt. 3, Waddy v. Riggleman, 216 W. Va. 250, 606 S.E.2d 222 (2004); Syl. pt. 2, Orteza v. Monongalia County General Hosp., 173 W. Va. 461, 318 S.E.2d 40 (1984); Syl. pt. 2, Bethlehem Mines

Corp. v. Haden, 153 W. Va. 721, 172 S.E.2d 126 (1969). Terms of oil and gas leases are no exception to this rule. This Court has held that “an oil and gas lease which [sic] is clear in its provisions and free from ambiguity, either latent or patent, should be considered on the basis of its express provisions and it is not subject to a practical construction by the parties.” Cotiga Dev. Co. v. United Fuel Gas Co., 147 W. Va. 484, 128 S.E.2d 626 (1962). In fact, “it is not the right or province of the court to alter, pervert or destroy the clear meaning and intent of parties as plainly expressed in their written contract or to make a new and different contract for them.” Id.

The significance of the meaning of “at the well” language becomes clear when looking at the effect of prohibiting deductions from post-production expenses. If royalty holders were to be relieved of their obligation to pay their proportionate share of post-production expenses, “at the well,” “at the wellhead,” and “at the mouth of the well” language not only becomes meaningless, it becomes blatantly contrary to the expressed intent of the parties. Rather than entitling royalty owners to 1/8 of the proceeds “at the well,” royalty holders would be entitled to 1/8 of proceeds “at the point of sale,” after the value of the gas has been enhanced as a result of post-production expenses. This is inarguably inconsistent with the clear and unambiguous term calling for royalties to be determined “at the wellhead.” It is “at the wellhead” that gas comes to the surface. It is not until after gas leaves the wellhead that expenses such as gathering, transportation, and processing are incurred. These expenses incurred downstream of the wellhead increase the quality of gas and the proceeds received from the sale thereof. It necessarily follows then that where a lease states that royalties are to be determined “at the wellhead,” the lease directs that the lessor is entitled to something less than a percentage share of total profit received from the sale of gas. The lessor is entitled to a royalty from which

deductions have been taken for his or her proportionate share of costs that increased the value of the gas downstream of the wellhead.

This conclusion is reinforced by consideration of “at the well” and similar language together with additional express marketing language such as the language contained in many of the subject leases. A number of the leases at issue contain an additional clause stating that “the time and method of marketing...shall be within the sole discretion of the lessee.” When reading such language together with “at the well” and similar royalty language, there can be no question that CNR is entitled to deduct post-production expenses.

3. Case Law Confirms That “At The Well” And Similar Language Provides For The Allocation Of Post-Production Expenses.

This Court has already recognized the clear meaning of “at the well” language on more than one occasion. As noted above, this Court in Wellman acknowledged that the language “at the mouth of the well” had meaning. Specifically, the Wellman Court stated, “this Court believes that the language of the leases in the present case indicating that the ‘proceeds’ shall be from the ‘sale of gas as such at the mouth of the well where gas ... is found’ might be language indicating that the parties intended that the Wellmans, as lessors, would bear part of the costs of transportation of the gas from the wellhead to the point of sale.” Wellman, 210 W. Va. at 211, 557 S.E.2d at 265. While the Plaintiffs argue that these statements of the Wellman Court are unpersuasive dicta, it is clear that the above-quoted language was included in the Wellman Court’s opinion for the purpose of explaining and giving meaning to its holding in Syllabus Point 5 in which this Court states that the allocation of post-production expenses will be permitted where expressly provided for in a lease.

The Wellman Court’s understanding of the meaning of “at the well” no doubt was influenced by this Court’s earlier decisions. For example, this Court recognized long before

Wellman that the “wellhead price” is something less than the price received where gas is delivered and sold. For example, the Supreme Court of Appeals held in Cotiga Dev. Co. that a lessee must pay the amount it received for the gas when and where delivered and “not just the wellhead price” where the lease provides for a royalty based on the rate received by the lessee for such gas. The Court recognized that “the wellhead price” was something different from the price received at the point of sale, stating that “the amount of the damages to which Cotiga is entitled, if any, ... depends upon a determination whether such damages are computed on the wellhead price or the price received by United Fuel for such gas when marketed by it.” Cotiga Dev. Co., 147 W. Va. at 494, 128 S.E.2d at 633.

