



# Post-Production Royalty Disputes

48<sup>th</sup> Annual Ernest E. Smith Oil, Gas and Mineral  
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## THE ROYALTY CLAUSE & TEXAS DECISIONS



- The Early Cases: Vela, Middleton, Yzaguirre, Heritage, Judice
  - The Later Cases: Hyder, Potts, Warren, Texas Crude
- The Most Recent Cases: Blueston v. Randle, Bluestone v. Engler
  - The Pending Case: Devon v. Sheppard

## ROYALTY AUDIT ISSUES

Downstream Commingling, Condensate Shrinkage, Lease/Plant Fuel, Flaring/Venting, Lost & Unaccounted for (LUF), T&F Fees, Skim Oil, etc

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## Post Production Costs from the Lessor and Lessee's Sometimes Differing Perspectives



### William James Murray



**Full Name:** William James Murray  
**AKA:** Bill  
**Location:** Section: Statesman's Meadow, Section 1 (E)  
 Row: B Number: 12  
**Reason for Eligibility:** Member and Chairman, Railroad Commission of Texas  
**Birth Date:** February 17, 1915  
**Died:** August 3, 2004  
**Buried:** August 6, 2004



**MURRAY, WILLIAM JAMES (1915 - 2004).** William James "Bill" Murray, Jr., member and chairman of the Railroad Commission of Texas, was born February 17, 1915, in Coleman, Texas, to William James, Sr. and Virginia McGowan Murray. Growing up in the oil fields of northwest Texas, Murray, naturally, became interested in the oil business. After graduating from Cisco High School as the salutatorian in 1931, he was awarded a scholarship to attend Simmons College, now Hardin-Simmons University, in Abilene. After two years, in 1933, he transferred to the University of Texas at Austin, where he enrolled in the newly created Petroleum Engineering department. In 1936, after receiving his undergraduate degree, he continued his studies at UT and earned a Master's degree in Petroleum Engineering, graduating with the first class - four students - to the complete program. While at UT, he was awarded the Dean's medal for the highest number of grade points in the Engineering School (a record that stands today), as well as the Distinguished Graduate award of the UT School of Engineering.

Murray's devotion to the College of Engineering continued throughout his life, and in 1969, the William J. "Bill" Murray Endowed Chair of Engineering was established by several of his industry friends. Matched by university funds, the program now funds six or more projects per year, in all engineering disciplines.

After teaching petroleum engineering and doing research work at UT, Murray joined his father in Abilene and worked for Brannon Oil and Gas as an engineer, geologist, and lease superintendent. During this time, he courted Miss Emma Jo Newton of Buford, Texas, who was a freshman at John Tarleton College, now Tarleton State University. They were later married in 1939.

In July, 1939, Murray returned to Austin to work for the Railroad Commission of Texas as a senior petroleum engineer. During this time, he was labeled a "conservationist." Knowing that Texas oil would not last forever, he worked to conserve and preserve the driving force behind Texas' economy. He also worked to prevent companies from flaring, or burning off the natural gas that was a by product in drilling

## Petroleum Politics and the Texas Railroad Commission

by David F. Prindle



## Post Production Costs from the Lessor and Lessee's Sometimes Differing Perspectives



Oscar's founder Oscar Wyatt waves to all the work at a legislative hearing. His story: Coastal did nothing wrong.

## POWER POLITICS

by Paul Burka

How one company's wheeling and dealing brought the energy crisis into your life.

**W**hen L. E. Neenan opened his monthly utility bill from the San Antonio City Public Service Board last June, he couldn't believe his eyes. Yes, the figures were in the correct columns, all right, and they indeed read \$101.97. But it had to be a mistake. His May bill had been only \$32.93, and even that was a substantial increase over the March amount of \$20.68. How could his bill have tripled in one month, quipped in only three? Other San Antonians besieged City Hall with similar questions: In their dismay they learned there had been no mistake. Worse, they were told bluntly that their bills would continue to soar; another increase could be expected by August and still others would follow.

Austin was next, then Corpus Christi. Utility rates in both cities jumped high all winter, and will certainly climb even higher during the hot months ahead. (An Austin-based engineer for the Lower Colorado River Authority, which provides electricity for rural Central Texas, predicts it will cost nearly \$100 per month to keep his all-electric home functioning this summer.) Not has the rest of the state escaped the malaise spreading like a plague from South Texas. Natural gas rates will rise in Fort Worth beginning May 1, while Dallas and Houston are fighting delaying actions against inevitable increases. Nothing, absolutely nothing, indicates that utility rates will decrease or even level off; on the contrary, all economic and political signs suggest that the situation will continue to worsen.

