

PUBLICATION

Louisiana Second Circuit: Oil and Gas Lender Held Liable for Certain Mineral Lease Obligations

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A recent opinion from the Louisiana Court of Appeal, Second Circuit regarding *Gloria's Ranch, L.L.C. v. Tauren Exploration, Inc.*, has left a number of oil and gas lenders bellyaching. In this case, the Second Circuit found that a mineral lessee's lender can be held solidarily liable for certain mineral lease obligations.

The lessor, Gloria's Ranch, granted an oil and gas lease to Tauren Exploration (mineral lessee) in 2004. Tauren then assigned portions of its lease rights to Cubic Energy and EXCO USA (also, mineral lessees). In 2007, Cubic borrowed money from Wells Fargo Energy Capital and executed a credit agreement. The agreement required that the borrowed money be used for certain purposes (e.g., drilling), and that Wells Fargo retained the right to approve (i) the location and depth of wells, (ii) Cubic's entry into new operating agreements, or (iii) Cubic's alienation of its oil and gas lease rights. Wells Fargo did not obtain a working interest, however. The lease covered portions of five sections in Caddo Parish. Tauren drilled wells in three of the sections, while in the other two sections, an unrelated company drilled wells that served as unit wells. Later, Gloria's Ranch believed that the lease terminated for lack of production in paying quantities, and, in 2010, it wrote a letter to the mineral lessees (and Wells Fargo) demanding that they execute a recordable act recognizing that the lease had terminated. They refused, so Gloria's Ranch sued them.

Following a trial of the matter, the trial court determined that, in four of the five sections, the lease had terminated for lack of production in paying quantities. The court also concluded that Gloria's Ranch had lost valuable leasing opportunities because of the defendants' failure to execute an act recognizing partial lease termination. As for the fifth section, the court concluded that Tauren and Cubic failed to pay royalties to Gloria's Ranch for the portion of unit production that was attributable to the leased premises. The trial court entered judgment holding that the lease terminated in its entirety and granted a money judgment for: the unpaid royalties, statutory penalties equaling twice the unpaid royalties, millions of dollars for lost leasing opportunities, interest and attorney's fees. Remarkably, the trial court also held that Wells Fargo was solidarily liable with Tauren and Cubic for the entire money judgment, even though Wells Fargo never owned a working interest.

On appeal, the Louisiana Second Circuit affirmed the trial court's decision. Wells Fargo applied for rehearing, but a five-judge panel denied the application by a 3 to 2 vote. In an assertive opinion, the two judges who dissented from the denial of rehearing believed that the judgment was erroneous and that it would create a "chilling effect on the financing of oil and gas operations" and, ultimately, would adversely affect the economy of the State of Louisiana.