



The battle over oil and gas royalty payments is heating up in Ohio. Late in 2016, the Ohio Supreme Court declined to answer the certified question of whether Ohio follows the “at the well” rule, or a version of the “marketable product” rule. *Lutz, et al v. Chesapeake Appalachia, L.L.C.*, 2016-Ohio-7549. In short, the “at the well” rule provides that royalties are to be calculated based upon the value of the product at the wellhead. Producers calculate the value of the product at the wellhead through a “work back” method, wherein post-production expenses are deducted from the final sale price. On the other hand, the “marketable product” rule provides that producers have an implied duty to incur all costs up until a marketable product is created.

In *Lutz*, the Ohio Supreme Court declined to set forth a steadfast rule in Ohio, instead simply holding that “an oil and gas lease is a contract that is subject to the traditional rules of contract construction.” Thus, if the language of a royalty provision is unambiguous, that language will control. What is left unknown is which rule the Ohio Supreme Court will adopt when presented with ambiguous royalty provisions.

Not surprisingly, courts in fellow Utica and Marcellus Shale states have decided issues relating to royalty payments in recent years. Pennsylvania appears to have sided with the majority of states in following the “at the well” rule. *Kilmer v. Elexco Land Servs., Inc.*, 605 Pa. 413, 990 A.2d 1147 (2010). In contrast, West Virginia adopted what may be the most producer-unfriendly rule in the country, requiring that they incur all costs up until the actual point of sale absent language setting forth with particularity which deductions are to be taken and how they will be calculated. *Leggett v. EQT Production Company*, No. 16-0136, 2016 WL 6835732 (W. Va. Nov. 17, 2016).

In Ohio, numerous lawsuits have arisen in recent months alleging the underpayment of royalties. The basis of the allegations in those suits centers on the deduction of post-production costs from royalties. As those cases are resolved in the coming months and years, it will be interesting to see whether Ohio courts follow the producer friendly path of Pennsylvania, or the producer adverse rule of West Virginia.



WILLIAM BECKLEY

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