NOTES

ASSIGNING GAS BALANCING RIGHTS IN THE ABSENCE OF A GAS BALANCING AGREEMENT

I. INTRODUCTION

When two or more working interest owners share an undivided interest in a natural gas well, it is not uncommon for production imbalances to occur. Sometimes such imbalances are remedied pursuant to a gas balancing agreement (GBA) entered into by the interest owners. However, if no GBA is entered into the common law rules of cotenancy and any other agreement between the parties will be used to cure the production imbalance.

Although cotenant-like relationships may be created by the common law of cotenancy, the parties themselves can also create such a relationship, called a contractual cotenancy, through the execution of an operating agreement. When this occurs, the rights (and duties) of the parties arise from the operating agreement, not merely from the common law rules of cotenancy. These contractual rights in the operating agreement should be assignable by the original parties to the agreement and enforceable by their assignees, unless the operating agreement specifies otherwise. Many of these rights, particularly the right to make up underproduction, should be deemed as running with the land and not as merely personal to the original parties.

However, in *Weiser-Brown Oil Co. v. Samson Resources Co.*,[1] the Court of Appeals for the Eighth Circuit held that, absent a GBA, a co-owner has no contractual right to recoup underproduction, only a right to an accounting as between cotenants, and that this right to an accounting does not run with the land to subsequent cotenants, but is only personal to the cotenant who was underproduced.[2] This note analyzes the *Weiser-Brown* decision by first addressing the common law of cotenancy and how the common law is affected by the existence of an operating agreement. The conclusion reached below is that, under an operating agreement, the right to make up underproduction, even absent a GBA, is an assignable contract right, and that this right runs with the land to inure to subsequent grantees of the original party to the operating agreement.

II. CIRCUMSTANCES UNDER WHICH PRODUCTION IMBALANCES OCCUR

A. Cotenancy

At common law, some type of cotenancy is created whenever there are two or more owners of undivided shares in the same parcel of land.[3] When

1. 966 F.2d 431 (8th Cir. 1992).
2. *Id.* at 434.
3. The cotenancy is either a tenancy in common, joint tenancy, or tenancy by the entirety. Tenancy

the parcel of land is a mineral estate, such concurrent ownership will usually create a tenancy in common.[4] In the absence of any statute[5] or agreement, if one or more of the cotenants removes minerals from the mineral estate, the rights and liabilities of all the cotenants will be governed by the common law of cotenancy applicable in that state.[6]

In England, the common law of cotenancy underwent revision in 1285 with the enactment of the Statute of Westminster II.[7] Thereafter, when one cotenant produced minerals from the land held in cotenancy, the Statute of Westminster II provided the nonproducing cotenant a choice of two remedies: partition in kind or balancing in kind.[8] The Statute of Anne was enacted in England in 1705.[9] It provided the nonproducing cotenant with another remedy in addition to partition and balancing in kind. Now the nonproducing cotenant could sue for an accounting of profits made by the cotenant who produced more than his share of the minerals from the land.[10]

Today, in the majority of states,[11] each cotenant has the non-exclusive right to produce his share of the minerals.[12] In these states, a cotenant may develop and produce the oil and gas without the consent of the other cotenants.[13] He may even assign his own interest in the well without the consent of the other cotenants, and his assignee will succeed to his rights and become a cotenant in his assignor's place.[14] However, he may not convert the interests of the other cotenants and must account to them for their respective shares of the gas produced.[15]

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by the entirety is applicable only as between spouses. Tenants in common are owners of undivided shares in the land, and there is no survivorship between them, i.e., when one dies that person's share in the property passes to his heirs or devisees. Joint tenants are also owners of undivided shares in the land, but there is survivorship between them, i.e., when one dies the other is sole owner. *See* A. JAMES CASNER & W. BARTON LEACH, CASES & TEXT ON PROPERTY 255 (3d ed. 1984). The necessary element of any common law cotenancy is the right of each cotenant to occupy the entire undivided interest in the property, i.e., unity of possession. David E. Pierce, *The Law of Disproportionate Gas Sales*, 26 TULSA L.J. 135, 140 (1990).

4. RICHARD W. HEMINGWAY, THE LAW OF OIL & GAS § 3.1, at 112 (3d ed. 1991). *See also, e.g.*, Earp v. Mid-Continent Petroleum Corp., 27 P.2d 855, 858 (Okla. 1933).

5. *See, e.g.*, Oklahoma's Natural Gas Market Sharing Act, OKLA. STAT. ANN. tit. 52, §§ 581.1-.10 (West Supp. 1993), commonly called the "Sweetheart Gas Act," which governs the rights and obligations of all interest owners in natural gas wells [hereinafter Sweetheart Gas Act].

6. Eugene Kuntz, *Gas Balancing Rights & Remedies in the Absence of a Balancing Agreement*, 35 ROCKY MTN. MIN. L. INST. 13-1, 13-5 (1989).

7. *Id.* at 13-17. Before that time a cotenant could extract minerals from the land held in cotenancy without incurring liability to the other cotenants.

8. *Id.* Note that most operating agreements preclude partition in kind. The specific provisions contained in the Model Form Operating Agreements under which the parties waive the right to partition appear as Article VIII, F in the A.A.P.L Form 610-1977; Article VIII, E in the 82 Form; and Article IX, E in the 89 Form. *Id.* at 13-20 n.39.

9. 4 Anne, ch. 16, § 27, 11 Stat. 161 (1705).