Other courts agree. For instance, a New Mexico court held that an “at the well” royalty clause was “unambiguous and means that Plaintiffs are entitled to royalties based on the value of the carbon dioxide gas as it emerges at the wellhead.” Creson v. Amoco Production Co., 129 N.M. 529, 533, 10 P.3d 853, 857 (2000). A Michigan court reached the same conclusion, finding that the term “gross proceeds at the wellhead” clearly contemplates deductions for post-production expenses. Schroeder v. Terra Energy, Ltd., 223 Mich. App. 176, 565 N.W.2d 887 (Mich. App. 1997). The Michigan court noted that it would permit deductions where “at the wellhead” language is used because it “prefer[s] a reasonable and fair construction over a less just and less reasonable construction” that ignores “at the wellhead” language altogether. Id. at 188, 894. A Texas court recently acknowledged its existing case law on the subject, stating “we note once again that ‘at the well’ means before value is added by preparing the gas for market.” Cartwright v. Cologne Production Co., 2006 WL 22681, 3 (Tex. App. 2006).

Because the plain meaning of the language “at the well,” West Virginia law, and the law of other jurisdictions show that “at the well” and similar royalty language clearly and

unambiguously calls for the allocation of post-production expenses between the gas lessor and lessee, and because where the express language of a gas lease calls for such deductions, implied covenants do not operate, CNR requests that this Court answer its first reformulated question “yes.” In the alternative, CNR asserts that the arguments set forth above offer ample proof that deductions for post-production expenses are permissible where “at the well” and similar language is used because such language is clear and unambiguous; therefore, this Court should answer both certified questions, as presented by the lower court, in the affirmative.

4. Colorado’s Holding In Rogers Expresses An Extreme Minority View With Regard To The Deductibility Of Post-Production Expenses That Should Not Be Adopted By This Court.

Despite the Plaintiffs’ argument that Rogers should be adopted by this Court, thereby rendering “at the well” and similar language meaningless with regard to the allocation of post-production expenses, the weight of scholarly authority shows that the Rogers Court took an extreme position that should not be followed by other courts.

In a number of cases that have discussed the issue of deductibility of post-production expenses, the outcome has been dependent on whether or not the court believed the lease was silent as to the allocation of post-production expenses. The recent trend has been that where the lease is silent, the lessee bears the costs to move the gas to market. Many of these cases have been summarized and analyzed in scholarly articles that have recognized the relevant issue to be at what point should the market value or proceeds from the sale be determined for purposes of calculating royalty. See, David E. Pierce, Recent Developments in Non-Regulatory Oil and Gas Law: Unfinished Business, Institute for Energy Law, 53rd Annual Institute (February 21, 2002) (hereinafter cited as “Pierce”), Owen L. Anderson, 2001: A Royalty Odyssey, Institute for Energy Law, 53rd Annual Institute (February 21, 2002) (hereinafter cited as “Anderson”), Scott

Lansdown, The Marketable Condition Rule, 44 S. Tex. L. Rev. 667, 671 (hereinafter cited as "Lansdown," see page 3 thereof), David E. Pierce, Royalty Calculation in a Restructured Gas Market, 13 Eastern Min. L. Inst. ch. 18, 18-34 through 18-36 (1992). These scholarly articles point out that certain jurisdictions, such as Colorado, that have adopted a rule disallowing the deduction of post-production expenses, engage in legal fictions to reach their holdings, are unconvincing, or are just plain wrong and irrational.

Professor David E. Pierce has written extensively on this issue in various articles. His writings explain that the trend is for courts to find that post-production expenses are not deductible when the lease is *silent* as to deductibility, but that the use of an implied covenant to attempt to override the express language of a lease is misguided. Cases from Colorado, Kansas and Oklahoma have held, based on variations of an implied covenant theory, that the lessee should – *in certain circumstances* – bear the cost of certain post-production expenses.

In Rogers, a case not considered by this Court in Wellman, the Colorado court dealt with a series of proceeds and market value leases that all provided royalties were to be computed "at the well" or "at the mouth of the well." Despite this language, the Colorado court somehow concluded that the leases were silent with respect to the allocation of costs and decided that it must look to the implied covenant to market to determine whether or not post-production expenses were deductible. The Rogers Court's conclusion that the leases were silent as to where royalties were to be calculated has been soundly criticized. See, Pierce, Anderson, Lansdown, *supra*. Notably, the Rogers Court stated in a footnote that it was making its ruling in part based upon a theory espoused by and advocated by Professor Anderson. Professor Anderson, however, did not agree with the ruling and thereafter wrote to the Rogers Court asking it to modify its footnote suggesting that he recognized the lessee's possible duty to move gas to a marketable

location, as that was the opposite of what he had actually said! See, Anderson, at 16. The Court subsequently modified the footnote, but declined to modify its opinion to limit the holding to local gathering expenses. It is this misguided view that the lower court adopted in denying CNR's motion for summary judgment and in granting summary judgment in favor of the Plaintiffs.

