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IN THE SUPREME COURT
STATE OF NORTH DAKOTA

DAVID A. BLASI and PAULA J. BLASI, as TRUSTEES OF THE BLASI LIVING TRUST, on behalf of themselves and a class of similarly situated persons,	)	
Plaintiffs-Appellants,	)	
	)	Supreme Court Nos. 20200327-20200331
v. Bruin E&P Partners, LLC, et al., v. Lime Rock Resources Operating Company, Inc., et al., v. Kraken Development III LLC, et al., v. Continental Resources, Inc., v. EOG Resources, Inc.,	)	
Defendants-Appellees.	)	

Certified Question of Law Submitted November 30, 2020
Case Nos. 3:20-cv-85; 3:20-cv-91; 3:20-cv-92; 3:20-cv-93; 3:20-cv-94
United States District Court for the District of North Dakota
The Honorable Peter D. Welte, Chief Judge

BRIEF OF DEFENDANTS-APPELLEES LIME ROCK RESOURCES OPERATING COMPANY, INC., LIME ROCK RESOURCES III-A, L.P., AND EOG RESOURCES, INC.

ORAL ARGUMENT REQUESTED

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STATEMENT OF THE ISSUES PRESENTED

[¶1] Whether the instant oil royalty provision is interpreted to mean the royalty is based on the value of the oil "at the well:"

> Lessee agrees … "[t]o deliver to the credit of the lessor, free of cost, in the pipeline to which lessee may connect wells on said land, the equal [fractional] part of all oil produced and saved from the leased premises."

ORAL ARGUMENT REQUESTED

[¶2] Appellees Lime Rock Resources Operating Company, Inc. and Lime Rock Resources III-A, L.P ("Lime Rock") and Appellee EOG Resources, Inc. ("EOG") believe that oral argument will assist the Court in resolving the certified question. This case will have a significant impact in North Dakota, as it involves an oil royalty clause used in thousands of leases in North Dakota and currently at issue in at least twelve putative class actions. Appellees urge the Court to enforce the clause's plain language, consistent with interpretations by courts in other states. On the other hand, Appellants urge this Court to adopt a novel interpretation at odds with every other jurisdiction to have interpreted similar royalty language. Given the significance of these issues, Appellees Lime Rock and EOG respectfully request oral argument in this matter.

STATEMENT OF THE CASE

[¶3] In this case, Appellants seek to upend nearly a century of settled oil and gas law and change the deal embodied in the lease language itself. In May 2020, Appellants filed five putative class actions in federal court, asserting federal jurisdiction under the Class Action Fairness Act and claiming that Appellees improperly deducted post-production costs from lessors' royalty interests.[1] *See* 28 U.S.C. § 1332(d). The cases were all assigned

[1] *See* App. 103, *Blasi v. Bruin E&P Partners, LLC*, No. 3:20-cv-00085 (D.N.D. May 20, 2020) ("*Blasi v. Bruin*"); App. 8, *Blasi v. Lime Rock Res. Operating Co., Inc.*, No. 3:20-

(or reassigned) to Chief Judge Peter D. Welte of the District of North Dakota, and each defendant separately moved to dismiss.[2] Chief Judge Welte reserved judgment on the motions to dismiss and held a status conference regarding the possibility of certifying the disputed question of law to this Court. Each party submitted their position on the matter to Chief Judge Welte on November 16, 2020.[3] On November 30, 2020, Chief Judge Welte certified the meaning of the royalty provision to this Court and stayed all five cases pending resolution of the certified question. *See, e.g.*, App. 21, Order for Certification, *Blasi v. Lime Rock*, No. 20-cv-00091 [Dkt. 27] (D.N.D. Nov. 30, 2020) ("Certification Order") at

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cv-00091 (D.N.D. May 26, 2020) ("*Blasi v. Lime Rock*"); App. 31, *Blasi v. Kraken Dev. III LLC*, No. 3:20-cv-00092 (D.N.D. May 26, 2020) ("*Blasi v. Kraken*"); App. 53, *Blasi v. Cont'l Res., Inc.*, No. 3:20-cv-00093 (D.N.D. May 26, 2020) ("*Blasi v. Cont'l.*"); App. 77, *Blasi v. EOG Res., Inc.*, No. 3:20-cv-00094 (D.N.D. May 26, 2020) ("*Blasi v. EOG*").

2 *See* Mot. to Dismiss, *Blasi v. Lime Rock*, No. 3:20-cv-00091 [Dkt. 17] (D.N.D. July 22, 2020); Mot. to Dismiss, *Blasi v. Kraken*, No. 3:20-cv-00092 [Dkt. 15] (D.N.D. July 22, 2020); Mot. to Dismiss, *Blasi v. Cont'l*, No. 3:20-cv-00093 [Dkt. 16] (D.N.D. July 13, 2020); Mot. to Dismiss, *Blasi v. EOG*, No. 3:20-cv-00094 [Dkt. 15] (D.N.D. July 24, 2020). One case, *Blasi v. Bruin E&P Partners, LLC*, was stayed before any responsive pleading was filed. Order Adopting Stipulation & Staying Case, *Blasi v. Bruin*, No. 3:20-cv-00085 [Dkt. 15] (Sept. 11, 2020). The stay has been lifted for the limited purpose of participation in these certification proceedings. Order Granting Req. to Lift Stay, *Blasi v. Bruin*, No. 3:20-cv-00085 [Dkt. 21] (Nov. 12, 2020).

3 *See* Defs.' Submission, *Blasi v. Bruin*, No. 3:20-cv-00085 [Dkt. 22] (D.N.D. Nov. 16, 2020); Defs.' Submission, *Blasi v. Lime Rock*, No. 3:20-cv-00091 [Dkt. 25] (D.N.D. Nov. 16, 2020); Defs.' Submission, *Blasi v. Kraken*, No. 3:20-cv-00092 [Dkt. 23] (D.N.D. Nov. 16, 2020); Def.'s Submission, *Blasi v. Cont'l*, No. 3:20-cv-00093 [Dkt. 24] (D.N.D. Nov. 16, 2020); Def.'s Submission, *Blasi v. EOG*, No. 3:20-cv-00094 [Dkt. 21] (D.N.D. Nov. 16, 2020). Plaintiffs-Appellants filed the same submission in all five cases. *See, e.g.*, Pls.' Submission, *Blasi v. Lime Rock*, No. 3:20-cv-00091 [Dkt. 26] (D.N.D. Nov. 16, 2020).