10. ROGER A. CUNNINGHAM ET AL., THE LAW OF PROPERTY § 5.8, at 220 (1984).

11. In Illinois, Louisiana, and West Virginia the production of oil and gas by one cotenant may be enjoined by another cotenant. HEMINGWAY, *supra* note 4, § 5.1, at 201.

12. He cannot exclude his fellow cotenants from doing likewise. HEMINGWAY, *supra* note 4, § 5.1, at 201.

13. Pierce, *supra* note 3, at 140.

14. Prairie Oil & Gas Co. v. Allen, 2 F.2d 566, 572 (8th Cir. 1924).

15. HEMINGWAY, *supra* note 4, § 5.1, at 202.

To review, both the right to an accounting and the right to balance in kind may be based on the common law of cotenancy. These common law rights arise from the Statute of Anne and the Statute of Westminster II respectively. The right to balance in cash, however, is not a right found in the common law of cotenancy. Nevertheless, the right to balance in cash, as well as the right to balance in kind, and to an accounting, may be based on a contractual cotenancy created by an operating agreement.

B. Operating agreement[16]

A contractual cotenancy is a cotenant type relationship created by a contract.[17] Such a contract between working interest owners may supplement and alter their common law cotenant rights, and the contract that usually does this is the operating agreement.[18] Four "Model Form Operating Agreement" versions have been used or are currently being used.[19]

Operating agreements are entered into for a variety of reasons. In most states, the common law rights of cotenants allow each cotenant to independently drill and operate a gas well, but they do not provide a basis for sharing the risks and costs of doing so.[20] The operating agreement, therefore, "is used as a means of exercising operating rights in oil and gas when they cannot be exercised effectively under the common law rights of cotenants without an agreement."[21] It provides these co-owners with a method for sharing costs and production.

The right of each working interest owner to take his share of oil and gas production in kind is provided in all of the Model Form Operating Agreements.[22] Furthermore, implied in all operating agreements is the operator's duty to conduct operations in a good and workmanlike manner, and this duty encompasses the obligation to insure that each party to the operating agree-

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16. An operating agreement is a contract between working interest owners to coordinate development of the property. It designates an operator and specifies each working interest owner's rights and obligations. Whenever there is more than one working interest owner, they will normally enter into such an agreement, often called a joint operating agreement or JOA. Pierce, *supra* note 3, at 136 n.5.

17. Pierce, *supra* note 3, at 139 n.17.

18. Pierce, *supra* note 3, at 144. A "contractual cotenancy is created by the ownership clause of the operating agreement." Pierce, *supra* note 3, at 145.

19. (1) the "Ross-Martin Form 610 Model Form Operating Agreement-1956" (56 Form); (2) the "A.A.P.L. Form 610-1977 Model Form Operating Agreement" (77 Form); (3) the "A.A.P.L. Form 610-1982 Model Form Operating Agreement" (82 Form); (4) the "A.A.P.L. Form 610-1989 Model Form Operating Agreement" (89 Form).

20. Kuntz, *supra* note 6, at 13-15. Oklahoma's Sweetheart Gas Act, *supra* note 5, does address this concern.

21. Kuntz, *supra* note 6, at 13-15.

22. Pierce, *supra* note 3, at 156. The 56 Form, *supra* note 19, § 13, at 6, provides: "Each party shall take in kind or separately dispose of its proportionate share of all oil and gas produced from the Unit Area." The 77 Form, *supra* note 19, Art. VI, C, at 6-7, provides: "Each party shall have the right to take in kind or separately dispose of its proportionate share of all oil and gas produced from the Contract Area." The 82 Form, *supra* note 19, Art. VI, C, at 7-8, provides: "Each party shall take in kind or separately dispose of its proportionate share of all oil and gas produced from the Contract Area." The 89 Form, *supra* note 19, Art. VI, G, at 11, provides: "Each party shall take in kind or separately dispose of its proportionate share of all Oil and Gas produced from the Contract Area." The language in the 82 Form and in the 89 Form is the same whether or not there is a GBA. Pierce, *supra* note 3, at 157 nn.113-14.

ment receives its proportionate share of production.[23] There seems to be two possible sources of this duty. First, a finding that the parties to an operating agreement have created a joint venture will establish a fiduciary relationship between the co-owners.[24] Second, even without such a finding, a fiduciary relation will be established if a court finds a "relationship of trust and confidence" between the parties.[25] Therefore, when a production imbalance does arise,[26] the underproduced party's right to take his share of production in kind, expressed in the operating agreement, and the operator's fiduciary duty implied therein, should give the underproduced party a right to a remedy.

Although an operating agreement usually provides that if an imbalance is created it will be balanced in accordance with an attached balancing agreement, such a balancing agreement is not always attached.[27] "[T]raditionally, gas balancing agreements have been the exception instead of the rule. Instead, working interest owners rely upon the operating agreement as the basic document that will govern their rights in production."[28] If the operating agreement is silent on the subject of balancing, the court must decide whether to apply the common law that is applicable in the absence of an agreement to balance, or to apply the common law by incorporating it in the operating agreement by implication.[29] Of course, if the common law of cotenancy is applied or incorporated in the operating agreement, an accounting or a balancing in kind would be available to the underproduced party, but not cash balancing.[30] However, if the court also incorporates into the operating agreement the industry custom and usage, then a cash balancing would also be

23. Theodore R. Borrego, *Gas Balancing Agreements - Selected Problems and Issues*, 40 INST. ON OIL & GAS L. & TAX'N 4-1, 4-12 (1989).

