

**UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION**

REGIS F. LUTZ, et al.,)	CASE NO. 4:09-cv-2256
)	
)	
PLAINTIFFS,)	JUDGE SARA LIOI
)	
vs.)	
)	
CHESAPEAKE APPALACHIA, L.L.C.,)	
)	
)	
DEFENDANT.)	

ORDER CERTIFYING QUESTION TO OHIO SUPREME COURT

Pursuant to Rule 9 of the Rules of Practice of the Supreme Court of Ohio, this Court respectfully certifies a question to the Supreme Court of Ohio.

1. Name of Case

Lutz, et al. v. Chesapeake Appalachia, L.L.C., No. 4:09-cv-02256 (N.D. Ohio).

2. Statement of Facts

This case is a putative class action in which plaintiffs (landowner-lessors) claim that defendant (lessee) underpaid their gas royalties under the terms of their respective leases. It is undisputed that the lessee (and working interest holders) bear all production costs—*i.e.*, the costs of producing gas from below-ground and bringing it to the wellhead. The dispute centers on post-production costs—*i.e.*, the costs incurred after the gas is produced at the wellhead and before it is sold farther downstream. Those post-production costs may include the cost of gathering the gas from various wells, the cost to process and compress the gas, and the cost of transporting the gas to the point of sale, among others. At issue is whether defendant is permitted

to deduct post-production costs from plaintiffs' royalties and, if so, how those costs are to be calculated.

The leases of the named plaintiffs have the following three variant royalty clauses.

[1] The royalties to be paid by Lessee are... (b) on gas, including casinghead gas or other gaseous substance, produced and sold or used off the premises or for the extraction of gasoline or other product therefrom, the market value at the well of one-eighth of the gas so sold or used, provided that on gas sold at the wells the royalty shall be one-eighth of the amount realized from such sale.

or

[2] Lessee to receive the field market price per thousand cubic feet for one-eighth (1/8) of all gas marketed from the premises.

or

[3] Lessee covenants and agrees to deliver to the credit of the Lessor, as royalty, free of cost, in the pipeline to which the wells drilled by the Lessee may be connected the equal one-eighth part of all Oil and/or Gas produced and saved from said leased premises.

Courts across the country are split as to whether these types of royalty clauses allow the lessee to deduct post-production costs from gas royalties. The question driving this case is a question of state law. Although neighboring states have addressed the issues presented by the parties in their federal lawsuit, there is no controlling precedent in the decisions of the Ohio Supreme Court.

The discussion in *Poplar Creek Dev. Co. v. Chesapeake Appalachia, L.L.C.*, 636 F.3d 235 (6th Cir. 2011), is helpful in framing the question this Court certifies. Applying Kentucky law, the U.S. Court of Appeals for the Sixth Circuit explained the issue and resolution as follows:

These cases arise out of a dispute over the respective rights of lessors and lessees under Kentucky oil and gas leases. Both actions are resolved by determining whether Kentucky law allows lessees, in calculating gas royalty payments, to take into account certain post-production costs as an offset against the value or proceeds upon which royalty payments are based. ...

[W]e hold that Kentucky follows the “at-the-well” rule, which allows for the deduction of post-production costs before paying appropriate royalties. ...

The dispositive issue in this case is the meaning of “wholesale market value of such gas at the well” in the parties’ royalty clause and the propriety, under Kentucky law, of deducting post-production costs from the lessor’s royalties. A number of courts in gas-producing states across the country have considered the meaning of similar royalty clauses in deciding which marketing or post-production costs, if any, are to be borne by the royalty owner. The decisions of these courts, however, have not been uniform. There are two diverse viewpoints, with some decisions picking and choosing between the two, depending on the specific cost under consideration. At one end of the spectrum is the view that, because the operator has an implied duty or an implied covenant to market the gas, all post-production costs must be borne by the operator. ... Poplar Creek advocates for this view, which the parties term the “marketable product” rule.

At the other end of the spectrum, several courts have held that while there is an implied duty or covenant to market the gas, this duty does not extend to expenses incurred in sales not at the wellhead; post production costs are to be shared proportionately by the working interest and royalty owners. ... Chesapeake advocates for this rule, which the parties term the “at the well” rule.

Id. at 237, 240-41 (citations omitted).

3. Question Certified

This Court certifies to the Ohio Supreme Court the following question, which may be determinative of these proceedings:

Does Ohio follow the “at the well” rule (which permits the deduction of post-production costs) or does it follow some version of the “marketable product” rule (which limits the deduction of post-production costs under certain circumstances)?

4. Names of Parties

The plaintiffs in this action are: Regis & Marion Lutz; Leonard Yochman; Joseph Yochman; and C.Y.V., L.L.C.

The defendant in this action is Chesapeake Appalachia, L.L.C. All claims against previously-named defendants have been dismissed.

5. Names of Counsel

Plaintiffs' counsel in this action are:

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6. Moving Party

The Court designates Chesapeake Appalachia, L.L.C. as the moving party.

ORDER

In accordance with Rule 9.03(A) of the Rules of Practice of the Supreme Court of Ohio, the Clerk of the United States District Court for the Northern District of Ohio is hereby instructed to serve copies of the certification order upon counsel for the parties and to file this certification order under the seal of this Court with the Supreme Court of Ohio, along with appropriate proof of service.

IT IS SO ORDERED.

Dated: April 1, 2015



HONORABLE SARA LIOI
UNITED STATES DISTRICT JUDGE