

**IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF OKLAHOMA**

CHIEFTAIN ROYALTY COMPANY,)	
)	
Plaintiff,)	
)	
v.)	No. CIV-11-212-R
)	
QEP ENERGY ENERGY COMPANY,)	
)	
Defendant.)	

ORDER

This matter comes before the Court on the Motion for Judgment on the Pleadings, filed by Defendant, QEP Energy Company, pursuant to Federal Rule of Civil Procedure 12(c). Plaintiff, Chieftain Royalty Company responded in opposition to the motion. Having considered the parties' submissions, and in light of prior rulings of this Court in separate but factually-similar litigation of which the parties are well aware, the Court finds as follows.

Plaintiff filed this putative class action alleging that Defendant operates certain oil and gas wells in Oklahoma in which Plaintiff and other class members own royalty interests. Plaintiff seeks relief on theories of breach of contract, tortious breach of contract, breach of fiduciary or quasi-fiduciary duty, fraud, conversion, conspiracy, and seeking an accounting, as well as injunctive relief and damages.¹ Defendant seeks judgment on the pleadings on certain of Plaintiff's claims. .

The Court analyzes a motion for judgment on the pleadings under Rule 12(c) using

¹ Plaintiff also alleges that Defendant was unjustly enriched by its actions, although it does not include a separate cause of action entitled "unjust enrichment."

the same standard as it would for a Rule 12(b)(6) motion to dismiss. *Park Univ. Enters., Inc. v. Am. Cas. Co. of Reading, PA*, 442 F.3d 1239, 1244 (10th Cir.2006). Accordingly, Plaintiff's well-pleaded factual allegations are accepted as true and are considered in the light most favorable to Chieftain. *Tomlinson v. El Paso Corp.*, 653 F.3d 1281, 1285–86 (10th Cir.2011). The Court need not accept legal conclusions as true. *Kansas Penn Gaming, LLC v. Collins*, 656 F.3d 1210, 1214 (10th Cir.2011) (citing *Ashcroft v. Iqbal*, 129 S.Ct. 1937, 1949–50)). Additionally, when considering a motion under 12(b)(6) or 12(c), the court may not consider matters outside the pleadings without treating the motion as one for summary judgment. *See Fed.R.Civ.P. 12(d)*.

Defendant first argues that there is no basis in Oklahoma law for concluding that it owed a fiduciary duty to Plaintiff by virtue of its status as operator of oil and gas wells in Oklahoma. Defendant bases its argument in part on *Howell v. Texaco, Inc.*, 112 P.2d 1154, 1160-61 (Okla. 2004), wherein the court held that a lessee does not owe a fiduciary duty to its lessors solely by virtue of the lease. The Court has acknowledged this decision in other cases cited by the parties to this action. However, the parties are equally aware of the Court's prior order in *Naylor Farms v. Anadarko OGC Co.*, Case No. CIV-08-668-R (July 14, 2011), wherein the Court held that a fiduciary relationship between an operator and the royalty owners arises by operation of law when a drilling and spacing unit exists pursuant to Okla. Stat. tit. 52 § 87.1. In an Order dated July 8, 2011, the Court concluded

In *Leck v. Continental Oil Co.*, 800 P.2d 224 (Okla. 1989), in which the Oklahoma Supreme Court recognized that an operator of a drilling and spacing unit under Section 87.1 owes a fiduciary duty to royalty owners and lessees

within the drilling and spacing unit, the court cited and obviously found persuasive the decisions in *Young v. West Edmond Hutton Lime Unit*, 275 P.2d 304 (Okla. 1954) and *West Edmond Hunton Lime Unit v. Young (Young II)*, 325 P.2d 1047 (Okla. 1958) holding that the relationship between the unit and its operator under Okla. Stat. tit. 52, § 286.1, *et seq.*, the predecessor statute to Okla. Stat. tit. 52, § 287.1 *et seq.*, and the royalty owners is fiduciary in nature. *Young I*, 275 P.2d at 309; *Young II*, 325 P.2d at 1052. The Oklahoma Supreme Court in *Young I* held that the unit operator in that case breached its fiduciary or trustee-type duties to the royalty owners by failing to obtain the best or highest price available for the unit production. *Young I*, 275 P.2d at 306-07, 310. Although the operator was authorized to purchase oil production from the unit, the Court concluded that the unit operator's conduct gave rise to the breach of its fiduciary or trustee-type duty by realizing a profit "at the direct loss to the royalty owners affected." *Id.* at 310. The Court's holding in *Young I* is consistent with a basic tenet of the law governing fiduciary and trustee relationships which precludes a fiduciary from acting for its self-interest at the expense of its principal.