The lower court acknowledged that the rules pronounced in Rogers are the minority view and that this minority view has been the subject of much criticism. At the September 19, 2005, hearing, the lower court asked Plaintiffs' counsel:

What about the fact that this view that you're advocating, the Plaintiffs are advocating, is recognized to be the minority view in the nation and it's been around and criticized roundly?

See, Hearing Transcript at 96:5-8. In fact, not only does the Rogers opinion go well beyond this Court's earlier holding in Wellman, such an opinion has not been, to date, accepted by any appellate court outside of Colorado. In light of the poor reasoning underlying the Rogers holding – as recognized in the criticisms of many scholars – this Court should refuse to adopt Rogers as the law of West Virginia.

5. West Virginia Has Not Adopted the Marketable Condition And/Or Location Rule.

The Plaintiffs contend that this Court should apply the “marketable condition and location rule,” which provides that the implied duty to market is dependent on the point at which the gas is sold regardless of the distance from the wellhead. It is clear, however, that Wellman failed to adopt the marketable condition and location rule even after the Wellman Court's obvious review of the cases citing such a rule.

While this Court noted in the Wellman opinion that it found the Colorado (pre-Rogers), Kansas and Oklahoma line of authorities persuasive, the Court nevertheless included as Syllabus

Point 5, and in its analysis in the opinion, a statement establishing that it was not in complete agreement with the authorities from Colorado, Kansas and Oklahoma, and which certainly is not in accord with Rogers. This Court has ruled that lease language providing for the calculation of royalties at the “mouth of the well,” is language that might authorize the deduction of post-production expenses, provided that the lessee proves as if in an action for an accounting that the costs were actual and reasonable. Wellman, 210 W. Va. at 211, 557 S.E.2d at 265. Thus, this Court has rejected the Rogers “legal fiction” that an “at the wellhead” lease is silent as to allocation of post-production expenses. The Court merely shifted the burden to the defendant in cases where the defendant relies on at-the-wellhead language, to prove, as if in an action for an accounting (an equitable cause of action), that the post-production expenses were actual and reasonable. An analysis of the cases cited in Wellman confirms this conclusion.

The Colorado (pre-Rogers), Kansas and Oklahoma cases cited in Wellman held that an implied covenant to market imposes on the lessee all costs of production up to the point at which the gas is placed in a “marketable condition.” Pierce, Anderson. This is a question of fact related to the physical condition of the gas. Id. If the gas is in such physical condition at the wellhead that it can be sold, then the lessor bears a proportionate part of any expense to move the gas from the wellhead and otherwise compress it, or put it into interstate commerce downstream of the wellhead. Id.

Wellman cites the Colorado case of Garman v. Conoco, Inc., 886 P.2d 652 (Colo. 1994), which involved a certified question regarding whether an overriding royalty owner should bear any part of post-production expenses. The royalty clause in question was not quoted by the court, which held it was the lessee’s obligation to get the gas into a marketable condition. The court indicated that its ruling was “limited to those post-production expenses required to

transform raw gas into marketable product.” Garman, 886 P.2d at 660. The Garman rationale was radically altered in Rogers into what has been called by Professors Pierce and Anderson a “marketable location” rule. According to Rogers, the implied duty to market is dependent on the point at which the gas is sold, regardless of the distance from the wellhead. Professors Pierce, Anderson and Lansdown, among others, have criticized the holding in Rogers as completely contrary to law and fact. The main error they see in Rogers is that it adopted a “legal fiction,” that the lease was silent as to the location at which royalties would be calculated. See, Anderson, at 13, 22. See also, Pierce, at 25-26, noting that an implied covenant at law such as the one created in Rogers is a “legal fiction.”