24. Howard L. Boigon, *The Joint Operating Agreement in a Hostile Environment*, 38 INST. ON OIL & GAS L. & TAX'N 5-1, 5-10 (1987).

25. *Id.* at 5-11. This was the case in Teel v. Public Serv. Co. of Okla., 767 P.2d 391, 396 (Okla. 1985). *See also* Beren v. Harper Oil Co., 546 P.2d 1356 (Okla Ct. App. 1975). In *Beren* the court held that even though operating agreements provide that it is not the intention of the parties to create a partnership nor to render them liable as partners, the operator still has a responsibility to the non-operators. *Id.* at 1358 (stating that he is "obligated to conduct all such unit operations in a good and workmanlike manner as would a prudent operator under the same or similar circumstances").

26. The causes of production imbalances are numerous. As in *Weiser-Brown*, the well operator may be selling gas while the non-operating co-owners are either unable to obtain gas purchase contracts or unwilling to market their shares of gas at current prices. This results in a "split-stream" sale of gas. Production imbalances caused by a split-stream sale can also occur when all the working interest owners have entered into sales contracts for their respective shares of production, but one or more of the purchasers is delayed in hooking up to the wellhead, while the other purchasers have already connected and begun taking gas. For a good discussion of these and other potential causes of production imbalances, *see* Borrego, *supra* note 23, at 4-7 to 4-9.

27. Kuntz, *supra* note 6, at 13-17.

28. Pierce, *supra* note 3, at 138. An excellent discussion of gas imbalances in the absence of a GBA is found in Edel F. Blanks, III et al., *A Primer on Gas Balancing*, 37 LOY. L. REV. 831 (1992). *See also* Doheny v. Wexpro Co., 974 F.2d 130, 133 (10th Cir. 1992) (stating that in the absence of a formal GBA, the only issue is the proper remedy to correct a production imbalance, that there is no dispute that the parties to the operating agreement must balance production); Pogo Producing Co. v. Shell Offshore, Inc., 898 F.2d 1064, 1066-67 (5th Cir. 1990) (holding that in absence of GBA, balancing in kind is the preferred method).

29. Kuntz, *supra* note 6, at 13-21.

30. *See supra* part II.A.

available.[31] In fact, industry custom and usage provide three methods of correcting production imbalances: balancing in kind, periodic cash balancing, and cash balancing upon reservoir depletion.[32] The equities of the particular case dictate which method will be applied.[33] In other words, the basis for adjusting production imbalances under an operating agreement is determined by a court on a case-by-case basis, following either a common law accounting for a proportionate share of net profits, or enforcing industry custom as an adjunct to the operating agreement and requiring cash or in kind balancing.[34]

It should be noted here that although the remedy of cash balancing bears a superficial resemblance to an accounting, they are distinct. An accounting is simply for the actual profits received by the overproduced party for what had been produced and sold, determined by the gross receipts from the sale minus the costs.[35] Cash balancing, on the other hand, is based on the value to be placed on the gas not made up, and the value to be used for cash balancing may be (1) the price actually received by the overproduced party; (2) the fair market value of the gas not taken by the underproduced party; or (3) the price that otherwise would have been received by the underproduced party.[36]

III. *WEISER-BROWN OIL CO. V. SAMSON RESOURCES CO.*[37]

A. Facts

Mobil Exploration and Producing Southeast, Inc. (Mobil) and Samson Resources Company (Samson) each owned, as lessors, an undivided fifty percent interest in a natural gas well (the Jane Scott well). An operating agreement dated June 1, 1979, was entered into by Mobil and Samson under which Samson agreed to act as operator. The operating agreement gave each party the right to take in kind or separately dispose of its proportionate share of the production. It also stipulated that in the event of disproportionate deliveries, the balancing was to be in accordance with a gas balancing agreement to be entered into separately or attached to the operating agreement;[38] however, no GBA was ever made.

Samson thereafter entered into a ten year gas purchase contract and com-

31. Kuntz, *supra* note 6, at 13-21.

32. Beren v. Harper Oil Co., 546 P.2d 1356, 1359 (Okla. Ct. App. 1975).

33. *See, e.g.*, case cited *infra* note 64.

34. Pierce, *supra* note 3, at 166.

35. Kuntz, *supra* note 6, at 13-14.

36. Patrick H. Martin, *The Gas Balancing Agreement: What, When, Why, and How*, 36 ROCKY MTN. MIN. L. INST. 13-1, 13-64 (1990).

37. 966 F.2d 431 (8th Cir. 1992).

38. The operating agreement covering the Jane Scott well provided as follows:

> Each party shall have the right to take in kind or separately dispose of its proportionate share of all oil and gas produced from the contract area. . . . In the event [of a production imbalance], the balancing or accounting between the respective accounts of the parties shall be in accordance with a Gas Balancing Agreement between the parties hereto, whether such Agreement is attached as Exhibit "E", or is a separate Agreement.