Section 87.1(e) provides that "each royalty interest owner shall share in all production from the well or wells drilled within the unit . . . to the extent of such royalty interest owner's interest in the unit," Okla. Stat. tit. 52, § 87.1(e), determined by the royalty owner's proportionate acreage in relation to the total acreage within the unit. *See id.*; *see also Ward v. Corporation Commission*, 501 P.2d 503, 507 (Okla. 1972), *Shearn v. Ward Petroleum Corp.*, 808 F.Supp. 15309, 1534 (W.D. Okla. 1992). In *Ward*, the Oklahoma Supreme Court stated expressly what is implicit in Okla. Stat. tit. 52, § 87.1(e): "The operation [of the unit] is free of costs to them [the royalty owners and overriding royalty owners under the oil and gas lease or leases]." *Ward v. Corporation Commission*, 501 P.2d at 507. Finally, the Oklahoma Court of Civil Appeals in *Hebble v. Shell Western E & P, Inc.*, 238 P.3d 939 (Okla. Civ. App 2010), *cert. denied* (Okla. 2010) held that the unit operator of either a secondary recovery unit created under Okla. Stat. tit. 52, § 287.1 *et seq.* or of a drilling and spacing unit under Okla. Stat. tit. 52, § 87.1 "owed a fiduciary duty to Owners to properly account for and distribute oil and gas proceeds from the units." *Hebble*, 238 P.3d at 943. The owners in *Hebble* were successors to a net profits interest reserved in the assignment of an oil and gas lease which lease the operator had acquired. 238 P.3d at 941. A net profits interest is or is treated as a royalty interest. *See Hebble*, 238 P.3d at 943 n. 2.

Based upon the case law and statute discussed above, the Court concludes that Defendant QEP as the operator of drilling and spacing units in which the 18 class wells were drilled had a fiduciary duty to calculate and pay royalties to

each royalty owner class Plaintiff based upon all production from each well drilled within each unit, according to each royalty owner's proportionate acreage in relation to the total acreage within the drilling and spacing unit; to calculate and pay royalties to each royalty owner based upon the gross proceeds or income derived from the sale of all unit production; and to calculate and pay royalties to the royalty owner class Plaintiffs free of or unreduced by any costs of drilling, development, operations and marketing costs. Based upon the facts which are undisputed herein, reasonable jurors could find that Defendant QEP breached these duties by failing to calculate and pay royalties to the royalty owner class Plaintiffs based upon the amounts for which DCP sold the residue gas and NGLs, unreduced by the amounts retained by DCP and not remitted to Defendant QEP, to the benefit of Defendant QEP and to the loss of the royalty owner class Plaintiffs. Plaintiffs' claims for additional royalties do not lie outside the scope of Defendant QEP's fiduciary duties as operator of the drilling and spacing units in which the class wells are located and from which production has been sold. If Defendant QEP received \$9,000 from DCP for production attributable to a well within a unit pursuant to a 90% POP contract, Defendant QEP could have calculated and paid royalty based upon \$10,000 and retained and paid working interest owners from the remaining amount received from DCP.

Order at p. 3-5 (footnote omitted). In this case, Plaintiff alleged in the petition that Defendant QEP is the operator or markets natural gas as a non-operator in certain wells in Oklahoma in which Plaintiff owns a royalty interest. Plaintiff further alleges Defendant has underpaid royalty by taking improper deductions, including fees for marketing, gathering, compression, dehydration, processing, and treatment, by not paying royalty on wellhead gas that is used off the lease premises, and by not paying royalty on condensate that dropped out of the gas stream. Petition ¶ 13. Plaintiff contends Defendant was in a fiduciary relationship with the class members created by orders of the Oklahoma Corporation Commission.