Wellman also cited the Oklahoma case of Wood v. TXO Production Corp., 854 P.2d 880 (Okla. 1992). The issue presented in Wood was whether the lessor should bear a share of the costs for compression facilities that were *on the leased premises*. The court held that the lessee was responsible for all production costs, which included the costs of compression on the lease to put the gas in a marketable condition. The Wellman opinion, however, did not cite the subsequent Oklahoma case of Mittelstaedt v. Santa Fe Minerals, Inc., 954 P.2d 1203 (Okla. 1998), which affirmed the marketable condition rule, but noted that in the earlier case of Johnson v. Jernigan, 475 P.2d 396, 398 (Okla. 1970), it had allowed the deduction of transportation costs because “there was no market available for the gas at the lease.” Mittlestaedt, 954 P.2d at 1205. The Mittelstaedt Court also noted that once a marketable product was obtained at the well, royalty owners should be charged with any costs incurred thereafter if the lessee could demonstrate that the costs enhanced the value, were reasonable, and actual revenues increased in proportion with the costs assessed. Id. This is similar to the holding in Wellman. So long as the lessee can prove that costs incurred to gather and process and get the gas to a downstream market

location were actual and reasonable, the lessor bears a proportionate share of those costs as they are not “production” costs.

Finally, the Plaintiffs cite the case of Gilmore v. Superior Oil Co., 388 P.2d 602 (Kan. 1964), in support of the notion that the marketable condition rule has been adopted by this Court. However, Wellman did not address Gilmore in the context of adopting the marketable condition rule, but generally as a case recognizing the implied covenant of marketability which applies where no contract language addressing the subject matter can be found. As noted above, language to the contrary can be found in the leases involved in this case. Significantly, Gilmore dealt with whether the costs associated with compressor facilities *on the lease* could be deducted when calculating royalties. In Gilmore, however, the Kansas court held that because the facilities were on the lease, and it considered the “at the well” language as precluding allocation to the lessor of any costs incurred on the lease, *i.e.*, the deductions were not proper. Gilmore, 388 P.2d at 606. The more recent Kansas case of Sternberger v. Marathon Oil Co., 894 P.2d 788 (Kan. 1995), recognized the marketable condition rule, but went on to find that “there is no evidence in this case that the gas produced...was not marketable at the mouth of the well other than the lack of a purchaser at that location.” *Id.* at 799. The court, therefore, held that the deductions for expenses downstream of the wellhead *were proper*. This is the same situation faced by CNR. The gas is marketable at the well, but there is no longer a viable market at the wellhead due to the restructuring of the gas industry by the Federal Energy Regulatory Commission in the 1990s.⁷

Thus, despite stating that it found the Colorado (pre-Rogers), Oklahoma and Kansas line of authorities persuasive, this Court (a) did not discuss or recognize that additional and contrary

⁷ Gas does need to have NGLs removed to be transported on interstate pipelines; however, the removal of NGLs is not necessary for access to gathering systems.

authority in Oklahoma and Kansas supports the deductibility of post-production expenses in circumstances such as those relevant to CNR, and, more importantly, (b) expressly decided that language indicating that royalties were to be calculated at the mouth of the well could be language indicating that the lessee was entitled to deduct post-production expenses, provided that it could prove, as if in an action for an accounting, that the costs were actual and reasonable. See, Syl. pt. 5, Wellman, 210 W. Va. 200, 557 S.E.2d 254 (2001). It should also be noted that the reference to Colorado authority was pre-Rogers, and, accordingly, Wellman never endorsed the “marketable location” rule.

The holding in Wellman recognizing that post-production expenses may be deductible is expressly inconsistent with the “marketable location” rule. It is clear that Wellman does not ignore the express terms of the lease and where “at the wellhead” or similar language is present, the royalty owner bears a proportionate share of post-production expenses if shown to be actual and reasonable. For this reason, this Court should reject the Rogers holding and find that “at the well” language is not silent with regard to the deduction of post-production expenses, but expressly provides that such deductions are permissible.

Even if this Court determines that “at the well” and similar royalty language is not clear and unambiguous, the reasoning in Wellman shows that the Rogers rule advocated by the Plaintiffs is an extreme view that should not be adopted. Based upon such reasoning, this Court should answer the second certified question, as reformulated, in the negative. In the alternative, because Rogers is an extreme view soundly criticized by legal scholars and not considered by this Court in Wellman, this Court should answer both certified questions, as formulated by the trial court, in the affirmative.

C. "GROSS PROCEEDS," "MARKET PRICE," AND "NET OF COSTS" LANGUAGE PERMITS THE DEDUCTION OF POST-PRODUCTION COSTS WHEN READ WITH "AT THE WELL" LANGUAGE.