"These rates, and the more that four million Texans who live in them, have one thing in common: all depend to some degree on a single company for the natural gas which heats their homes and generates their electricity. That company is the giant Coastal States Gas Corporation, an enterprise which, before it helped bring the energy crisis home to Texas—was one of the great success stories of American business.

Today the company is fighting for its very existence; the value of its common stock has long ago collapsed, and its assets are threatened by lawsuits totaling more than a billion dollars. Behind it all is Oscar Wyatt, Coastal's founder and chairman of the board. Wyatt is tireless, innovative, daring, charismatic—a man remarkable enough to have numbered among his friends Frank Erwin, Roy Farnsworth, Price Daniel, Ralph Yarborough, and Leon Jaworski. Once Wyatt was hailed as an entrepreneurial genius; now he is vilified by critics who seem to blame him for most of the world's crisis since the Deformation of Progress.

In order to understand what has happened to Coastal and its customers, it is first necessary to know something about the gas business. Natural gas is a form of petroleum, but for many years it remained the poor stepchild of crude oil. As late as the 1950s, oil producers wasted billions of cubic feet of gas by flaring it—a colossal squandering of usefulness of gas was limited to home heating or cooking; today gas used in this manner is described as thermogas or domestic gas. Gradually, however, people began to recognize the potential of gas as a clean-burning, marvelously efficient form of energy.

And cheap! Oh, was it ever cheap, sometimes as little as two cents per thousand cubic feet (2¢ per mcf). Natural gas would generate heat far more cheaply than its chief competitors, coal and fuel oil. This discovery led to the use of natural gas as a *fuel fuel* in power plants; gas heated the water in the boiler, converting it into steam to drive the generators and produce electricity.

Everybody benefited; cheap boiler fuel meant cheap electricity. One of the major beneficiaries was Coastal States Gas Producing Company, the forerunner of Coastal States Gas Corporation. Between 1962 and 1968, Coastal secured contracts to supply virtually all of Coastal and South Texas with gas for power plants and domestic use; it also agreed to supply gas to companies that served the mammoth Houston and North Texas markets. On the strength of these contracts, Coastal borrowed money to expand its operations until its complex of 41 corporations and subsidiaries formed the sixteenth largest corporation in Texas.

How did this corporate Goliath get up—and fall—into this mess? The answer is deceptively simple: Coastal ran out of gas. More precisely, it had more commitments to deliver gas than it had gas to deliver. This is another way of saying that Coastal sold what it never had to begin with—its own gas. The same type of transaction that got Billie Sol Estes in trouble. There are a number of crucial differences, however, not the least of which is that Billie Sol dealt in fertilizer, a product which can be used, if necessary, stockpiled and stored. Natural gas, on the other hand, is burned far before ground, and is in-

Post Production Costs from the Lessor and Lessee's Sometimes Differing Perspectives

BlueStone v. Randle

06796 1889 0015 VOL. PG. OIL, GAS AND MINERAL LEASE (FAS-07) MURRAY RANDLE with the last day of April 2011, Lessee MURRAY RANDLE ALSO SOMETIMES KNOWN AS WALKER MURRAY RANDLE ALSO SOMETIMES KNOWN AS WALKER R. RANDLE

1309 0047 VOL. PG.

EXHIBIT 'A' Attached to and made a part of Oil, Gas and Mineral Lease dated April 1, 2003, by and between MURRAY RANDLE, Lessor and QUICKSILVER RESOURCES, INC, Lessee It is understood and agreed by all parties that the language on this Exhibit "A" supersedes any provisions to the contrary in the printed lease hereof

14 ANYTHING HEREIN TO THE CONTRARY notwithstanding, the royalties to be paid Lessor on production are ONE-FIFTH (1/5) Three-Sixths (3/6), and wherever the word One-Eighth appears in this lease, the same is hereby amended to read Three-Sixths (3/6) ONE-FIFTH (1/5); WMR

26 LESSEE AGREES THAT all royalties accruing under this Lease (including those paid in kind) shall be without deduction, directly or indirectly, for the cost of producing, gathering, storing, separating, treating, dehydrating, compressing, processing, transporting, and otherwise making the oil, gas and other products hereunder ready for sale or use Lessee agrees to compute and pay royalties on the gross value received, including any reimbursements for severance taxes and production related costs



POST PRODUCTION EXPENSES AFTER HERITAGE

Warren v. Chesapeake Expl., L.L.C., 759 F.3d 413, 414 (5th Cir. 2014)

- "20% of the amount realized, computed at the mouth of the well"
• No deductions clause
• Post-production deductions: OK
• But not 3rd lease: "market value at the point of sale"

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First appeared as part of the conference materials for the  
48<sup>th</sup> Annual Ernest E. Smith Oil, Gas and Mineral Law Institute session  
"Royalty Litigation Post Production Cost"