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The Oil and Gas Unit Operator's Duty to Nonoperating Working Interest Owners

I. INTRODUCTION

In producing oil or gas from a single reservoir, owners often "unitize"¹ the individual property interests that attach to the reservoir. Unitization allows more efficient and complete extraction of the oil or gas² and spreads the costs and risks of development.³ In fact, for a small property owner, or any owner subject to conservation regulations, production may be possible only through unitization.⁴

When an oil or gas unit is formed, one of the parties is designated "operator"; the others are "nonoperators." The operator produces⁵ the oil and gas in the unit and bills the nonoperators

1. Unitization is the pooling of the property interests, usually leases, overlying a reservoir. The unitizing of the property is accomplished by the execution of a unit agreement. The relationship of the interest owners is governed by a second document, the unit operating agreement. For a summary of the history and benefits of unitization, see 1A W. SUMMERS, *THE LAW OF OIL AND GAS* § 104 (1954) and L. HOFFMAN, *VOLUNTARY POOLING AND UNITIZATION* at iii-vii (1954).

2. In the early life of an oil field, oil from the reservoir is forced to the surface by the weight of the overlying rock. However, this natural "energy" diminishes over time, leaving much of the oil trapped in the reservoir. In many cases, the energy level of the reservoir can be maintained or restored through the injection of pressurized gas or water; the variety of injection techniques are broadly classed "secondary recovery." Effective secondary recovery must occur on a reservoir-wide basis. See 1A W. SUMMERS, *supra* note 1. Therefore, unitization of all interests in the reservoir is essential to increasing the total production.

Likewise, maintaining a constant pressure in the reservoir during production prevents oil from seeping into the dry rock or sand surrounding the reservoir. As a result, unitization increases both the yield and the productive life of a reservoir. The dwindling of the nation's domestic reserves suggests that secondary recovery, and hence unitization, will be of increased importance in the future.

3. The sharing of costs and risks is especially important in deep drilling operations and in production from economically marginal reservoirs. *Id.*

4. The owner of a small interest may be unable to cover the fixed costs of drilling a well; unitization permits that owner to enjoy the same cost structure as a much larger owner. Likewise, state or federal conservation agencies may limit the number and spacing of wells in an area, irrespective of the number of interest owners. *Id.* Unitization allows all owners to recognize the value of their interest without violating the regulations.

5. "Production" encompasses all activities associated with bringing discovered oil or gas to the surface. It does not include exploration, which occurs before production, or processing and marketing, which occur after. The parties to a unit often specify that

for costs incurred. The specific obligations and relationships of the parties are defined by an operating agreement,⁶ a lengthy contract executed before unit operations begin.

The intricacy of the parties' relationship, and its facial similarity to a joint venture,⁷ suggests that the operator may owe a duty to the nonoperators that would not exist in an arm's length transaction. The issue of the nature and scope of that duty has been litigated frequently.⁸

This comment inquires into the nature of the operator's duty.⁹ A careful study of the cases shows that courts tend to address the question needlessly—because the operating agreement usually controls the litigation—and with terms borrowed from inapt areas of law. The comment then seeks to clarify the operator's responsibility by proposing a two-pronged duty: (1) the operator is bound to observe the terms of the operating

produced oil or gas will be taken by each party "in kind" at the well head, before any processing. See A.A.P.L. Form 610-1982 Model Form Operating Agreement [hereinafter Model Form 610]; 6 W. SUMMERS, *THE LAW OF OIL AND GAS* § 1328 para. 13 (1967) (Operating Agreement Among Working Interest Owners Only).

6. For three standard form operating agreements, see Model Form 610, *supra* note 5 and 6 W. SUMMERS, *THE LAW OF OIL AND GAS* § 1328 (1967 & Supp. 1987).

7. The commonly recognized elements of a joint venture are (1) a joint interest in property, (2) an agreement to share profits and losses, and (3) mutual control of, or cooperation in, the project. *Crosby-Mississippi Resources, Ltd. v. Saga Petroleum U.S., Inc.*, 767 F.2d 143, 147 (5th Cir. 1985); *White v. A.C. Houston Lumber Co.*, 179 Okla. 89, 91, 64 P.2d 908, 910 (1937); *Ayco Dev. Corp. v. G.E.T. Serv. Co.*, 616 S.W.2d 184, 186 (Tex. 1981). Unit operations may satisfy these conditions; the issue has been the focus of many cases and articles. See, e.g., Boigon, *Liabilities and Relationships of Co-Owners Under Agreements for Joint Development of Oil and Gas Properties*, 37 INST. ON OIL & GAS L. & TAX'N 8-1 (1986); Lane & Boggs, *Duties of Operator or Manager to its Joint Venturers*, 29 ROCKY MTN. MIN. L. INST. 199 (1983). However, the issue is one step removed from the ultimate question of what duty the operator owes. See *infra* notes 14-25 and accompanying text.