Defendant's Brief in Support of Objection and Appeal from the Magistrate's Order Compelling Production of Settlement Agreements at 4-5, Weiser-Brown v. Samson Resources Co., No. 90-2171 (W.D. Ark. filed Mar. 5, 1991).

menced delivery from the well in 1980. Mobil, on the other hand, was unable to sell its gas until 1985. Thus, Mobil was underproduced, and though it was entitled to recoup this underproduction,[39] Mobil did not do so. Instead, in 1988, Mobil conveyed its interest in the well to Weiser-Brown. The "Assignment and Bill of Sale" from Mobil to Weiser-Brown stated, in pertinent part, as follows:

> [Mobil] . . . does hereby grant, sell, convey, assign and deliver to [Weiser-Brown] . . . all of [Mobil's] right, title and interest in and to the [Jane Scott well] . . . except as hereinafter provided . . . . It is agreed between the parties that the transfer is subject to the following terms: . . . [Paragraph 4] . . . . Mobil shall be . . . entitled to all unit revenues . . . attributable to its interest in the Properties prior to the Effective Date hereof [October 1, 1988] . . . . [Paragraph 7]. Notwithstanding anything to the contrary herein, [Weiser-Brown] acknowledges and agrees to the following regarding possible gas imbalance on the Properties: a. Gas Underproduction- In the event [Mobil] is underproduced . . ., [Weiser-Brown] agrees not to hold [Mobil] liable for such underproduction. *[Mobil], however, agrees to assign all of its contractual rights to make up such underproduction.*[40]

Weiser-Brown filed its complaint against Samson on August 29, 1990, seeking an accounting for the accrued underproduction. On May 9, 1991, the district court granted partial summary judgment in favor of Samson. The district court held that Weiser-Brown could not assert a claim to the underproduction right that had accrued prior to the effective date of Mobil's assignment to Weiser-Brown because the assignment did not convey previously accrued rights to underproduction.

Weiser-Brown brought an interlocutory appeal from the district court's grant of partial summary judgment in favor of Samson. Weiser-Brown asserted that the district court erred in ruling that Mobil did not convey to Weiser-Brown Mobil's accrued right to recoup underproduction from Samson. The issue addressed by the Eighth Circuit on appeal was whether Mobil could assign and did assign to Weiser-Brown the right to recoup Mobil's accrued underproduction.

B. Decision

Interpreting the "Assignment and Bill of Sale" under the "four corners" rule,[41] the court stated that "all rights not incident to an assignment must be specifically mentioned in order to pass the right to the assignee."[42] The court found that the interest Mobil assigned to Weiser-Brown encompassed only the remaining oil and gas.[43] The court determined that paragraph seven failed to convey to Weiser-Brown the accrued underproduction because it only conveyed Mobil's contractual right to recoup. Therefore, Mobil's agreement to

39. *Weiser-Brown*, 966 F.2d at 432. The court did not specify on what grounds Mobil was entitled to recoup the underproduction, but apparently it was on the common law of cotenancy.

40. Petition for Leave to Appeal Interlocutory Order, Exhibit C, *Weiser-Brown*, No. 90-2171 (W.D. Ark. filed Jun. 12, 1991) (emphasis added).

41. A court is to determine the intention of the parties from the four corners of the instrument itself. 966 F.2d at 433.

42. *Id.*

43. *Id.* at 433-34.

assign to Weiser-Brown all contractual rights to make up the underproduction was ineffective, leaving paragraph four to govern. Paragraph four reserved to Mobil all unit revenues attributable to its interest prior to the effective date of the assignment.[44] However, the court concluded that the Jane Scott well was not covered by a GBA between Samson and Mobil. Therefore, Mobil had no contractual right to the underproduction.[45] The court held that Mobil "merely had a right to an accounting as between contenants."[46] According to the court this right to an accounting is personal to Mobil and does not run with the land to a successive tenant.[47]

IV. ANALYSIS

A. Assigning Rights Under a Contract

The district court judge in *Weiser-Brown*, in granting partial summary judgment, observed that under the law of assignments when one succeeds to a property, one does not ipso facto by virtue of that mere succession also succeed to any accrued causes of action that have to do with damage to that property. The judge then analogized to a trespass, stating that if a trespasser comes onto a person's land and does damage, then that person sells his land to another person, that other person would not take by virtue of that assignment his grantor's cause of action for trespass.[48] Trespass, however, is an action sounding in tort, and it is the general rule that the assignment of claims arising out of tort is prohibited.[49] This general rule is not applicable to actions sounding in contract, however.[50] The assignee of a claim based on a contract is not barred from maintaining the action.[51] Generally, the only causes of action that are *not* assignable or transferable are those which are founded upon wrongs of a purely personal nature, such as torts.[52] This is significant because, as already mentioned, an accounting action may be based on a contractual relationship, and so too may the remedies of in kind and in cash balancing arise from the same contractual relationship.

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44. *Id.* at 434.

45. *Id.*

46. *Id.*

47. *Id.*

48. Hearing on Motion for Summary Judgment at 9, Weiser-Brown Oil Co. v. Samson Resources Co., No. 90-2171 (W.D. Ark. filed May 9, 1991).

49. *See, e.g.*, OKLA. STAT. ANN. tit. 12, § 2017D (West 1993) ("[t]he assignment of claims not arising out of contract is prohibited").

50. *See* RESTATEMENT (SECOND) OF CONTRACTS § 317 (1981).