1; Order Staying Cases, *Blasi v. Lime Rock*, No. 3:20-cv-00091 [Dkt. 28] (D.N.D. Nov. 30, 2020).[4]

[¶4] A single question of law was certified to this Court: Does an oil royalty clause that requires the lessee "[t]o deliver to the credit of the lessor, free of cost, in the pipeline to which lessee may connect wells on said land, the equal [fractional] part of all oil produced and saved from the leased premises" value oil "at the well"?

[¶5] On January 8, 2021, Appellants submitted a Motion to Decline to Answer the Certified Question to this Court. *See* Jan. 8, 2021 Plaintiffs'/Appellants' Motion to Decline to Answer Certified Question at This Time [Dkt. 8]. Appellees responded to that motion on January 22, 2021.[5] On January 27, 2021, this Court ruled that Appellants' Motion to Decline would be considered alongside the merits of this case. Jan. 27, 2021 Order [Dkt. 34].

[¶6] The unambiguous language of the leases answers the certified question in the affirmative. The provision in question is an in-kind royalty provision, meaning that it contemplates the delivery of actual oil to the lessor on the leased premises, rather than a cash payment to the lessor based on the proceeds from the lessee's sale of oil. Specifically, the provision states that the lessor is entitled to receive its percentage of the oil "free of cost, in the pipeline to which Lessee may connect ***wells on said land***." While Appellants

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[4] Identical orders certifying the question and staying the cases were filed in each of the five proceedings.

[5] *See* Bruin's & Kraken's Joint Resp. to Mot. to Decline to Answer Certified Question at this Time [Dkt. 20] (Jan. 22, 2021); Lime Rock's Resp. to Mot. to Decline to Answer Certified Question at this Time [Dkt. 21] (Jan. 22, 2021); EOG's Resp. to Mot. to Decline to Answer Certified Question at this Time [Dkt. 22] (Jan. 22, 2021); Cont'l's Resp. to Mot. to Decline to Answer Certified Question at this Time [Dkt. 23] (Jan. 22, 2021).

attempt to contort the lease language to suit their position in this case, it is susceptible to only one reasonable interpretation: It expressly sets the valuation point for oil where it is to be delivered on the leased property—at the well. Here, Appellants choose to receive their royalty "in value," rather than "in kind." But the fact that Appellants chose cash rather than oil does not entitle them to more than what they are due under the contract, does not change the meaning of the leases, and does not entitle them to a windfall: No matter how they take their royalty, Appellants are only entitled to the value of the oil at the "wells on said land." As such, Lime Rock and EOG respectfully submit that the answer to the certified question in this case is a definitive "yes"—the provision in question values oil "at the well."

STATEMENT OF FACTS

[¶7] Appellants, trustees of the Blasi Living Trust, allege they are successors to oil and gas leases covering certain lands in North Dakota, making the trustees the lessors. App. 21 ¶ 1, Certification Order. Those leases grant lessees the right to explore for and produce hydrocarbons (including oil and natural gas) from wells drilled on the lessors' property. *Id.*

[¶8] The leases each contain an oil royalty provision that states:

> Lessee agrees … "[t]o deliver to the credit of the lessor, free of cost, in the pipeline to which Lessee may connect wells on said land, the equal [fractional] part of all oil produced and saved from the leased premises."

Id. ¶ 2.

[¶9] This is an "in-kind" royalty provision, meaning that it provides for delivery of the oil itself, rather than monetary payment. *See* 3 Williams & Meyers, Oil and Gas Law § 642.5 (2019). Appellants, however, have chosen to receive a cash royalty rather than taking the oil in kind. App. 21 ¶ 3, Certification Order. Thus, lessees market the oil on Appellants' behalf and pay Appellants royalties in cash. *Id.*

[¶10] Here, Appellants allege that lessees calculate the value of oil at the well by deducting "costs such as gathering or moving the oil and other costs" when calculating royalty payments. *Id.* Appellants filed five putative class action lawsuits against five separate lessees (Appellees) in federal court, claiming that the royalty provision in question prohibits lessees from deducting post-production costs. *Id*. ¶¶ 3-4.[6]

[¶11] Concluding that no North Dakota Supreme Court precedent directly resolves whether this royalty provision values oil "at the well" and that resolution of the certified question of law in Appellees' favor would likely end Appellants' claims, Chief Judge Peter D. Welte certified the interpretation of the royalty provision to this Court. *Id.* at 2-3.

STANDARD OF REVIEW

[¶12] To interpret a royalty provision, this Court applies the same rules of interpretation to oil and gas leases as it would to any other contract. *Johnson v. Statoil Oil & Gas LP*, 2018 ND 227, ¶ 7, 918 N.W.2d 58. Under North Dakota law, "[a] contract must be so

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[6] In addition to the five putative class actions arising out of the Eastern Division of the District of North Dakota at issue here, six additional putative class actions have been filed in the Western Division of the District of North Dakota concerning the interpretation of the same or a similar royalty clause, for a total of eleven cases. *See Hystad Ceynar Mins., LLC v. Whiting Oil & Gas Corp.*, No. 1:20-cv-00216 (D.N.D. Nov. 20, 2020); *Ceynar v. Oasis Petroleum N. Am. LLC*, No. 1:20-cv-00139 (D.N.D. Aug. 3, 2020); *Double Diamond C Min., LLC v. Zavanna, LLC*, No. 1:20-cv-00140 (D.N.D. Aug. 3, 2020); *Heggen Lewis v. XTO Energy Inc.*, No. 1:20-cv-00125 (D.N.D. July 15, 2020); *Heggen Lewis v. Nine Point Energy, LLC*, No. 1:20-cv-00124 (D.N.D. July 15, 2020); *Nelson v. Equinor Energy LP*, No. 1:20-cv-00133 (D.N.D. July 27, 2020). In a ***twelfth*** pending putative class action in the Western Division of the District of North Dakota, a different judge—Judge Daniel M. Traynor—denied a motion to dismiss on the interpretation of the same royalty clause, "[i]n the absence of any North Dakota caselaw construing the [] provision." *See White River Royalties, LLC v. Hess Bakken Invs. II, LLC,* 2020 WL 6231893 (D.N.D. May 22, 2020).

interpreted as to give effect to the mutual intention of the parties as it existed at the time of contracting so far as the same is ascertainable and lawful." N.D.C.C. § 9-07-03. Moreover, "the intention of the parties is to be ascertained from the writing alone if possible." *Id.* § 9-07-04.