8. See, e.g., *infra* notes 46-47.

9. This comment explores only the relationship between an operator and a nonoperating working interest owner. Often the working interest owner is a lessee or sub-lessee holding the property subject to an overriding royalty, production payment, or net profits interest. See 5 E. KUNTZ, *A TREATISE ON THE LAW OF OIL AND GAS* §§ 63.2 at 197-98, 63.3 at 213, 63.5 at 228-29 (1978). The operator's limited duty to these latter interest owners is discussed in Note, *Fiduciary Protection of Nonoperating Oil and Gas Interests Against the Acts of an Operator*, 18 TULSA L.J. 496 (1983) and in Martz & Hames, *Implied Rights of Royalty Owners*, 3 ROCKY MTN. MIN. L. INST. 195 (1957). Likewise, the duties among parties to "hard rock" unit agreements are not addressed.

However, this comment does encompass operating agreements entered into by cotenants. Cotenants can be included in the ambit of this discussion because "[t]here is no trust relationship between cotenants as such—one is not the agent of the other." *Britton v. Green*, 325 F.2d 377, 383 (10th Cir. 1963); see also *Tenneco Oil Co. v. Bogert*, 630 F. Supp. 961, 965 (W.D. Okla. 1986).

agreement, and (2) the operator must not use its position to obtain unfair advantage over the nonoperators. Finally, this comment explores the policy reasons supporting the limitation of the operator's duty to these two prongs, versus the broader duties often inferred from judicial decisions.

II. JUDICIAL STRUGGLE WITH THE DUTY ISSUE

The unit operator, manager of a complex process in an industry of high risk and fluctuating profits, is frequently accused of wronging the nonoperators. In resolving disputes among operators and nonoperators, courts often couch their decisions in the language of various duties rather than base their holdings on simpler contractual grounds.

A. *The Range of Possible Duties*

The operator oversees the day-to-day aspects of the production process. Along with extracting the oil or gas, the operator must account for costs incurred and make charges to the nonoperators. If unit production is sold to a third party, the operator remits the profits to the nonoperators. The duties relating to production decisions are specified in detail in the operating agreement and are rarely the subject of litigation.¹⁰

Nonoperators often assert that the operator has broader, even fiduciary duties. For example, nonoperators have argued that the operator must disclose information about the reservoir obtained by virtue of the operator's position.¹¹ Nonoperators have also demanded that an operator take costly steps to protect the individual interests of nonoperators.¹²

In addition, nonoperators have asserted negative duties not addressed by the parties' contract. Clearly, the operator may not defraud the nonoperators.¹³ However, a more difficult question is

10. The operator is bound only to act with "reasonable skill and diligence" in production decisions. *See, e.g.,* Great Western Oil & Gas Co. v. Mitchell, 326 P.2d 794, 798 (Okla. 1958) (quoting J.E. Crosbie, Inc. v. King, 192 Okla. 53, 56, 133 P.2d 543, 546 (1943)).

11. *See, e.g.,* Frankfort Oil Co. v. Snakard, 279 F.2d 436 (10th Cir. 1960) (nonoperator unsuccessfully alleged duty to disclose results of seismic surveys and to furnish geological and geophysical data).

12. *See, e.g.,* Tenneco Oil Co. v. Bogert, 630 F. Supp. 961, 964 (W.D. Okla. 1986) (nonoperator claimed that operator had duty to drill an increased density well to prevent drainage from the unit).

13. *See, e.g.,* Oklahoma Co. v. O'Neil, 440 P.2d 978, 988 (Okla. 1968) (operator defrauded nonoperators in formation and operation of the unit).

whether the operator has a duty not to gain any personal advantage over the nonoperators. In the extreme, that duty would require the operator to disclose everything it learns in its business during the term of the operating agreement, both inside and outside the unit.

B. *The Courts' Varied Approaches*

Courts have resolved disputes over the operator's duty consistently, but in the process have fallen into a morass of borrowed terms. As a result, decisions discussing the operator's duty are characterized by many apparent differences. Those differences arise from conflicting terms and analytical approaches, and needlessly confuse the question of the operator's duty.