Relying on the Rogers case, the Plaintiffs claim that "gross proceeds," "market price," and "net of costs" language is insufficient to call for the allocation of post-production expenses. The Plaintiffs' argument is unconvincing when considering general principles of contract law. West Virginia holds fast to the canon of construction that individual terms in a contract provision are not to be interpreted separately, but are to be read together with all other words in that contract provision so that all words are given meaning. See, e.g., Moore v. Johnson Serv. Co., 158 W. Va. 808, 814, 219 S.E.2d 315, 320 (1975), Chambers v. Simmons, 76 W. Va. 174, 179, 85 S.E. 182, 184 (1915). The discussion cited by the Plaintiffs from Rogers describes the lease language noted above in isolation from the remainder of the language in the Plaintiffs' royalty provisions; therefore, those words have not been given their proper meaning in light of the language that is conveyed in the royalty clauses as a whole.

The leases at issue in CNR's motion for summary judgment below vary slightly in their provisions, but such leases provide for royalty calculations to be made "at the well," "at the mouth of the well," or "beyond the wellhead."⁸ As argued above, the Plaintiffs do not contest that it is "at the well" that gas produced from the Plaintiffs' leaseholds comes to the surface. Likewise, the Plaintiffs do not contest that after gas leaves the wellhead expenses such as gathering, transportation, and processing are incurred. Because these expenses incurred after gas leaves the wellhead increase the quality and, thereby, the price received from the sale of gas, it is

⁸ For example, the royalty provision contained in Garrison Tawney's 1989 Oil & Gas Lease provides "To pay Lessor an amount equal to one-eighth of the price, **net of all costs beyond the wellhead.**" Kanawha & Hocking Coal & Coke's 1963 lease provides that the lessor will receive a royalty to be determined by the "wholesale market value of the gas **at the well.**"

evident that where parties enter into leases specifically providing that royalties are to be determined “at the well,” the lease clearly and explicitly expresses the parties’ intent that the royalty holder is entitled to something less than a share of the total proceeds received from the sale of gas.

As noted above, this Court has held that “an oil and gas lease which [sic] is clear in its provisions and free from ambiguity, either latent or patent, should be considered on the basis of its express provisions and it is not subject to a practical construction by the parties,” Cotiga Dev. Co., 147 W. Va. at 494, 128 S.E.2d at 694, and that a court has no right to “alter, pervert, or destroy the clear meaning and intent of parties as plainly expressed in their written contract or to make a new and different contract for them.” Id. However, even where contract language is interpreted, words are to be given their ordinary meaning. Bischoff v. Francesa, 143 W. Va. 474, 498, 56 S.E.2d 865, 878 (1949).

When language such as “gross proceeds” is added to the “at the well” language, it becomes apparent when reading all of the terms together that “gross proceeds at the well” clearly and unambiguously means that no deductions are to be taken from the royalty payment for production expenses; that is, expenses incurred to bring the gas to the surface of the earth. Still, for all expenses that are incurred beyond the wellhead – or post-production expenses – the operator is permitted to deduct the lessor’s proportionate share of such expenses. This is because while the term “gross proceeds” makes it clear that no deductions may be taken from the payment amount, when adding that language to the “at the wellhead” language, the words are taken in their proper context to mean that while no deductions are to be taken from the proceeds, such proceeds are to be determined “at the wellhead” rather than at the point of sale. Therefore, any expenses incurred beyond the wellhead must be borne by both the lessor and operator to give

the contract language its proper meaning. The Supreme Court of Oklahoma has recognized the significance of this language, stating that “gross proceeds” does indicate an amount without deduction from or charge against the royalty interest, but only when the point of sale occurs at the leased premises. However, where there is no market for the gas at the well, the operator may deduct post-production expenses shown to be actual and reasonable. Mittelstaedt, 1998 OK 7, 954 P.2d 1203 (1998).

Likewise, “market price” when teamed with the “at the wellhead” language has virtually the same effect. However, “market price” indicates that the Plaintiffs are entitled to the market value of the gas at the wellhead, not the market price at the point of sale. While the Plaintiffs argue that this language is silent as to situations in which there is no market at the well, it is clear that provisions of this kind have been used by gas operators for many years and are commonly understood to mean that the market price is simply to be calculated at the wellhead by subtracting the lessors’ proportionate share of expenses beyond the wellhead. Courts have commonly interpreted such language in a similar manner, holding that where there is no market for gas “at the well,” expenses incurred in getting the gas to market are reasonably deducted from a lessor’s royalty payment. See, e.g., Sternberger, 257 Kan. 315, 894 P.2d 788 (1995); Atlantic Richfield Co. v. State of California, 214 Cal. App. 3d 533 (1989).