51. *See, e.g.*, Hoffmann v. Barnett, 178 P.2d 89 (Okla. 1946); Minnetonka Oil Co. v. Cleveland Vitrified Brick Co., 111 P. 326 (Okla. 1910); Poling v. Condon-Lane Boom & Lumber Co., 47 S.E. 279 (W. Va. 1904). *See also* 4 ARTHUR L. CORBIN, CORBIN ON CONTRACTS: A COMPREHENSIVE TREATISE ON THE WORKING RULES OF CONTRACT LAW § 860, at 420 (1951). "Contract rights are assignable; they are the subject of bargain and sale." "The effectiveness of [such] an assignment does not depend upon the assent of the obligor." *Id.* § 870, at 474.

52. CORBIN, *supra* note 51, § 886, at 560-61. Of course, the *Weiser-Brown* court did not say that claims arising from contract were not assignable. It merely held that there were none assigned or could have been assigned.

1. Right to an Accounting

When an operating agreement exists, the right to an accounting for profits does not arise solely from the common law of cotenancy. An accounting action may be based on contract, express, or implied.[53] As Professor Pierce states, contracts between parties may create cotenant-like rights and obligations, and the contract that will most often create the relationship (the contractual cotenancy) is the operating agreement.[54]

In Oklahoma, this right to an accounting is not based merely on the common law of cotenancy, as the *Weiser-Brown* court suggests. Rather, the Oklahoma legislature has expressly codified this right in the "Sweetheart Gas Act."[55] Thus, although a cotenant may lawfully produce oil and gas from the well, the underproduced cotenant still retains the right to an accounting from the overproduced cotenant.[56] Indeed, each owner who produces gas and separately sells it *must account* to each other owner not selling or otherwise disposing of gas from the well, for that owner's part of the gas being sold,[57] regardless of the nonexistence of a GBA.[58]

2. Right to Balance In Kind and In Cash

An operating agreement has been interpreted as incorporating the rights of balancing in kind and in cash.[59] In *Beren,* as in *Weiser-Brown,* the parties had executed an operating agreement but failed to make any arrangements to balance among themselves any inequalities which might result from disproportionate deliveries.[60] The *Beren* court relied on the reasoning from *Wolfe v. Texas Co.*[61] and stated:

> 1. Parties to a contract are presumed to know a well-defined trade usage generally adopted by those engaged in the business to which the contract relates. 2. Persons, who enter into a contract in the ordinary course of business, *unless the terms of the contract indicate a contrary intention,* are presumed to have incorporated therein any applicable, existing general trade usage relating to such

53. 1A C.J.S. *Accounting* § 2 (1985).

54. Pierce, *supra* note 3, at 144.

55. Oklahoma's Natural Gas Market Sharing Act, OKLA. STAT. ANN. tit. 52, §§ 581.1-.10 (West Supp. 1993).

56. *Id.* § 581.7 of the "Sweetheart Gas Act" states as follows:

> [A]n owner of a well producing natural gas or casinghead gas may produce from the well that amount of gas which may be lawfully produced therefrom; however, the foregoing shall not diminish the rights of each owner against an overproduced owner by reason of such production, such as the right to an accounting as among co-owners and the right to balance in cash or in kind, as those rights may otherwise be established by law or contract.

57. Gadsco, Inc. v. TXO Prod. Corp., 840 P.2d 1270, 1273 (Okla. Ct. App. 1992).

58. *See, e.g.*, Heiman v. Atlantic Richfield Co., No. 70739, 1993 WL 20229 (Okla. Feb. 2, 1993) (reasoning that in the absence of a GBA, the "Sweetheart Gas Act" gives parties to an operating agreement who do not market their gas the right to balance from the proceeds received from the marketing owners).

59. *See* Beren v. Harper Oil Co., 546 P.2d 1356 (Okla. Ct. App. 1975). This case was decided before the enactment of the "Sweetheart Gas Act," which incorporates in kind and cash balancing by statute. Although an Oklahoma appellate court decision has limited precedential weight, this case was cited with approval by the federal district court in United Petroleum Exploration, Inc. v. Premier Resources, LTD., 511 F. Supp. 127, 130 (W.D. Okla. 1980).

60. *Beren*, 546 P.2d at 1358.

61. 83 F.2d 425, 429 (10th Cir. 1936).

business.[62]

According to the *Beren* court, the industry custom and usage is to permit balancing in kind, except upon well depletion when cash balancing is proper.[63]

Although the underproduced party may petition for one or the other kind of relief, a court will decide based on the equities of the case.[64] Nevertheless, as one commentator has stated, the important point is that even "in the absence of a gas balancing agreement, it seems clear that an underproduced party's right to take its proportionate share of production in kind [pursuant to the operating agreement][65] should give the underproduced party a *contractual right* to balance its underproduction."[66]

The *Weiser-Brown* court held that absent a GBA, a co-owner in a natural gas well has no contractual right to the underproduction even though he is a party to an operating agreement covering the well. This holding conflicts with the common interpretation of operating agreements given by commentators and courts. Such a cotenant has one of three contractual rights to underproduction arising under an operating agreement: accounting, in kind balancing, and cash balancing. Such rights, being based on contract, are all assignable and will pass on assignment so long as all the parties so intend.

3. Intent of the Parties

Even though the weight of authority holds that an underproduced party has a contractual right arising from the operating agreement to make up the underproduction, and that this right is assignable, a party claiming to be the assignee of that right may still face obstacles to recovery. These obstacles are based on the intent of the parties. First, and, in this author's view, foremost, it can be asserted that the parties to the operating agreement intended for a GBA to provide the exclusive means for gas balancing, and that therefore, there is no contractual right to balance arising from the operating agreement. Furthermore, even if a court finds that a contractual right to correct production imbalances exists under the operating agreement, it can still be asserted that the parties to the operating agreement intended to make such a right nonassignable. Finally, even if a court determines that the parties to the operating agreement did not intend for the right to balance production imbalances to be nonassignable, the question might arise as to whether this right was in fact assigned.