1. *Relationship analyses*

Courts frequently answer the question of the operator's duty indirectly through an analysis of the parties' relationship—by first classifying that relationship and then imposing a concomitant duty. One common approach is to analyze the relationship to determine if the unit parties are joint venturers or mining partners, and hence bear fiduciary duties.¹⁴ This classification simplifies a court's task because the elements of a joint venture and partnership are well defined and relatively easy to identify.¹⁵ Unfortunately, because the elements of joint venture and mining partnership are often borrowed from cases involving third-party liability,¹⁶ the analysis yields erroneous results when applied *among* parties to a unit agreement.

An example of a joint venture analysis is found in *Hamilton v. Texas Oil & Gas Corp.*¹⁷ In *Hamilton* the court cited another Texas opinion, *Rankin v. Naftalis*,¹⁸ for the proposition that an operator has a fiduciary duty "only upon a finding of joint ven-

14. The law is well settled that joint venturers and mining partners are bound by fiduciary duties. See, e.g., *Blackstock Oil Co. v. Caston*, 184 Okla. 489, 491, 87 P.2d 1087, 1089 (1939); *Fitz-Gerald v. Hull*, 150 Tex. 39, 54, 237 S.W.2d 256, 264 (1951); Williams, *The Fiduciary Principle in the Law of Oil and Gas*, 13 INST. ON OIL & GAS L. & TAX'N 201, 260-61 (1962).

15. See *supra* note 7. The distinction between joint venture and mining partnership is that the latter requires joint ownership, rather than a simple joint interest in the property. See Fiske, *Mining Partnership*, 26 INST. ON OIL & GAS L. & TAX'N 187, 195 nn.14 & 16 (1975). The distinction is insignificant for purposes of this comment.

16. See *infra* note 22.

17. 648 S.W.2d 316 (Tex. Ct. App. 1982, no writ).

18. 557 S.W.2d 940 (Tex. 1977).

ture."¹⁹ The court then listed the elements of a joint venture, one of which is a right of mutual control or cooperation in the project,²⁰ and found that because the operator had exclusive control no joint venture was created; thus, no fiduciary duty existed.²¹

This conclusion demonstrates how formally classifying the parties' relationship adds an extra step to the duty analysis, clouds the issue, and potentially yields an erroneous result. The *Hamilton* court seemed to hold that because the operator had exclusive control of the project, it owed no fiduciary duty to the nonoperators. The folly of this joint venture analysis of the operator's duty is that the elements of joint venture are most often defined in the context of liability to third parties;²² imposing that liability on an alleged joint-venturer would be unfair to a party with no control over the operations that created the liability. Thus, in the third-party context, a key element of a joint venture is the right of mutual control or cooperation.

However, joint venture analysis in the context of an operator's liability to nonoperators can yield counterintuitive results, as in *Hamilton*. Indeed, increased control by the operator should increase, not decrease, the duty owed.²³ Joint venture analysis of an operator's duty suffers from a logical fallacy: though every joint venturer is a fiduciary, not every fiduciary is a joint venturer.²⁴ Even if an operator were deemed to owe a traditional fiduciary duty, a joint venture analysis would often fail to reveal it. Thus, the proper place to look for duties is not in a judicial definition of the parties' relationship, but in their operating agreement.²⁵

19. 648 S.W.2d at 321.

20. See *supra* note 7.

21. 648 S.W.2d at 321.

22. See, e.g., *White v. A.C. Houston Lumber Co.*, 179 Okla. 89, 91, 64 P.2d 908, 910 (1937) (elements of joint venture listed in suit by laborers and materialmen against parties to a drilling venture).

23. See Note, *Fiduciary Duties of Partners*, 48 IOWA L. REV. 902, 908 (1963).

24. *Gaines v. Hamman*, 163 Tex. 618, 623, 358 S.W.2d 557, 560-61 (1962). The argument applies to mining partnerships as well as to joint ventures: In many cases, a court would find that the parties to a unit do not satisfy the "joint ownership" requirement of mining partnership. See *supra* note 15. However, their mutual duties should not be obliterated by a finding of separate ownership.