[¶13] "When the language of the contract is unambiguous and the parties' intent can be determined from the language alone, the interpretation of the contract is a question of law." *Northstar Founders, LLC v. Hayden Cap. USA, LLC,* 2014 ND 200, ¶ 46, 855 N.W.2d 614. This Court is "the final arbitrator of unsettled questions of state law." *Mosser v. Denbury Res., Inc.*, 2017 ND 169, ¶ 12, 898 N.W.2d 406.

ARGUMENT

[¶14] The plain language of the royalty provision answers the question before this Court. The oil royalty provision is an in-kind provision requiring oil to be delivered to lessors "free of cost, in the pipeline to which Lessee may connect wells on said land." App. 22 ¶ 2, Certification Order. For over a century, this lease language has been consistently interpreted by courts and scholars all over the country to mean that lessors are entitled to the actual oil in kind or the value of oil at the well free of the costs of production, but before the oil has been transported downstream. North Dakota should not be the only court in the country to adopt Appellants' distorted interpretation of the lease language.

[¶15] This Court has already resolved a similar question in the context of ***gas*** royalties. In *Bice v. Petro-Hunt, LLC*, this Court interpreted a royalty provision that "call[ed] for gas royalty payments to be calculated based on the market value of the gas at the well," concluding that the lease language set the valuation point "at the well." 2009 ND 124, ¶¶ 4, 21, 768 N.W.2d 496.

[¶16] In *Bice*, as here, the lessors argued that the royalty language prohibited the lessee from deducting costs incurred after gas left the wellhead, and that the lessors should receive the downstream value of the gas without sharing in any of the costs of obtaining that downstream value. *Id.* ¶ 10. The lessee in *Bice* argued that the lease language providing that royalties were to be based on the "market value ***at the well***" meant that gas should be valued at the wellhead, permitting the lessee to deduct a pro rata share of costs incurred between the wellhead and the downstream point of sale to calculate the value of the gas "at the well." *Id.* ¶ 8 (emphasis added). This is commonly known as the "netback" or "work-back" method of calculating wellhead value. *Id*. ¶ 14. Noting that the majority of scholars and states favored this approach, this Court held that the phrase "at the well" values hydrocarbons at the wellhead and permits lessees to deduct costs incurred once hydrocarbons leave the wellhead (known as "post-production costs") from lessors' royalties. *Id.* ¶¶ 13–15, 21.

[¶17] This case presents a similar question as *Bice*, but in the context of ***oil*** royalties. Specifically, the question here is whether the "free of cost, in the pipeline to which lessee may connect wells on said land" language at issue also values oil at the well, like the gas royalty provision valuing gas "at the well" in *Bice*. The plain language of this provision makes clear that the answer is "yes," and this interpretation is confirmed by both common sense and decades of settled law.

[¶18] Appellants' proposed interpretation—under which the lessor would receive the downstream value of the oil without sharing in any of the substantial costs incurred to obtain that downstream value, simply because they choose to take the oil in cash rather than in kind—would rewrite the leases and runs contrary to law and logic. To start, valuing the oil at any point other than on the leased property would ignore the "on said land" language in the leases in violation of settled North Dakota law. Valuing oil at a different location would also ignore the verb "connect," which points to a joining or fastening together of the referenced "pipeline" and the "wells" on the leased premises. While Appellants lean heavily on the "free of cost, in the pipeline" lease language, they ignore the fact that such language means that lessees may not deduct ***production*** costs, which are incurred ***before*** oil enters the pipeline, but that language does not forbid deduction of the ***post***-production costs at issue here. Moreover, Appellants ignore the rest of the clause, which provides that the "pipeline" referred to is the one "to which lessee may connect wells on said land."

[¶19] Appellants' interpretation would not only rewrite the leases and overturn a century of jurisprudence, but it would also result in a windfall to Appellants. Oil is more valuable after substantial costs have been incurred to transport it downstream to a variety of distant markets. Appellants seek to shift the valuation point for oil to those downstream points, and to receive those higher downstream prices without sharing in the costs required to obtain those higher prices—an inequitable result never contemplated by the parties, as reflected by the lease language itself.

I. The Certified Question is Ripe for This Court's Review.

[¶20] As Lime Rock and EOG previously argued, this Court can—and should—resolve the certified question now. Lime Rock and EOG hereby incorporate their Responses to Appellants' Motion to Decline to Answer the Certified Question at this Time into this Brief by reference. *See* Jan. 22, 2021 Resps. of Lime Rock & EOG to Mot. to Decline to Answer Certified Question at this Time [Dkts. 21 & 22].

II. The Plain Language of the Leases Values Oil at the Well.

[¶21] The leases set the point of valuation at the well by unambiguously providing that the lessee is "[t]o deliver to the credit of [l]essor, free of cost, ***in the pipeline to which Lessee may connect wells on said land***, the equal [fractional] part of all oil produced and saved from the leased premises." App. 21 at 1, Certification Order (emphasis added). The provision thus explicitly provides that royalty oil will be delivered where the lessee "may connect" the anticipated pipeline to "wells on said land," *i.e.*, on the leased property, not at some unspecified point downstream.

[¶22] The provision is an in-kind provision: It provides that a lessor is to receive its share of oil at the wellhead, such that the lessor can then either use or market and sell the oil itself as it sees fit. Here, lessors have chosen not to take the oil in-kind; rather, lessees market the oil on their behalf and then pay royalties in cash. The fact that lessors have decided not to take the oil in kind at the well—either because they do not wish to use it or do not wish to shoulder the burden of selling it—does not entitle them to a different and higher value of the oil. That is because the lease language fixes the valuation point at the place where lessors would be entitled to receive the oil if they took it in kind: "in the pipeline to which the lessee may connect wells on said land." This should be the beginning and end of the analysis.