Finally, “net price” language certainly expresses clearly and unambiguously that deductions for expenses are to be taken from royalty payments at the wellhead. “Net” has consistently been defined as a term indicating an amount remaining after sale and after deductions for expenses. See, e.g., Black’s Law Dictionary 1061 (Bryan A. Garner ed., 7th ed., West 1999) (stating that “net” means “an amount of money remaining after a sale, minus any deductions for expenses, commissions, and taxes”); American Heritage Dictionary of the English

Language 1181 (Joseph P. Pickett ed., 4th ed., Houghton Mifflin Company 2000) (stating that “net” means “[r]emaining after all deductions have been made, as for expenses: *net profit*”). Recognizing the plain meaning of this language, a Texas court has held that the language “net proceeds” in a lease provision providing for a royalty of “1/8 of the net proceeds at the well received from the sale thereof” makes it clear that post-production costs should be deducted from the sale price. Martin v. Glass, 571 F. Supp. 1406 (N.D. Tex. Ft. Worth 1983). Even one of the cases previously used by the Plaintiffs in support of their argument that such deductions could not be taken recognizes that where “net of all costs” language is used deductions are called for by the contract. See, Hanna Oil & Gas Co. v. Taylor, 297 Ark. 80, 81, 759 S.W.2d 563, 564 (1988) (noting that if the parties had intended to provide for deductions “they would have made some reference to costs, or ‘net’ proceeds”). Thus, it is clear that the language “net” clearly requires that deductions for expenses are to be made, and, when coupled with the language “at the well” it is even clearer that post-production expenses are properly deducted from lessors’ royalty payments. Because the language claimed by the Plaintiffs to be ambiguous is not ambiguous to those willing to take all terms of a royalty provision into account, the Plaintiffs’ arguments must fail and this Court must answer the first certified question, as reformulated by CNR, “yes,” and the second certified question, as reformulated, “no.” However, even if this Court does not accept CNR’s proposed reformulation of the certified questions, CNR believes that it has adequately addressed both certified questions on this issue, and this Court should answer the certified questions, as drafted by the lower court, in the affirmative.

D. EVEN IF AMBIGUOUS, "AT THE WELL" AND SIMILAR LANGUAGE SHOULD NOT BE CONSTRUED TO PROHIBIT DEDUCTIONS FOR POST-PRODUCTION EXPENSES.

Even if this Court believes that "at the well" and similar royalty language is ambiguous with regard to the allocation of post-production expenses, deductions are not automatically prohibited as suggested by the Plaintiffs. In accordance with accepted rules of interpretation, even if the language is ambiguous, CNR is entitled to a determination by the finder-of-fact as to the intent of the parties to the oil and gas leases. Furthermore, the rule of construction directing courts to strictly construe oil and gas leases against the lessees (i) must not be applied unless the parties' intent cannot be determined by a fact finder, and (ii) must not be applied at all where, as here, the purposes of that rule are not furthered by its application.

1. If "At the Well" Language Is Ambiguous, CNR Is Entitled To First Have The Parties' Intent Determined By A Fact Finder.

CNR is entitled to have the parties' intent determined by a fact finder before a court may consider whether to apply the rule of strict construction against lessees that is advocated by the Plaintiffs and the lower court. Where the terms of a contract are ambiguous, there is an order to rules that must be followed in determining the intent of the parties to the contract. West Virginia has acknowledged this:

[T]his and all other courts of this land have laid down certain rules for ascertaining the intent of parties to any written instrument. If the language used be clear and unambiguous, it simply "applies" the language used to the factual situation. If it is found to be ambiguous, the rules applicable to that type of instrument are used to ascertain the meaning of the parties and if the instrument contains irreconcilable provisions the rules are equally well established for determining the dominant intent in the circumstances.

Lewis v. Dils Motor Co., 148 W. Va. 515, 523-24, 135 S.E.2d 597, 601-02 (1964). Thus, the Lewis Court makes clear that where a contract is ambiguous, courts must follow the rules of construction prescribed, in the order prescribed. First among the rules alluded to by the

Supreme Court in Lewis is the rule that a “[d]etermination of the intent of parties to a contract typically creates a question of fact to be determined by a jury.” Coleman v. Sopher, 201 W. Va. 588, 599, 499 S.E.2d 592, 603 (1997). See also, Energy Dev. Corp. v. Moss, 214 W. Va. 577, 586, 591 S.E.2d 135, 143 (2003) (holding that “if an inquiring court concludes that an ambiguity exists ... the ultimate resolution of it typically will turn on the parties’ intent. ... [F]acts together with reasonable inferences extractable therefrom are superimposed on the ambiguous words to reveal the parties’ discerned intent.”)