25. See *Andrau v. Michigan Wis. Pipe Line Co.*, 712 P.2d 372, 375 (Wyo. 1986) (citing *Beadle v. Daniels*, 362 P.2d 128, 131 (Wyo. 1961)) (because operating agreements control it is unnecessary to consider the alleged existence of a mining partnership). Additional reasons for avoiding joint venture and mining partnership analyses are that most operating agreements expressly deny these relationships, see *infra* note 53 and accompa-

2. *Fiduciary/trustee analyses*

A second method of indirect analysis is to analogize the operator to a traditional fiduciary or trustee. A number of courts have expressly imposed a fiduciary duty on the operator,²⁶ though many, particularly in Texas, have rejected the idea.²⁷ Several courts have gone so far as to place the operator in the position of trustee for the nonoperators.²⁸

However, the operator technically is neither a fiduciary nor a trustee. A true fiduciary is required to subordinate his own interests to those of his coadventurers.²⁹ Likewise, "[i]n a strict

nying text, and that the traditional fiduciary duties that accompany them frequently would conflict with the express terms of the operating agreement, *see infra* notes 87-89.

For articles discussing the "relationship" analysis, see Boigon, *supra* note 7, Lane & Boggs, *supra* note 7, and Note, *Oil and Gas: A.A.P.L. Form 610 Model Form Operating Agreement: Imposing Limitations on the Operator's Ability to Require Contributions from Nondefaulting Nonoperators*, 36 OKLA L. REV. 730 (1983).

26. *See, e.g., In re Mahan & Rowsey, Inc.*, 817 F.2d 682, 684 (10th Cir. 1987); *Frankfort Oil Co. v. Snakard*, 279 F.2d 436, 443 (10th Cir. 1960); *Envirogas Inc. v. Walker Energy Partners*, 641 F. Supp. 1339, 1345 (W.D.N.Y. 1986); *Rankin v. Naftalis*, 557 S.W.2d 940, 944 (Tex. 1977).

27. *See, e.g., Crosby-Mississippi Resources, Ltd. v. Saga Petroleum U.S., Inc.*, 767 F.2d 143, 147 (5th Cir. 1985); *In re Wilson*, 69 Bankr. 960, 965 (Bankr. N.D. Tex. 1987); *Tenneco Oil Co. v. Bogert*, 630 F. Supp. 961, 966-67 (W.D. Okla. 1986); *Hamilton v. Texas Oil & Gas Corp.*, 648 S.W.2d 316, 320-21 (Tex. Ct. App. 1982, no writ).

Texas' strong position on this issue is also reflected in its general partnership statute, which specifies that "[o]peration of a mineral property under a joint operating agreement does not of itself establish a partnership." TEX. REV. CIV. STAT. ANN. art. 6132b § 7(5) (Vernon 1970).

28. *See, e.g., Reserve Oil, Inc. v. Dixon*, 711 F.2d 951, 953 (10th Cir. 1983); *Britton v. Green*, 325 F.2d 377, 383 (10th Cir. 1963); *Young v. West Edmond Hunton Lime Unit*, 275 P.2d 304, 309 (Okla. 1954), *appeal dismissed*, 349 U.S. 909 (1955); *Beadle v. Daniels*, 362 P.2d 128, 130 (Wyo. 1961). *Contra Luling Oil & Gas Co. v. Humble Oil & Ref. Co.*, 144 Tex. 475, 484, 191 S.W.2d 716, 722 (1945).

The imposition of a "trustee-type" duty has questionable foundations and has been criticized widely. *See infra* notes 41, 45 and accompanying text.

29. A true fiduciary has been defined as follows:

[A] person holding the character of a trustee, or a character analogous to that of a trustee, in respect to the trust and confidence involved in it and the scrupulous good faith and candor which it requires. A person having duty, created by his undertaking, to act primarily for another's benefit in matters connected with such undertaking.

BLACK'S LAW DICTIONARY 563 (5th ed. 1979) (emphasis added).

In the classic opinion *Meinhard v. Salmon*, 249 N.Y. 458, 164 N.E. 545 (1928), then Chief Judge Cardozo penned the language that has come to be synonymous with fiduciary duties. In particular, Cardozo declared: "Salmon [the defendant] had put himself in a position in which thought of self was to be renounced, however hard the abnegation." *Id.* at 468, 164 N.E. at 548.

However, a wealth of cases have rejected claims by nonoperators that an operator must place their interests ahead of the operator's. *See, e.g., Crosby-Mississippi Re-*

sense, a 'trustee' is one who holds the legal title to property for the benefit of another."³⁰ The strict definitions of these terms are at odds with the nature of unit operations: as a practical matter, the operator does not intend to subordinate its own interests to those of the nonoperators, nor do the nonoperators have that expectation. Moreover, no title to property passes to the operator. The terms fiduciary and trustee have been used to impose a broad range of duties, only a part of which is consistent with unit operations.³¹ The terms properly apply to operators only in the broadest, loosest senses.