As to the first obstacle, the rights to an accounting as well as to balance in cash or in kind arise from the operating agreement by incorporating therein

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62. *Id.* (emphasis added).

63. *Beren,* 546 P.2d at 1359. There are two types of cash balancing, periodic cash balancing and cash balancing upon reservoir depletion. *Id.*

64. *See, e.g.*, Doheny v. Wexpro Co., 974 F.2d 130 (10th Cir. 1992) (plaintiff sought cash balancing; court awarded in kind balancing instead); Pogo Producing Co. v. Shell Offshore, Inc., 898 F.2d 1064 (5th Cir. 1990) (plaintiff denied cash balancing; awarded in kind balancing); United Petroleum Exploration, Inc. v. Premier Resources, Ltd., 511 F. Supp. 127 (W.D. Okla. 1980); Amoco Prod. Co. v. Thompson, 516 So. 2d 376 (La. Ct. App. 1987); *Beren*, 546 P.2d 1356.

65. *See supra* note 22.

66. Borrego, *supra* note 23, at 4-19 (emphasis added).

the common law of cotenancy and the industry custom and usage, when the operating agreement is silent on the subject of balancing.[67] Therefore, it might be asserted that if the operating agreement is not silent on the subject of balancing, but rather contains a clause expressly stating that any balancing shall be in accordance with any GBA entered into separately between the parties to the operating agreement,[68] that this term indicates a contrary intention on the part of the parties not to incorporate the common law of cotenancy nor industry custom and usage into the operating agreement.[69] However, if no such GBA is ever in fact entered into, that clause should not be deemed as indicating such a contrary intention. That is because this is a boiler plate clause incorporated in all the 77 Form, 82 Form, and 89 Form Operating Agreements,[70] and it is not uncommon for the parties to ignore it.[71] The operating agreement, therefore, gives an underproduced party the right to an accounting or the right to make up the underproduction by balancing in kind or in cash. The effect of a GBA is to supersede these rights with its own terms.[72] Only in such cases where an unambiguous GBA exists would "the parties be limited to the specific remedies set forth in the [GBA]."[73] When there is no GBA, however, these rights are not superseded, and the underproduced party to the operating agreement can assert any one of these rights, limited only by equity.

Second, even if a contractual right to underproduction exists under the operating agreement, the assignee of that right may still face a challenge that the parties to the operating agreement intended for this right to be nonassignable. The question of assignability of a contract or the rights under a contract is governed by the presumption that if a contract was to be nonassignable, the parties thereto would have so expressly provided; if not so provided then it is to be considered assignable.[74] The operating agreement executed between Samson and Mobil stipulated that it was to be binding upon the parties' assigns.[75] The general rule is that "the use of such terms as heirs, successors,

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67. *See supra* text accompanying notes 29-31.

68. The *Weiser-Brown* operating agreement contained such a clause. *See supra* note 38.

69. Persons who enter into a contract in the ordinary course of business are presumed to have incorporated therein any applicable, existing general trade usage relating to such business, "*unless the terms of the contract indicate a contrary intention.*" *Beren*, 546 P.2d at 1358 (emphasis added).

70. *E.g.*, Article VI, C, at 8 of the standard 82 Form provides:

> In the event one or more parties' separate disposition of its share of the gas causes split-stream deliveries to separate pipelines and/or deliveries which on a day-to-day basis for any reason are not exactly equal to a party's respective proportionate share of total gas sales to be allocated to it, the balancing or accounting between the respective accounts of the parties shall be in accordance with any gas balancing agreement between the parties hereto, whether such an agreement is attached as Exhibit "E", or is a separate agreement.

71. Kuntz, *supra* note 6, at 13-17.

72. *See, e.g.*, Chevron U.S.A., Inc. v. Belco Petroleum Corp., 755 F.2d 1151, 1154 (5th Cir. 1985), *cert. denied*, 474 U.S. 847 (1985) (reading the GBA as providing the exclusive means of bringing the parties back into balance).

73. Borrego, *supra* note 23, at 4-26 to 4-28.

74. *See, e.g.*, Earth Products Co. v. Oklahoma City, 441 P.2d 399, 404-05 (Okla. 1968).

75. Defendant's Objection and Appeal from the Magistrate's Order Compelling Production of Settlement Agreements at 2, Weiser-Brown Oil Co. v. Samson Resources Co., No. 90-2171 (W.D. Ark. filed Mar. 5, 1991). The same language is present in all the Model Form Operating Agreements. *See, e.g.*, 77 Form, Art. XVI.

and assigns, indicates that it was the intention of the parties that the contract should be assignable."[76] It is also a matter of public policy that the assigning of choses in action as well as account and contract rights be recognized as effective.[77]

Finally, the question may arise whether this right was in fact assigned. The question of whether a contract right was in fact assigned is governed by the rule that "only those rights are passed by assignment that are incident thereto, and all other rights . . . must be specifically mentioned to pass to the assignee."[78] Operating agreements provide all owners the right to take in kind or to separately dispose of their proportionate share of all oil and gas produced from the well.[79] It should be needless to say that incident to this right are the contractual rights, mentioned above,[80] to recoup an owner's proportionate share when that owner becomes underproduced. Therefore, when the assignment-bill of sale from Mobil to Weiser-Brown[81] assigned to Weiser-Brown all rights, title, and interest in the Jane Scott well, the rights to make up the accrued underproduction were incident to that assignment. Moreover, in this case, in paragraph seven Mobil's contractual right to accrued underproduction was specifically mentioned to pass to Weiser-Brown.[82] In conclusion, Mobil had a contractual right to the accrued underproduction arising from the operating agreement and could have and did assign this right to Weiser-Brown.