[¶23] Historically, the same or similar language has always been interpreted to value oil at the well—even without the language in the leases at issue underscoring that the valuation point is "on said land." For instance, one 1926 treatise states that "ordinary commercial oil and gas lease[s] … provide[] that the lessor shall deliver, to the credit of the lessor, free of cost, into the pipe line, to which he shall connect his wells the equal [fractional part] of all the oil produced and saved from the premises." Lawrence Mills & J.C. Willingham, *The Law of Oil and Gas* 183 (1926). That same treatise ***also*** states that such in-kind royalty provisions render lessees liable only for "the reasonable value of the royalty share at the well." *Id.* at 190. Historical sources agree that, where an in-kind provision requires delivery into a pipeline and there is no pipeline on the land, "the lessee's obligations are at an end when he has made a delivery at the place designated," so "the expense of storage and transportation thenceforth must be borne by the lessor." A.W. Walker, Jr., *The Nature of the Property Interests Created by an Oil & Gas Lease in Texas*, 10 Texas L. Rev. 291, 313 (1932). The additional language incorporated into the leases at issue here, specifying that oil is to be delivered "on said land," further emphasizes that understanding.

[¶24] Valuing the oil at the well also makes good sense. Oil can be transported from the wellhead to downstream points of sale in numerous ways—*e.g.*, it can flow from the wellhead into a gathering pipeline connected to the wellhead; it can flow from the wellhead to a storage tank on the leased premises and then be transported by truck or train downstream; or it can be transported by numerous other means. Oil can also be sold in many places—at the well where it is extracted, downstream after it has been refined and transported, or anywhere in between. The value of the oil varies based on where it is sold, and in what condition. Unsurprisingly, "[p]roducts on which post-production costs have been expended are generally more valuable than products straight out of the well." *Burlington Res. Oil & Gas Co. LP v. Tex. Crude Energy, LLC*, 573 S.W.3d 198, 203 (Tex. 2019). For this reason, "a royalty on products at their downstream point of sale is more valuable than a royalty on the same products at the well." *Id.*; *see also Zehentbauer Family Land, LP v. Chesapeake Expl., LLC*, 935 F.3d 496, 501 (6th Cir. 2019) ("[B]ecause the midstream products are closer to downstream markets, they are worth more than the raw upstream products."); *Kilmer v. Elexco Land Servs., Inc.*, 990 A.2d 1147, 1158 (Pa. 2010) (similar).

[¶25] This Court has held that when a royalty provision values hydrocarbons "at the well" but hydrocarbons are not actually sold at the well, the lessee must calculate their value as it would have existed at the well. *See Bice*, 2009 ND 124, ¶ 14, 768 N.W.2d 496. Under the "work-back" or "netback" method, the lessee calculates the value of the oil or gas at the well by subtracting post-production costs incurred after extracting the oil or gas from the ground (for instance, "transportation, gathering, compression, processing, treating, and marketing costs") from the sales price it received for the oil or gas. *Id.* (quoting Byron C. Keeling & Karolyn King Gillespie, *The First Marketable Product Doctrine: Just What is the Product?*, 37 St. Mary's L.J. 1, 31–32 (2005)).[7]

[¶26] If lessors like Appellants took the oil in kind, they would bear the transportation and marketing expenses discussed above for their share of the oil. Requiring royalties to be paid on a downstream value without lessors bearing their pro rata share of post-production costs would incentivize lessors to skirt the plain language of their leases simply by choosing to take payment in cash instead of in kind, and to receive the windfall of higher downstream prices without sharing in any of the costs incurred to obtain that higher downstream price. *Cf. Bice*, 2009 ND 124, ¶ 27, 768 N.W.2d 496 (declining to create an "absurd result" by interpreting "free use" clause to confer unjust benefit to lessor contrary to parties' intent).

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[7] Appellants claim that the "at the well" rule discussed in *Bice* applies only in the natural gas context. *See* Opening Br. ¶¶ 29–30 [Dkt. 9]. That is clearly wrong—*Bice* described the "at the well" rule as applying to oil ***and*** gas. *See* 2009 ND 124, ¶ 14, 768 N.W.2d 496 ("States that follow the 'at the well' rule allow a lessee to use one of two methods to calculate the gas or oil's market value at the well.").

[¶27] Moreover, Appellants' interpretation of the lease language would result in a Frankenstein-like system in North Dakota, under which the many gas leases that value gas "at the well" would be read to value gas "at the well," but oil provisions that value oil at the "wells on said land" would value oil ***downstream*** of the "wells on said land." *See, e.g.*, App. 17 ¶ 3, Oil and Gas Lease, Ex. 1 to Compl.; App. 25 ¶ 3, Exemplar Lease, Ex. A, Certification Order. This incongruous result runs counter to common sense and the plain language of the leases.

[¶28] At bottom, there is no reason why this royalty provision, under which the parties intended that Appellants would take oil in kind, on the land where the wellhead is located, could ever be read to mean that oil must be valued at a point far downstream from that land without any sharing in the costs incurred to obtain that downstream price. The plain language of the leases set the point of valuation at the well.

III. Lessees' Interpretation is Supported by Well-Established Authority.

[¶29] Unsurprisingly, this straightforward interpretation of the lease language is supported by an unbroken, century-old chain of case law and scholarly work from all over the country. Appellants ask this Court to disregard this precedent and stake out a new minority position that would be the first of its kind in the nation. The Court should decline the invitation.

[¶30] To start, the leading oil and gas treatises confirm that the very royalty provision at issue here values oil "at the well." Dean Kuntz addressed this point head on in his seminal treatise: "If the royalty clause provides for delivery of royalty gas to the lessor's credit ***free of cost in the pipeline to which the well is connected***, the parties contemplate a delivery of royalty gas ***at the well***." Eugene Kuntz, A Treatise on the Law of Oil & Gas § 40.5(a) (2019) (emphasis added). While Appellants claim that this provision "does not even pertain to wellhead valuation," Opening Br. ¶ 38, that position simply is not credible. Kuntz clearly states that this language contemplates delivery "at the well," and this Court held in *Bice* that an "at the well" provision requires that hydrocarbons be valued at the well. While Appellants attempt to distinguish Kuntz by emphasizing that the relevant statements are made in the context of gas rather than oil, they do not (and cannot) provide any explanation whatsoever as to why the "free of cost, in the pipeline" language should be given a differing interpretation in the context of oil.[8] Indeed, that Appellants urge this Court to develop divergent lines of authorities in the gas context and the oil context only underscores why their position should not be adopted.