The Court finds that these allegations are sufficient to withstand Defendant's motion. The Court has found on at least two prior occasions that a drilling and spacing unit pursuant

to § 87.1 creates a fiduciary duty, and in at least one prior case the Court has concluded that the fiduciary duty extends to payment of royalty in a proper manner. Although Defendant attempts to distinguish its motion as arguing about the scope of the fiduciary duty rather than the existence thereof, the Court has previously rejected an attempt to limit the fiduciary duty of a unit operator under the facts alleged herein. The Court declines Defendant's invitation to reconsider its prior decisions. Defendant's motion for judgment on the pleadings with regard to Plaintiff's breach of fiduciary duty claim is denied.

Defendant also seeks judgment on Plaintiff's claim for unjust enrichment. In support of this argument Defendant relies on this Court's prior order in *Chieftain v. Dominion Oklahoma Texas Exploration & Production, Inc.*, CIV-11-344-R (Order July 14, 2011), wherein the Court concluded that Plaintiff failed to sufficiently allege a claim for unjust enrichment. Defendant further relies on the Court's language in that order that "where an enforceable express contract governs the parties' relationship, quasi-contractual remedies such as unjust enrichment are not available" and Defendant argues Plaintiff has not established that it lacks adequate statutory or legal remedies so as to invoke the Court's equity jurisdiction. Plaintiff responds by noting that alternative pleading is permissible under the Federal Rules of Civil Procedure, and that it has adequately alleged a claim for unjust enrichment.

The Court notes that this case differs in its pleading from the prior *Chieftain* litigation. Specifically, there, unlike here, *Chieftain* pled that it had a contractual relationship with the defendant. In this case, although Plaintiff includes a cause of action for breach of contract,

it did not plead the existence of a contract or facts from which the Court can infer that it had a lessor-lessee or other contractual relationship with Defendant. Accordingly, the Court finds that the outcome of *Chieftain v. Dominion* is not controlling here, because Plaintiff did not allege in the petition that it had a contractual relationship with QEP. The Court further finds that the allegation that QEP retained monies to which it was not entitled is sufficient to allege a claim for unjust enrichment, because Plaintiff has alleged that "defendant either retained a benefit or avoided an expense, and that, as a result, the plaintiff suffered a detriment." *N.C. Corff Partnership, Ltd. v. Oxy USA, Inc.* 929 P.2d 288, 295 (Okla.Ct.App. 1996)(citing *Teel v. Public Serv. Co. of Oklahoma*, 767 P.2d 391, 398 (Okla. 1985)(superseded by statute on other grounds). The Court concurs with the result advocated by Plaintiff, and the motion is denied with regard to Plaintiff's unjust enrichment claim.

Defendant next argues it is entitled to judgment on Plaintiff's claim for tortious breach of contract, because this claim is based on the "bare allegation that 'QEP's actions amount to much more than a simple breach of contract.'" Motion at p. 8 (quoting Pet. ¶ 34). As noted above, Plaintiff has not pled the existence of a contract with QEP, and therefore, the Court cannot conclude that Plaintiff has alleged that Defendant violated the implied duty to deal fairly and in good faith in the performance of that contract. Defendant's motion for judgment on the pleadings is therefore granted with regard to this claim.

Defendant also asserts it is entitled to judgment on Plaintiff's claim for conversion. Plaintiff urges the Court to reconsider its determination in earlier cases that conversion claims are inappropriate with regard to allegations of underpayment of royalties, citing to

Okla. Stat. tit. 52 § 570.10. Plaintiff argues the Court should adopt the position set forth in a November 2008 opinion of the Oklahoma Attorney General, 2008 OK AG 31, 2008 WL 4860573, which concluded that the proceeds of the sale of oil and gas attributable to a royalty owner are held in trust for the royalty owner by the operator. The Court has rejected this argument in prior cases, including *McKnight v. Linn Operating, Inc.*, Case No. CIV-10-30-R (April 1, 2010) [Doc. No. 33] and *Naylor Farms v. Anadarko OGC Company*, Case No. CIV-08-668-R (June 23, 2011) [Doc. No. 198].