B. Covenants Running with the Land

The *Weiser-Brown* court ruled that absent a GBA an underproduced co-owner merely has a right to an accounting based on the common law of cotenancy,[83] and that this right is personal to that co-owner and does not run with the land to successive co-owners.[84] Covenants running with the land achieve the transfer of rights in a way not permitted by traditional contract law. The common law action of account can be maintained so long as there is privity

76. *Earth Products*, 441 P.2d at 405.

77. *See, e.g.*, American Bank of Commerce v. City of McAlester, 555 P.2d 581, 584 (Okla. 1976) (stating that "as accounts and contract rights have become the collateral which secures an ever increasing number of financing transactions, it has been necessary to reshape the law so that these intangibles, like negotiable instruments and negotiable documents of title, can be freely assigned").

78. Wasson v. Taylor, 87 S.W.2d 63, 65 (Ark. 1935).

79. *See supra* note 22.

80. The right to an accounting, right to balance in kind, right to balance in cash.

81. *See supra* text accompanying note 40.

82. Of course, paragraph seven of the assignment (assigning to Weiser-Brown Mobil's contractual rights to make up underproduction accruing prior to the assignment) must be reconciled with paragraph four (providing that Mobil retains the rights to all revenues attributable to its interest in the well prior to assignment). A general rule of contract interpretation would give effect to paragraph seven. *See* RESTATEMENT OF CONTRACTS § 236 (1932) (stating that "[w]here there is an inconsistency between general provisions and specific provisions, the specific provisions ordinarily qualify the meaning of the general provisions"). However, the *Weiser-Brown* court ruled that even if the parties did intend to assign the contractual rights to the underproduction, there were no such rights legally assignable due to the absence of a GBA. Hence, the court held that paragraph four of the assignment governed by default. The court, therefore, never deemed it necessary to reconcile the two clauses.

83. *Weiser-Brown*, 966 F.2d at 434 (stating that Mobil "merely held a right to an accounting as between co-tenants").

84. *Id.*

between the parties,[85] and the law recognizes two kinds of privity: privity of contract and privity of estate. This section is concerned with the latter.

1. Elements

In contract law, rights and benefits may be assigned. In property law, rights and benefits are not assigned, but inure to remote persons because they acquire an interest in property that carries the rights and benefits with it.[86] In oil and gas law, the designated operator under an operating agreement has a duty to ensure that each party to the operating agreement receives its proportionate share of production.[87] This implied duty should be held to constitute a covenant whose benefit runs with the land,[88] that benefit being the underproduced party's right to its proportionate share.[89]

A covenant running with the land[90] is "a covenant which goes with the land, as being annexed to the estate, and which cannot be separated from the land, and transferred without it."[91] A covenant is said to run with the land when not only the original covenanting parties, but each successive owner of the land will be entitled to its benefit, or be liable to its burden, as the case may be.[92] To be enforceable, (1) the covenant must be intended by the original parties to run with the land, (2) it must touch and concern the land with which it runs, and (3) privity of estate must exist between the party claiming the benefit and the party who rests under the burden.[93]

The first element, intent by the original parties that the covenant runs with the land, is met in this case. The operating agreement between Mobil and Samson stated that it will be binding on the owners' assigns.[94] "Express provisions binding a party's heirs and assigns evidence an intention to create a covenant running with the land."[95]

The second element, that the covenant must touch and concern the land, is also met. The right to an accounting, arising from the disproportionate removal of value from the land without compensation to the injured party, so touches and concerns the land itself that it should run with the land. If a

85. 1A C.J.S. *Accounting* § 4 (1985).

86. CUNNINGHAM, *supra* note 10, § 8.13, at 468.

87. *Beren*, 546 P.2d at 1358. *See also* Borrego, *supra* note 23, at 4-12.

88. Although this is an affirmative, rather than a restrictive covenant, "the weight of authority permits affirmative covenants to run with the land." 7 GEORGE W. THOMPSON, COMMENTARIES ON THE MODERN LAW OF REAL PROPERTY § 3153, at 78 (repl. by John S. Grimes 1962).

89. While implied covenants are not favored in the law, the Oklahoma Supreme Court has held that this does not mean that covenants may never be implied from written agreements. Mercury Inv. Co. v. F.W. Woolworth Co., 706 P.2d 523 (Okla. 1985). *See also* THOMPSON, *supra* note 88, § 3159, at 100 (stating that "[a] restrictive covenant will not be implied unless such appears to be the presumed intention of the parties").

90. Also called a real covenant.

91. Jones v. Rock Island Improvement Co., 510 P.2d 1405, 1406 (Okla. Ct. App. 1973).

92. *Id.*

93. Noyes v. McDonnell, 398 P.2d 838, 840 (Okla. 1965). *See also* THOMPSON, *supra* note 88, § 3155 (Supp. 1981) (adding that "the promisee must benefit from the use of some land possessed by him as a result of the performance of the promise").