Wellman also indicates that whether “at the well” is sufficient to allocate costs is a determination to be made by the finder-of-fact rather than the court. Wellman requires that lessees provide evidence “of the type normally developed in legal proceedings requiring an accounting” to show that costs were actually and reasonably incurred. Wellman, 200 W. Va. at 211, 557 S.E.2d at 265. Thus, Wellman makes the relevant question not whether a lessee may deduct, but what deductions are actual and reasonable. The lower court has taken away CNR’s right to present evidence to a fact finder by answering the certified questions in such a way that deems the broad array of leases described in Exhibit A to the Order of Certification as silent with respect to the allocation of post-production expenses. Moreover, although it was noted in the lower court’s answer to both certified questions (see, Order of Certification) that the language contained in Exhibit A, including “at the well” language was “ambiguous,” CNR was not permitted to have “at the well” and similar royalty language reviewed by the fact-finder to glean the parties’ intent.

However, the Plaintiffs argue that because Martin v. Consolidated Coal & Oil Corp., 101 W. Va. 721, 133 S.E. 626 (1926), and similar cases recognize a rule of construction stating that oil and gas leases are generally construed liberally in favor of the lessor and strictly against the

lessee, a fact finder is not necessary to determine the intent of the parties. However, as the case law above shows, rules regarding “dominant intent” are not resorted to by courts until *after* other rules of construction have not proven sufficient to determine the true intent of the parties. Lewis, 148 W. Va. at 524, 135 S.E.2d at 602. Williston agrees with this: “*contra proferentem* [which literally means ‘against the offeror’] is generally said to be a rule of last resort and is applied only where other secondary rules of interpretation have failed.” 11 Williston on Contracts § 3212 (4th ed.) (2005).

In short, even if this Court agrees that the language is ambiguous, a fact finder should determine the intent of the parties. The strict construction rule advocated by the Plaintiffs and applied by the lower court improperly and prematurely denies CNR the right to deduct, before a factual investigation into the parties’ intent has been conducted.

2. Rule That Oil And Gas Leases Will Be Strictly Construed Against Lessees Is Not Applicable.

In this case, the rule of construction directing that oil and gas leases are to be construed against the drafter should not be applied at all. The Plaintiffs assert that this rule of construction operates in *all instances* automatically; however, it must not operate in situations where, as in the current matter, the non-drafting parties took advantage of their right to seek the advice of an attorney and to make modifications to their leases.

CNR acknowledges that West Virginia has long held that ambiguities in an oil and gas lease will be strictly construed against the lessee, Martin, 101 W. Va. 721, 133 S.E. 626 (1926); however, it challenges the Plaintiffs’ assertion that Martin stands for the proposition that “any ambiguity [will be] resolved in favor of the lessor,” as asserted by the Plaintiffs on page 9 of their Brief In Support of Affirming Trial Court’s Rulings on Certified Questions. The Plaintiffs suggest that Martin directs this Court that it *must* find in favor of the lessors if it first determines

that “at the wellhead” and similar royalty language is ambiguous. The Plaintiffs have taken improper liberties with the wording of the Martin decision. Martin specifically states “it is a recognized doctrine of this court that oil and gas leases generally are to be construed liberally in favor of the lessor and strictly against the lessee.” Id. at 628. Quite contrary to the Plaintiffs’ assertion, courts do have the ability to interpret oil and gas leases in favor of a lessee despite this rule of construction. Indeed, this Court has done so in the past. For example, in Warner v. Haught, 174 W. Va. 722, 329 S.E.2d 88 (1985), this Court determined that it could not find in favor of the lessor despite the Martin rule regarding strict construction against gas lessees. In Warner, this Court held that an ambiguous provision of an oil and gas lease should be interpreted in favor of the lessee. The Plaintiffs’ assertion that all ambiguities must be resolved in favor of the lessor is, therefore, an inaccurate depiction of the law in West Virginia – courts are permitted to resolve ambiguities in oil and gas leases in favor of the lessee.

The facts of this case do not warrant application of the rule of strict construction. The rule stating that ambiguous terms in oil and gas leases are construed strictly against the lessee was adopted by this Court as a measure of protection for lessors who know little about the oil and gas industry and who do not have the benefit of counsel when entering into boiler-plate leases. This Court has noted this purpose, stating that if it did not apply strict construction against lessees of oil and gas leases

[w]e would be blind to patent facts, – that those engaged in the production of oil send agents armed with printed leases to solicit leases, and they take leases for great areas, and they are forms already prepared, and the people in many instances know little of them, are inexperienced in oil operations, and are without legal advice.