[¶31] Similarly, the Williams & Meyers treatise explains that "in cases involving language … providing for delivery 'free of cost in ***the pipe line*** to which Operator may connect his wells,' … [t]he language employed suggests that the parties assumed that a pipe line connection ***at the well*** would be available." 3 Williams & Meyers, Oil and Gas Law § 646.2 (2019) (second emphasis added); *see also id*. § 642.3 (similar). "[W]here the delivery point is to the pipeline to which the well is connected, or is at the well, the lessee has no obligation to treat the royalty oil to render it marketable or transport the royalty oil to market." *Id.* § 645 (internal quotations omitted). Again, Appellants' only means of distinguishing those statements is by claiming that they concern "unrelated ***gas*** royalty provisions." Opening Br. ¶ 39 (emphasis in original). Not only is that irrelevant, but it is also demonstrably wrong. In fact, the two sections of Williams & Meyers cited by Appellants specifically relate to ***oil*** royalties. *See* 3 Williams & Meyers, Oil and Gas Law

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[8] Elsewhere in their brief, Appellants argue that case law regarding gas is applicable. *See* Opening Br. ¶ 36 (discussing gas case *Kretni Dev. Co. v. Consol. Oil Corp.*, 74 F.2d 497 (10th Cir. 1934)).

§ 642.3 (entitled "Variants of ***oil*** royalty clause: Expenses to which royalty is subject" (emphasis added)); *id.* § 645 (discussing absence of obligation to treat and transport ***oil*** where point of valuation is "the pipeline to which the well is connected" (emphasis added)).

[¶32] Because the lease language in question values oil at the well, the treatises also confirm that, under this language, a lessor is not entitled to the higher downstream value of the oil without sharing in any of the costs incurred to obtain that higher value. Instead, where a royalty provision values oil at the well but oil is not actually sold at the well, lessees are permitted to use the netback method to calculate the value of the oil, had it been sold at the well—a rule that makes good sense. According to Williams & Meyers, "the weight of authority" on provisions concerning delivery of oil "free of cost ***in the pipe line*** to which [lessee] may connect his wells" mandates that the cost of "transportation or of treating oil or gas or of compressing gas to make it deliverable must be shared by the owner of the nonoperating interest [*i.e.*, Appellants]." 3 Williams & Meyers, Oil and Gas Law § 646.2 (emphasis in original); *see also Bice*, 2009 ND 124, ¶ 14, 768 N.W.2d 496 (describing the "netback method" of calculating wellhead value under such circumstances).

[¶33] Courts across the country have uniformly reached this conclusion for decades. Each of these courts' decisions shed light on the plain meaning of the royalty provision at issue here. *See Bice*, 2009 ND 124, ¶ 15, 768 N.W.2d 496 (reviewing other states' conclusions in adopting the "at the well" rule, including the law of "major oil and gas producing states" like Texas).

[¶34] In *Burlington Resources*, the Texas Supreme Court concluded that a royalty provision specifying royalty interests were to be delivered "into the pipeline ... to which any well or wells on such lands may be connected … free and clear of all royalties" "fixe[d] the royalty's valuation point at the physical spot where the interest must be delivered—***at the wellhead*** or nearby." 573 S.W.3d at 201, 211 (emphasis added). Though this case is highly relevant to the analysis here, Appellants claim that the ruling in *Burlington* did not rest on the "into the pipeline" language, but instead turned on separate language in a joint operating agreement ("JOA"). Opening Br. ¶ 37. Again, that is simply incorrect. Rather, the court found that the language in the JOA provided "additional support" and was "consistent" with its interpretation of the "into the pipeline" provisions, which it found valued oil at the wellhead. *Id.* at 208. As such, *Burlington* is directly on point.

[¶35] Further, the Texas Court of Appeals, Fort Worth, recently applied *Burlington* to a royalty provision substantively identical to that at issue here and held that such language values oil at the well. In *BlueStone Natural Resources II, LLC v. Nettye Engler Energy, LP*, the lease provided for the delivery of "a free one-eighth (1/8) of gross production of any such oil, gas or other mineral said amount to be delivered to Grantor's credit, ***free of cost in the pipe line***, if any, otherwise free of cost at the mouth of the well or mine." 2020 WL 3865269, at *4–5 (Tex. Ct. App.—Fort Worth July 9, 2020) (emphasis added), *petition for review filed* (Aug. 31, 2020). Relying on *Burlington*, the *BlueStone* court concluded that "the phrase 'in the pipe line' effectively sets the valuation point at the wellhead." *Id.* at *5. That decision specifically "reject[ed] [the] suggestion that a gathering system is not a pipeline." *Id.* The same logic applies here.

[¶36] These recent Texas cases are just the latest in a long line of cases with similar holdings all over the country. For example, Kansas courts also long ago concluded that nearly identical lease language sets the valuation point at the well. *See Molter v. Lewis*, 134 P.2d 404, 405–06 (Kan. 1943) (construing nearly identical "free of cost, in the pipe line" provision as a "contract ... to deliver the oil to the lessor ***at the well***" (emphasis added)); *see also Scott v. Steinberger*, 213 P. 646, 647–48 (Kan. 1923) (holding that under similar language, "lessor's share of the gas was to be ascertained and the price determined at the pipe line with which the wells were connected"). Under such circumstances, where lessors have chosen to take their royalty in cash instead of in kind, lessees may calculate value at the well using the netback method. *Voshell v. Indian Territory Illuminating Oil Co.*, 19 P.2d 456, 458 (Kan. 1933) (interpreting similar provision and finding plaintiff was owed "the selling price … less the cost of transportation").

[¶37] *Voshell* is illustrative. *Id.* There, the Kansas Supreme Court found that defendant lessee was entitled to deduct transportation costs pursuant to a royalty provision similar to the one at issue here when it had previously been selling oil to purchasers "in the vicinity" (without taking royalty deductions), but due to a market downturn, began selling downstream and incurring transportation costs to do so. *Id.* at 457–58. Though the lessee previously had no need to deduct transportation costs (because it had been selling oil nearby), the court held that such post-production deductions were clearly permitted by the lease language, and the lessee could use the netback method.

[¶38] California also long ago concluded as much, holding that a royalty provision giving the lessor the option to have oil "deliver[ed] into Lessor's tanks or to pipe line within one mile of premises from which oil is being produced, free of cost" entitled the lessor only to "his royalty share in kind as the oil came ***from the well***." *Vedder Petroleum Corp., Ltd. v. Lambert Lands Co*., 122 P.2d 600, 604 (Cal. Ct. App. 1942) (emphasis added). Where lessors had chosen to receive their royalties in cash, the "only reasonable construction" was that they should bear their "proportionate share" of dehydrating costs. *Id.* at 604–05.