94. *See supra* note 75.

95. 21 C.J.S. *Covenants* § 26 (1990).

covenant is incident to the property assigned or conveyed, and affects its value, then it will run with the land.[96]

The third element, requiring privity of estate, is also met. Privity of estate requires both vertical privity between the promisee (Mobil) and his successor (Weiser-Brown), and horizontal privity between the promisor (Samson) and the promisee (Mobil).[97] Vertical privity exists as to benefits, when the subsequent owner succeeds to the promisee's estate or to a lesser estate carved out of that estate.[98] On the question of horizontal privity, most jurisdictions hold that it is not required for the benefit of a covenant to run.[99]

Therefore, it seems clear that when Weiser-Brown succeeded to Mobil's interest in the Jane Scott well, Weiser-Brown acquired the common law right to sue for an accounting for any underproduction accruing after the assignment. The question is whether its right to sue for an accounting may be maintained for underproduction accruing prior to the assignment for which its assignor, Mobil, had such a right.

2. Breach of Covenant Running with the Land

In most states, a transfer of land after breach of a covenant running with the land does not carry damages, because damages do not run with the land or inure to the benefit of subsequent grantees.[100] Once a covenant is broken it ceases to run with the land and becomes a mere personal covenant.[101] In other words, it becomes a chose in action, which has been defined as a personal right.[102] Nonetheless, a personal right is synonymous to a contract right,[103] and contract rights are assignable.[104]

In this case, as explained above, the right to an accounting and to in kind

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96. THOMPSON, *supra* note 88, § 3152, at 71. *See also* 21 C.J.S. *Covenants* § 28 (1990):

> The question whether a covenant will or will not run with the land does not depend so much on whether it is to be performed on the land itself as on whether it tends directly or necessarily to enhance its value or render it more beneficial and convenient to those by whom it is owned and occupied, and if this be the case, every successive assignee of the land will be entitled to enforce the covenant.

97. ROGER A. CUNNINGHAM ET AL., THE LAW OF PROPERTY §§ 8.17-.18 (1984).

98. *Id.* § 8.17.

99. *Id.* § 8.18. *See also* RESTATEMENT OF PROPERTY § 548 (1944): "It is not essential to the running of the benefit of a promise respecting the use of land of the promisee or *other person entitled to the benefit of the promise* that there be any privity between the promisor and the promisee other than that arising out of the promise." (emphasis added).

100. *See, e.g.*, Gulf Coal & Coke Co. v. Musgrove, 70 So. 179, 182 (Ala. 1915).

101. THOMPSON, *supra* note 88, § 3154, at 82. *But see* Cheves v. City Council of Charleston, 138 S.E. 867, 869 (S.C. 1927) (holding that "the right of an assignee to sue on a covenant broken, prior to the conveyance, is allowed").

102. Gibbons v. Tenneco, Inc., 710 F. Supp. 643, 648 (E.D. Ky. 1988).

103. CORBIN, *supra* note 51, § 860, at 420 (stating that contract rights are rights *in personam*, not *in rem*).

104. CORBIN, *supra* note 51, § 860, at 420 and *Gibbons*, 710 F. Supp. at 648 (holding that "[w]hile a chose in action does not run with land, it can be specifically assigned"). *See also* 21 C.J.S. *Covenants* § 35 (1990):

> A real covenant which has been broken ceases to run with the land and becomes a mere chose in action, and *unless such right is assignable and is expressly assigned*, it does not, as a general rule, pass with a transfer of land so as to enable a remote grantee to sue thereon. (emphasis added).

and cash balancing, arising from the operating agreement, were assignable contract rights. In the conveyance from Mobil to Weiser-Brown, Mobil's contractual rights to the accrued underproduction were expressly assigned in paragraph seven of the assignment. While the *Weiser-Brown* court held that a right to an accounting does not run with the land, this language was too broad, for a right to an accounting does run with the land, and it allows subsequent assignees to sue on it for underproduction accruing after the assignment. It is only when underproduction accrues before the assignment that the right to an accounting for that underproduction remains personal to the assignor. Nonetheless, in this case, that should still not have prevented Weiser-Brown from bringing that action in its own right because the right to an accounting was assigned to Weiser-Brown.

V. CONCLUSION

The court in *Weiser-Brown* held that absent a GBA, a co-owner in a natural gas well has no contractual right to make up any underproduction that might occur. The court reached this holding despite the presence of an operating agreement providing each co-owner the right to take his proportionate share of production; despite the operator's duty to insure that each co-owner receives its proportionate share of production; despite the custom and usage in the industry to provide in kind and in cash balancing when a co-owner is underproduced; and despite precedent and authority that incorporates in kind and in cash balancing as well as the right to an accounting into the operating agreement. The court also held that the right to an accounting based on the law of cotenancy did not pass to Weiser-Brown, but remained personal to Mobil. While this is true as to the accrued underproduction, the right to a common law accounting does run with the land insofar as underproduction accrues subsequent to the assignment. If *Weiser-Brown* serves as precedent, it would indeed threaten every present co-owner to an operating agreement who is underproduced and without a GBA. If, under an operating agreement, a co-owner has only the common law right to an accounting when a gas imbalance occurs, as the *Weiser-Brown* court holds, on what basis could an underproduced co-owner, or his assignee, seek balancing in kind or in cash when no GBA exists?

Mickey S. Moon