Bettman v. Harness, 26 S.E. 271, 276 (W. Va. 1896) (overruled on other grounds).

The concerns expressed by this Court in Bettman are not applicable to the leases of the named Plaintiffs in this matter, nor are they applicable to any of the leases contained in the record before this Court. The named Plaintiffs in this action, who were selected to represent the interests of the class and who the Plaintiffs asserted accurately represented them for class certification purposes, are simply not individuals this Court implemented the strict construction rule to protect. For example, Larry Parker, one of the named Plaintiffs, testified at deposition that he read the oil and gas lease he entered into with CNR and sought and received the advice of an attorney, Mr. Brumbaugh, before signing the lease. (See, Parker Depo., CNR's Designation of Record, Doc. No. 24, 63:14-21). Similarly, another named Plaintiff, Garrison Tawney, also testified that he read his lease before signing. In fact, Mr. Tawney testified that he understood the lease provisions and that he had the same attorney, Mr. Brumbaugh, review the lease. Further, Mr. Tawney testified that Mr. Brumbaugh made changes to the lease. (See, Tawney Depo., CNR's Designation of Record, Doc. No. 23, 92:19-23, 93:1-23, 94:1-23, 95:1-23, 96:1).

Additionally, a number of the lessors are business entities that can better negotiate lease terms and freely enter into leases. The entire large landowner subclass cannot reasonably claim to be in an unequal bargaining position and unable to understand the terms of the contract.⁹ Thus, business entity lessors are also not entitled to the benefit of the common law strict construction rule for this additional reason.

Based on the above testimony and law, if "at the well" language is ambiguous, CNR is entitled to have the parties' intent determined by a fact finder before any rules of construction or

⁹ The large landowner subclass includes the following Plaintiffs: Boone East Development Co.; Henry Closterman Trust; Cole & Crane Real Estate Trust; Cotiga Development Co.; Dingess-Rum Properties, Inc.; Horse Creek Coal Land; Horse Creek Land & Mining Co.; Kanawha Gauley Coal & Coke Co.; McCreery Coal Land Co.; Mingo Oil & Gas Co.; Mingo Wyoming Coal Land Co.; Southern Land Company Limited Partnership; Dickinson Properties Limited Partnership; and Williamson Mining & Manufacturing Co.

interpretation are implemented which call for a court to construe the terms against the lessee. Furthermore, where lessors are sophisticated parties and/or have had the opportunity to consult counsel and negotiate terms of an oil and gas lease, the rule of strict construction against oil and gas lessees should not be applied. Because the rule against strict construction does not apply where there is no danger of unduly influencing the lessor and because lessees are entitled to have the intent of the parties as expressed in the contract determined by a fact finder, deductions are not automatically improper where "at the well" language is used, even if such language is considered ambiguous.

VII. RELIEF PRAYED FOR

Based upon the foregoing, Columbia Natural Resources, LLC, respectfully requests that this Court answer the first certified question, as proposed to be reformulated, "yes" and to answer the second certified question, as proposed to be reformulated, "no." In the alternative, CNR asks that this Court answer both the certified questions, as presented by the lower court, in the affirmative.

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BEFORE THE WEST VIRGINIA SUPREME COURT OF APPEALS

**ESTATE OF GARRISON G. TAWNEY, by
LELA ANN GOFF, Executrix, LELA ANN
GOFF and VERNON B. GOFF, husband and
wife, JANICE E. COOPER and CLIFFORD R.
COOPER, husband and wife, LARRY G.
PARKER, JOHN W. PARKER, RICHARD L.
ASHLEY, MYRTLE JONES, by her
Attorney-in-Fact, ORTON A. JONES**

Plaintiffs,

v.

No. 32966

**COLUMBIA NATURAL RESOURCES,
LLC, f/k/a COLUMBIA NATURAL
RESOURCES, INC., a Texas corporation.**

Defendants.

CERTIFICATE OF SERVICE

I, Timothy M. Miller, counsel for COLUMBIA NATURAL RESOURCES, LLC., f/k/a COLUMBIA NATURAL RESOURCES, INC., do hereby certify that a true and exact copy of the foregoing **BRIEF OF DEFENDANT COLUMBIA NATURAL RESOURCES, LLC, ON CERTIFIED QUESTIONS** has been served upon counsel of record this 17th day of March, 2006, via U.S. mail, postage prepaid, addressed as follows:

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