[¶39] Federal courts agree that similar language values oil at the well. Though "[a] federal district court decision interpreting North Dakota law is not binding upon North Dakota courts … [this Court] will, however, respect a federal district court opinion if it is persuasive and based upon sound reasoning." *Bice*, 2009 ND 124, ¶ 19, 768 N.W.2d 496 (citation omitted) (examining Eighth Circuit decision in interpreting North Dakota law).

[¶40] *El Petron Enterprises, LLC v. Whiting Resources Corp.*, 2018 WL 1322391 (D.N.D. Mar. 14, 2018), is highly analogous and persuasive. There, the District of North Dakota considered how to calculate an overriding royalty reserved by El Petron when it assigned its interests in oil and gas leases to a third party. *Id.* at *1. The overriding royalty reservation provided that the overriding royalty "shall be paid or delivered to Assignor free and clear of all costs, except taxes, and shall be calculated in the same manner as [the production royalty on the underlying leases]." *Id.* at *3. In turn, the production royalty clause for oil was nearly identical to the provision before this Court, and required the lessee "deliver to the credit of Lessor, free of cost, in the pipeline to which Lessee may connect wells on said land, the equal 1/6th part of all oil produced and saved from the leased premises." *Id*. The court rejected El Petron's argument that the "free and clear of all costs" language in the overriding royalty reservation prohibited deduction of post-production costs. Instead, the court concluded that the defendant could "consider post-production costs to determine the value of the overriding royalty, as required by the Production Royalty calculation"—*i.e.*, use the netback method to calculate wellhead value—but could not further reduce the wellhead value by deducting production costs or administrative fees. *Id*. at *5. Notably, the production royalty clause was so clear that not even plaintiffs in *El Petron* disputed that it valued oil at the well. Thus, unsurprisingly, when interpreting these interlocking provisions, the court held that the lease valued oil at the well, citing this Court's decision in *Bice*. *Id.* at *4–5.

[¶41] Faced with this wealth of authority, ***Appellants have not pointed to a single case concluding that the royalty provision at issue values hydrocarbons someplace other than at the well***. Appellants cite *Kretni Development Co. v. Consolidated Oil Corp.*, 74 F.2d 497 (10th Cir. 1934), but that case supports Appellees' position, not Appellants'. There, the Tenth Circuit interpreted similar language providing for the delivery of oil "free of cost at the pipelines, to which [lessee] may connect his wells, one-eighth part of the oil and gas produced and saved from said premises." *Id.* at 497. The Tenth Circuit found that this language entitled the lessor only "to the royalty gas at the connection with the pipe line, or the proceeds from its sale at that point." *Id.* at 499–500. In other words, *Kretni* held that the language at issue here values hydrocarbons at the well, just like the many other authorities identified above.

[¶42] While Appellants claim that *Kretni* supports their theory that the term "pipeline" should be read to mean a long-haul pipeline, that claim is baseless. There was no dispute about the pipeline in *Kretni*: It was a pipeline on the leased premises that ran to Casper, Wyoming. The specific meaning of the word "pipeline" was not at issue, and the case contains no analysis regarding the term "pipeline" and whether or not it includes "conduit pipes, gathering lines, or any other 'system of pipe[lines].'" *Contra* Opening Br. ¶ 36. Moreover, the pipeline in *Kretni* ***was*** on the leased premises, and the case makes clear that the lease valued gas "at the point of connection with the pipe line to which the well was connected." 74 F.2d at 499 (emphasis added). Again, then, *Kretni* confirms that the language in question values oil on the leased property, at the connection to the well, not at a distant point downstream.

[¶43] Finally, Appellants' heavy reliance on *White River Royalties, LLC v. Hess Bakken Investments II, LLC* is misplaced, and underscores the desperation of their position. 2020 WL 6231893 (D.N.D. May 22, 2020); *see* Opening Br. ¶¶ 27–28. The judge in that case denied defendant's motion to dismiss precisely because there ***was no North Dakota case law available*** regarding the meaning of the exact royalty clause, not based on the merits of lessor's argument. *See White River*, 2020 WL 6231893 at *6 ("In the absence of any North Dakota caselaw construing the instant provision, White River presents a plausible interpretation."). That is the exact question now pending before this Court. As such, any claim by Appellants that *White River* supports their interpretation on the merits is nonsensical—the *White River* court explicitly declined to answer the question presented here because this Court has not yet answered it.

[¶44] In sum, the treatises, the states, and the federal courts who have addressed the question at issue all agree: The royalty provision values oil at the well.

IV. Appellants' Proposed Interpretation is Unfounded.

[¶45] Appellants' interpretation of the lease language runs counter to the plain language of the leases and the clear line of authority described above, and cannot be squared with the fact that the leases contemplate delivery in kind, on the leased property. Each argument offered in support of Appellants' strained interpretation is unavailing, and this Court should not be the first in the country to adopt it.

[¶46] ***First***, despite the straightforward lease language, Appellants claim that the "in the pipeline" language cannot be read to refer to a pipeline, but instead refers only to "a specialty type used for moving oil to the refinery." Opening Br. ¶ 20. They argue that "not all ‘pipes’ are ‘pipelines.’” *Id.* Based on their own definition, Appellants argue the proper point of valuation under the royalty agreement is the point at which oil enters a pipeline used to transport oil over long distances. *See id.* ¶ 19. There are a host of problems with this argument.

[¶47] To start, this reading of the lease language is substantially different from Appellants’ own complaint, which alleged that the deduction of ***any*** costs from the sale price of oil was improper, not just costs taken before the oil reaches a downstream pipeline. *See* App. 11 ¶ 11, Compl., *Blasi v. Lime Rock*, No. 3:20-cv-00091 [Dkt. 1] (D.N.D. May 26, 2020).

[¶48] Appellants’ particular, narrow definition violates black-letter law that contract language is to be given its plain meaning. *See* N.D.C.C. § 9-07-09. Appellants ask this Court to effectively read the word “pipeline” to mean an interstate or downstream pipeline, adding a new requirement that is not in the lease language itself.[9] *Contra Martin v. Allianz Life Ins. Co. of N. Am.*, 1998 ND 8, ¶ 11, 573 N.W.2d 823 (refusing to add words to contract).