The tendency to assess the simple operator-nonoperator relationship with the terms fiduciary and trustee, like the relationship analysis, has produced an apparently incohesive body of opinions. A recent decision of the Tenth Circuit Court of Appeals, *Reserve Oil, Inc. v. Dixon*,³² illustrates the confusion over the operator's duty.

The relationships among the parties in *Reserve Oil* typify those of unit operations. The plaintiffs, nonoperating working-interest owners, brought suit against the operator alleging that the operator's sale of their share of production, without remitting the proceeds of the sale, violated the operator's fiduciary duty.³³

The trial court dismissed the nonoperators' claims.³⁴ In reversing the lower court's decision, the court of appeals held that

sources, Ltd. v. Saga Petroleum U.S., Inc., 767 F.2d 143 (5th Cir. 1985); *Opeco, Inc. v. Scott*, 321 F.2d 471 (10th Cir. 1963); *Frankfort Oil Co. v. Snakard*, 279 F.2d 436 (10th Cir. 1960); *In re Wilson*, 69 Bankr. 960 (Bankr. N.D. Tex. 1987); *Tenneco Oil Co. v. Bogert*, 630 F. Supp. 961 (W.D. Okla. 1986); *Colpitt v. Skelly Oil Co.*, 499 P.2d 415 (Okla. 1972); *Rankin v. Naftalis*, 557 S.W.2d 940 (Tex. 1977); *Andrau v. Michigan Wis. Pipe Line Co.*, 712 P.2d 372 (Wyo. 1986).

30. *State v. Sartorius*, 344 Mo. 912, 918, 130 S.W.2d 547, 549 (1939) (citations omitted).

31. *Cf. Tenneco Oil Co. v. Bogert*, 630 F. Supp. 961, 967 (W.D. Okla. 1986) (noting that, especially with regard to operating agreements, "the term 'fiduciary' is easily bandied-about without precision").

32. 711 F.2d 951 (10th Cir. 1983).

33. *Id.* at 952.

34. The nonoperators sued on theories of breach of fiduciary duty and conversion. The trial court held that the operating agreement created no fiduciary relationship among the parties. *Id.* In dismissing the second count, the trial court defined conversion as "taking property without the owner's consent" and stated that money can be converted only if the fund from which it is taken is a specific chattel or if there is an obligation to return specific money. *Id.* The court ruled that the operator's sale of production created a general indebtedness to the nonoperators that could be discharged by any payment of money; thus, the court reasoned, the operator did not convert the nonoperators' interests in the oil and gas by misapplying the proceeds. *Id.*

the parties' contract³⁵ vested ownership of the oil and gas in each working interest owner on a pro rata basis.³⁶ Therefore, the failure of the operator to remit the profits of the sale was a clear breach of the operating agreement³⁷ and, according to the definition of the trial court,³⁸ should have been deemed a conversion.³⁹ The court's opinion could have ended with the following statement: "The operator has no right to or interest in either the oil and gas or the proceeds from its sale beyond the owner's unpaid proportionate share of the costs."⁴⁰

However, the court went on to read the contract as "creat[ing] a trustee type relationship imposing a duty of fair dealing between the operator and the non-operator owners in the matter of distribution of shares among the owners."⁴¹ The opinion introduces this trustee language, but fails to clarify

35. The terms "contract" and "operating agreement" are used interchangeably in the opinion. See 711 F.2d at 952 n.2.

36. *Id.* at 952-53.

37. See *id.* at 953.

38. See *supra* note 34.

39. See 711 F.2d at 952.

40. *Id.* at 953.

41. In a footnote, the court made the following admission:

Although we are simply construing the parties' contracts, we note that the Oklahoma Supreme Court has held that the operator of a unitized oil field stands in a position similar to that of a trustee with respect to those interested in the oil production. *Young v. West Edmond Hunton Lime Unit*, 275 P.2d 304 (Okla. 1954), *appeal dismissed*, 349 U.S. 909, 75 S.Ct. 600, 99 L.Ed. 1245 (1955).

