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Royalty Litigation Update: Colorado Court Of Appeals Addressed Jury Verdict In Class Action Lawsuit

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On October 13, 2015, the Colorado Supreme Court denied certiorari of an appeal from the Colorado Court of Appeals' decision in *Patterson v. BP America Production Co.*, 2015 COA 28, 2015 WL 1090004 (Colo. App. 2015).

In *Patterson*, 4,000 royalty owner members of the class obtained a favorable judgment of $7,941,809.23 based on their allegations against BP for underpaid royalties on natural gas production dating back to 1986. Due to BP's fraudulent concealment, royalty owners were allowed to toll the six-year statute of limitations. The district court also amended the damages award to include statutory prejudgment interest for a total of $40,215,626.23, but did not grant the class members their requested higher interest rate, or "moratory interest". C.R.S. § 5-12-201(1)(b).

A court can grant moratory interest if money is found to have been wrongfully withheld. Absent proof of the withholding party's gain or benefit, the statutory rate of 8% per year is applied. The moving party for moratory interest has the burden to prove by a preponderance of the evidence that the party withholding the money has realized a gain or benefit on the withheld funds. The Court of Appeals affirmed the trial court's rejection of moratory interest, because BP had not maintained the royalties or deductions withheld from royalties in separate bank accounts, but had instead commingled the revenues with other oil and gas operations. The record did not show BP's annual gain on the master bank account where the withheld money had been held.

Additionally, BP argued that the class was improperly certified because nine members of the class, operators themselves, admitted that they used the same netback accounting methodology in their own operations and were generally aware of this industry practice. However, the Court of Appeals affirmed the trial court's finding that the evidence was sufficient to certify the class and send the issue of fraudulent concealment on a class-wide basis to the jury. Among other evidence, the Court of Appeals relied on BP's failure to follow its own internal committee's recommendation that BP fully disclose the post-production cost deductions on its royalty statements to affirm the jury's verdict on fraudulent concealment. In addition, all of the 4,000 royalty owners had received the same royalty statements, which did not disclose any post-production cost deductions. Therefore, the Court of Appeals found, when viewing the evidence in a light most favorable to class members, the evidence was sufficient to send the issue of fraudulent concealment to the jury on a class-wide basis.

Finally, the Court of Appeals found that marketability of gas at the well is a question of fact for the jury to determine. An extensive amount of evidence was reviewed on this issue. The Court of Appeals found, therefore, that when viewed in a light most favorable to the royalty owners, a reasonable person could have concluded that the wellhead was not the first market for the gas produced.

In Colorado, the prevailing law regarding post-production cost deductions is *Rogers v. Westerman*, 29 P.3d 887 (Colo. 2001), which held that gas is not in marketable condition until it reaches the interstate pipeline, i.e. that an operator cannot charge royalty owners for any post-production costs necessary to make the gas marketable. The Kansas Supreme Court recently declined to follow *Rogers* in *Fawcett v. Oil Producers, Inc. of Kansas*, 352 P.3d 1032 (Kan. 2015), finding that when a lease provides for royalties based on a share of proceeds from the sale of gas at the well, and the gas is in fact sold at the well, the operator's duty to bear the expenses of making the gas marketable does not extend beyond that geographical point to post-sale expenses.

For more information on these cases, please contact Meg Gibson.

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