[¶49] If the word “pipeline” ***does*** have a specialized meaning, this Court should derive it from well-founded authority. The Williams & Meyers Manual of Terms defines the word “pipeline” as:

> A tube or system of tubes used for the transportation of oil or gas. Types of oil pipelines include: lead lines, from pumping well to a storage tank; flow lines, from flowing well to a storage tank; lease lines, extending from the wells to lease tanks; gathering lines, extending from lease tanks to a central

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[9] Appellants’ position is also contradicted by the amicus brief filed in support of their position, which asserts that the “customary meaning of ‘pipeline’ in the oil and gas industry is not admissible to determine the meaning of the royalty provision at issue.” White River *Amicus Curiae* Br. 8 [Dkt. 29].

> accumulation point; feeder lines, extending from leases to trunk lines; and trunk lines, extending from a producing area to refineries or terminals.

8 Williams & Meyers, Oil and Gas Law Scope, *Pipeline* (2021). Under that definition, the word "pipeline" can refer to ***any number*** of different tubes involved in transporting hydrocarbons, including flow lines and lead lines on the leased premises and gathering lines leading from the lease premises to a point downstream. Under that definition, Appellants' interpretation of the lease language fails.

[¶50] Even Appellants' dictionary definitions cannot support their untenable reading of the lease language, because those definitions confirm that the term "pipeline" is not as narrow as Appellants read it. Appellants' chosen definition of "pipeline" is "[a] tube ***or system of tubes*** used for transporting crude oil and natural gas from the field or gathering system to the refinery." Opening Br. ¶ 20 (emphasis added). This definition—like the Williams & Meyers definition—clearly recognizes that multiple different pipelines are involved in the transportation of oil, and contains no language suggesting that only a large, downstream tube moving oil long distances should be considered a "pipeline," to the exclusion of all of the other tubes involved to get the oil to that downstream pipeline.

[¶51] The other definition cited by Appellants, "a line of connected pipes that are used for carrying liquids and gases over a long distance," further underscores that multiple pipelines might be involved in transporting oil and does not exclude smaller pipelines on the leasehold from its definition. Opening Br. ¶ 20 n.4. Although Appellants claim this definition is from Merriam-Webster, it appears that it is from a special version of that dictionary designed for "non-native speakers of English." *See The difference between Learnersdictionary.com and Merriam-Webster.com,* Learner's Dictionary, https://bit.ly/39LezRP. The main Merriam-Webster's definition of "pipeline" is even less helpful to Appellants: "a line of pipe with pumps, valves, and control devices for conveying liquids, gases, or finely divided solids." *See Pipeline*, Merriam-Webster, https://bit.ly/35QlWXi. Indeed, later in their brief, Appellants actually claim that a "system of pipes" is not a pipeline at all, directly contradicting their own definitions. *Id.* at ¶ 36.

[¶52] Not only does Appellants' interpretation of the word "pipeline" add words to the leases, but it also does so in a manner that directly contradicts the lease language. Appellants explicitly say their proposed definition of pipeline describes a pipeline that does ***not*** connect to oil wells themselves. They state: "Every wellhead has one or more pipes connected to it, but very few wells, and ***none in this case, have an oil pipeline connected***." *Id.* ¶ 19 (emphasis added).[10] By contrast, the lease language in question describes a "pipeline to which the lessee ***may connect wells on said land***." App. 21 at 1, Certification Order (emphasis added). Clearly, the lease language contemplates that a "pipeline" is something that ***can*** connect to the well on the leased property. It makes no sense that the word "pipeline," as used in the phrase "pipeline to which the lessee may connect wells on said land," should be read to mean a pipeline that—by Appellants' own definition—does ***not*** "connect to wells on said land." Instead, the lease language means what it says—it describes in-kind delivery through a pipeline on the leased property that connects to the well.

[¶53] By a similar token, Appellants posit that the royalty provision does not reference delivery of the oil "on said land" and instead claim the phrase "on said land" modifies only the word "wells." Opening Br. ¶ 23. Even if one indulges that grammatical construction

[10] This statement is entirely unsupported. No factual record has been developed in this case, and as such, nothing in the record before the Court identifies whether oil pipelines are connected to the wells at issue here.

of this sentence, it makes no sense that a well "on said land" could "connect" to a pipeline in a place that is not also on that land. The provision in question is undisputedly an in-kind royalty provision. The only logical reading of an in-kind royalty provision like this one—that contemplates the delivery of oil in a pipeline that "connect[s] to wells on said land"—is that it references the delivery of oil on the leased property.[11]

[¶54] ***Second***, Appellants' comparison of the oil royalty provision with the leases' casinghead gas royalty provision requiring lessees "[t]o pay Lessor for gas produced from any oil well and used off the premises or in the manufacture of gasoline or any other product a royalty of [fractional share] of the proceeds, ***at the mouth of the well***, payable monthly at the prevailing market rate" does not change the above analysis. *See* Opening Br. ¶¶ 16, 24–25. These are two separate provisions. The oil royalty provision contemplates payment in kind, while the casinghead gas provision contemplates payment in cash. Thus, it is wholly unsurprising that the provisions are worded differently. It would be unnecessary—and redundant—for the in-kind royalty provision, which already requires delivery of a volume of oil into the pipeline that may be connected to the wells on said land, to also include the words "at the mouth of the well." As such, the allegedly "intentional contrast" between these two provisions is meaningless to the question at hand.

[11] For a similar reason, the fact that the article "the" is used in the leases ("***the*** pipeline" instead of "***a*** pipeline") actually supports ***Appellees'*** reading of the language, not Appellants'. *See id.* ¶ 22. Appellants claim that "the" indicates "the specific pipeline to which wells on this property were sent to—not simply any pipe or tube on the property." *Id.* That makes little sense. Multiple pipelines could be used to transport oil from a single well, with the lessee selling oil to different interstate pipelines in different proportions or at different times. Conversely, it is also possible that no downstream pipelines could be used at all, and truck or rail transportation could be used instead.

Id. The provisions are worded differently because they describe different things: a monetary royalty and a royalty in-kind.