In its most recent pronouncement on the issue, the Court stated:

[U]pon reconsideration, the Court is persuaded that the analysis of § 570.10(A) by the District Court in Delaware in *In re Sem Crude L.P.*, 407 B.R. 140 (D.Del. 2009) was correct and that the opinion of the Oklahoma Attorney General, Atty Gen. Op., 2008 OK AG 31, 2008 WL 4860573 at *10 (Nov. 5, 2008) was incorrect.

Section 570.10(A) states, in part, as follows: “Nothing in this subsection shall create an express trust.” So the only type of trust that could be created by § 570.10(A) would be an implied trust. However, Defendant QEP is correct that under Oklahoma law, implied trusts are trusts created by operation of law and are of two species, resulting trusts and constructive trusts. *Powell v. Chastain*, 318 P.2d 859, 862 (Okla. 1957); *Johnson v. Johnson*, 201 Okla. 268, 205 P.2d 314, 318 (Okla. 1949). Both resulting and constructive trusts are equitable remedies designed “to prevent wrongful taking of unlawful holding of property.” *Wooten v. Melton*, 631 P.2d 1337, 1341 (Okla. Civ. App. 1981); *See Goodwin v. Beard*, 343 P.2d 192, 196 (Okla. 1967); *Powell v. Chastain*, 318 P.2d at 862. “A constructive trust may be implied by law when one, through some manner of wrongdoing – e.g. fraud, abuse of confidence, or trick – obtains title to property.” *Wooten v. Melton*, 631 P.2d at 1341. “A resulting trust . . . may be judicially imposed on one holding legal title to property if it was obtained under facts and circumstances disclosing an intention that the beneficial interest was not to be enjoyed by the legal title holder.” *Id.* Not only is the law in Oklahoma that implied trusts are resulting and constructive trusts, but this is the prevailing usage of the term “implied trusts” in courts everywhere and by treatises. *See e.g., R. Chester, G. Bogert and G. Bogert,*

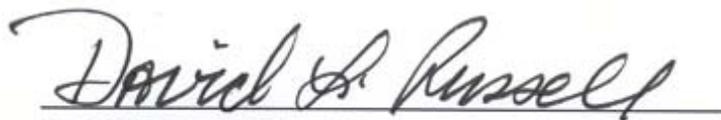
The Law of Trusts and Trustees, § 451 at p. 280 (3rd ed. 2005). Accordingly, § 570.10(A) cannot be said to create an implied trust.

Naylor Farms, Case No. CIV-08-668-R (Order June 23, 2011). The Court continued on to distinguish *Reserve Oil v. Dixon*, 711 F.2d 951 (10th Cir. 1983), before concluding that there was no implied trust or trustee relationship between the party holding proceeds of production and royalty owners. Although Plaintiff urges the Court to reconsider this decision, the Court declines to amend its prior determinations that conversion is not an appropriate claim under the circumstances alleged by Plaintiff in this petition. Defendant's motion for judgment on the pleadings is granted with regard to Plaintiff's conversion claim.

Finally, Defendant argues the Court should dismiss claims against "predecessors, successors and affiliates." In response Plaintiff states it will voluntarily dismiss those unidentified parties, rendering the motion moot. Accordingly, Defendant's motion is denied in this regard as moot.

For the reasons set forth herein, Defendant's motion for judgment on the pleadings is granted in part and denied in part. Specifically Defendant is entitled to judgment on Plaintiff's claims of tortious breach of contract and conversion and denied with regard Plaintiff's claims for breach of fiduciary duty and unjust enrichment.

IT IS SO ORDERED this 27th day of January, 2012.



DAVID L. RUSSELL
UNITED STATES DISTRICT JUDGE

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U.S. District Court

Western District of Oklahoma[LIVE]

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