[¶55] If anything, the casinghead provision favors Appellees' interpretation because it shows that ***all*** hydrocarbons are to be valued at the wellhead, rather than an inconsistent result where some hydrocarbons are valued downstream and some at the wellhead. Appellants' proposed interpretation would value casinghead gas at the wellhead, but value oil at a downstream point of sale—a result that does not comply with North Dakota's principles of contractual interpretation. *See* N.D.C.C. § 9-07-06 ("The whole of a contract is to be taken together so as to give effect to every part if reasonably practicable. Each clause is to help interpret the others."); *Markwed Excavating, Inc. v. City of Mandan*, 2010 ND 220, ¶ 20, 791 N.W.2d 22 (noting North Dakota law "require[s]" terms be "harmonized with other provisions of the contract"). Appellees' reading of the leases is not only faithful to the leases' plain language, but also harmonizes the oil and casinghead gas provisions.

[¶56] ***Third***, Appellants' argument that the phrase "free of cost" indicates that oil is not required to be valued at the wellhead is equally unavailing. Opening Br. ¶¶ 10–11. It is well-established that the phrase "free of cost, in the pipe line" signifies only "that the royalty interest is free of the costs of ***production***"—*i.e.*, the costs of extracting the hydrocarbon from below the earth and getting it to the wellhead—not the ***post***-production costs incurred after the oil leaves the wellhead. 3 Williams & Meyers, Oil and Gas Law § 642.3 (2019) (emphasis added). Production costs are not at issue in this case, and the "free of cost" language does not provide lessors a right to a ***downstream*** price.

[¶57] This interpretation, too, is supported by a long line of case law. As numerous courts have explained, "[f]ree of cost provisions are not inconsistent with allowing post-production, value-enhancing costs to be used to calculate the value of the gas at the wellhead." *Creson v. Amoco Prod. Co.*, 10 P.3d 853, 860–61 (N.M. Ct. App. 2000); *see also EQT Prod. Co. v. Magnum Hunter Prod., Inc.*, 768 F. App'x 459, 466 (6th Cir. 2019) ("[A]pplication of the at-the-well rule does not render the prohibition on deductions meaningless. Magnum Hunter remains unable to deduct ***production*** costs." (emphasis added)), *reh'g denied* (May 21, 2019); *Bounty Mins., LLC v. Chesapeake Expl., LLC*, 2019 WL 7171353, at *11 n.10 (N.D. Ohio Dec. 23, 2019) (finding that prohibition of "any deductions or expenses" did not apply to deduction of post-production costs), *appeal docketed*, No. 20-3043 (6th Cir. Jan. 9, 2020); *El Petron*, 2018 WL 1322391, at *3 (holding that "free and clear of all costs, except taxes" language permitted well operator to "consider post-production costs to determine the value of the overriding royalty" but prohibited deduction of "production costs or administrative fees"); *Molter*, 134 P.2d at 404 (permitting deduction of post-production costs under "free of cost, in the pipe line" provision); *Vedder*, 122 P.2d at 604, 602 (same); *Voshell*, 19 P.2d at 457 (same).

[¶58] Rather, under language "providing for delivery 'free of cost ***in the pipe line*** to which Operator may connect his wells,' the expense of transportation or of treating oil or gas or of compressing gas [*i.e.*, the post-production costs at issue here] to make it deliverable must be shared by the owner of the nonoperating interest." 3 Williams & Meyers, Oil and Gas Law § 646.2 (2019). Indeed, the same "free of cost, in the pipeline" language in question here was at issue in *El Petron*, and the federal district court found that the lessor could "consider post-production costs" when calculating royalty payments. 2018 WL 1322391, at *4–5. As such, the presence of the phrase "free of cost" in the leases does not change the result here.

[¶59] Furthermore, Appellants' contrary reading requires reading the "free of cost" language to the exclusion of all other language in the royalty provision—including the entire phrase "in the pipeline to which Lessee may connect wells on said land." But black-letter North Dakota law requires that each word in a contract be given meaning. *Felco, Inc. v. Doug's N. Hill Bottle Shop, Inc.*, 1998 ND 111, ¶ 12, 579 N.W.2d 576 (citing N.D.C.C. § 9-07-06). The only way to give meaning to every word in the royalty clause here is to conclude that royalty oil must be free of cost before it is placed in the pipeline on the leased property.

[¶60] Nor does the phrase "free of cost" inject an ambiguity into the lease language. Although Appellants protest that any ambiguities must be construed against the drafter and that oil companies are sophisticated actors, *see* Opening Br. ¶ 26, that rule only applies when language is susceptible to two meanings and the "uncertainty [is] not removed" by numerous preceding rules of interpretation, *see* N.D.C.C. § 9-07-19. By North Dakota law, "[w]hen a contract is reduced to writing, the intention of the parties is to be ascertained from the writing alone if possible." *Id.* § 9-07-04. Here, the meaning of the language is obvious on its face. *See supra* § II. There is no reason this Court should decline to give the royalty provision in question its plain, obvious meaning.

[¶61] Further, this canon is entirely irrelevant in any event. Appellants and *Amicus Curiae* admit that the leases at issue are standard "form contracts," either adopted or inherited by the parties. *See* Opening Br. ¶¶ 4, 22, 26 (describing "lease form" and "form contracts"); White River *Amicus Curiae* Br. ¶ 8 [Dkt. 29] (same). This squarely contradicts Appellants' claim that Appellees are sophisticated actors that intentionally drafted the lease language in question.

[¶62] The bottom line is that the "free of cost" language in the leases speaks to ***production*** costs, but the costs at issue are ***post***-production expenses incurred after the oil has left the leasehold. The requirement that oil be delivered "free of cost, in the pipeline to which Lessee may connect wells on said land" makes plain that Appellants are entitled to receive their royalty at the well. Appellants' attempt to value the royalty at a different location contradicts the language of the leases and settled precedent.

CONCLUSION

[¶63] Because the royalty provision values oil at the wellhead, this Court should answer the certified question "yes."

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CERTIFICATE OF COMPLIANCE

[¶64] The undersigned hereby certifies, in compliance with N.D. R. App. P. 32(a)(8)(A), that this Brief of Defendants-Appellees was prepared with proportional typeface, 12 pt. font, and that the total number of pages in the above Response is 37 pages.

/s/ Paul J. Forster

CERTIFICATE OF SERVICE

[¶65] On February 22, 2021, Defendants-Appellees Lime Rock Resources Operating Company, Inc., Lime Rock Resources III-A, L.P., and EOG Resources Inc.'s Brief of Defendants-Appellees was submitted to the Supreme Court of North Dakota and thereby served upon the following listed attorneys via the North Dakota Supreme Court E-Filing Portal:

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