711 F.2d at 953 n.4.

Thus, the court revealed two facts about its statement concerning the operator's duty. First, the statement was gratuitous—the contract admittedly was dispositive of the case before the court. Second, the statement was founded on questionable authority. The *Young* decision was based expressly on a forced pooling statute that compelled mineral interest holders to "surrender all right to produce and take oil," in return for a share of unit production. 275 P.2d at 308. The court in *Young* held that the unit organization formed pursuant to this statute, along with the operator, "stands in a position similar to that of a trustee for all who are interested in the oil production either as lessees or royalty owners." *Id.* at 309.

However, the unitization statute, enacted in 1945, was repealed by the Oklahoma legislature in 1951. *Id.* at 311 (Williams, J., dissenting). Thus, the unique foundation for the *Young* decision has long since been eliminated.

Moreover, the *Young* court used the term trustee in the strict sense: the right to produce oil actually passed from the nonoperators to the operator. *Id.* at 306, 308. (See 89 C.J.S. *Trusts* § 3 (1955) for the distinction between the technical and "broader" usages of the term trustee.) If the court of appeals intended to adopt the term as applied in *Young*, then it almost certainly mischaracterized the nature of the *Reserve* parties' relationship.

whether the operator's ultimate liability was contract or duty based.

Reserve Oil is typical of decisions discussing the operator's duty and illustrates two points. First, the operating agreement—the parties' contract—addressed the issue before the court and was dispositive of the litigation. Second, though the court properly decided the case,⁴² it needlessly explored the operator's duty to the nonoperators. In so doing, the court applied language from an inappropriate area of the law⁴³ and from an opinion not on point with the case before it.⁴⁴

Like the *Reserve Oil* court, few courts are led ultimately awry by labels such as fiduciary and trustee. However, the use of those terms in opinions does more than befuddle courts:⁴⁵ it promotes specious litigation by encouraging disgruntled nonoperators to sue on the basis of the operator's presumed "fiduciary duty," though their operating agreements offer no support for their claims.

Reserve Oil demonstrates both the capacity of operating agreements to resolve disputes and the propensity of courts to venture beyond the agreements. Nonetheless, the outcome of *Reserve Oil*, and of many other cases based on indirect analyses, is consistent with the nature of the operator's duty, as will be shown.

42. The dispute before the appeals court in *Reserve Oil* was properly resolved: the nonoperators' allegations, taken as true, established both conversion and breach of the operating agreement, the parties' contract. 711 F.2d at 952.

43. See *supra* note 41.

44. *Id.*

45. For cases rejecting the language of *Reserve Oil*, see *In re Wilson*, 69 Bankr. 960, 964-65 (Bankr. N.D. Tex. 1987) and *Andrau v. Michigan Wis. Pipe Line Co.*, 712 P.2d 372, 375 (Wyo. 1986). See also *Garfield v. True Oil Co.*, 667 F.2d 942, 944-45 (10th Cir. 1982) (recognizing that *Young* was based on a specific statute and refusing to impose a trust relationship between an operator and owners of a net profits interest).

In at least one instance, the language of the case has been applied with novel results. In *In re Mahan & Rowsey, Inc.*, 35 Bankr. 898 (Bankr. W.D. Okla. 1983), *aff'd* 817 F.2d 682 (10th Cir. 1987), the bankruptcy court cited *Reserve Oil* for the proposition that overpayments made by nonoperators to an operator for costs incurred are held in trust for the operator. *Id.* at 903. For an analysis of the ramifications of this decision on the law of bankruptcy, see Note, *Reserve Oil v. Dixon: Giving Unexpected Meaning to Trust Law in a Contractual Relationship and Its Impact Upon Bankruptcy*, 11 OKLA. CITY U.L. REV. 437 (1986).

III. TWO ASPECTS OF THE OPERATOR'S DUTY REVEALED IN JUDICIAL DECISIONS

Numerous opinions discuss the operator's duty to nonoperators. Though the language of these opinions is both diverse and confounding, the results attained can be reconciled. Moreover, the decisions establish a pattern or outline of the operator's duty. A study of those decisions shows that courts require the operator to (1) adhere to the terms of the operating agreement, and (2) shun the personal advantage to be gained through the operator's position.

A. *The Operator is Bound by the Operating Agreement*

The overarching principle seen in judicial opinions on the operator's duty is that the operating agreement controls the parties' obligations and circumscribes the operator's affirmative duties.⁴⁶ Though the operator cannot violate the agreement,⁴⁷ it need not take affirmative acts that the agreement does not require.⁴⁸

Cases hold that the operating agreement limits the territory

46. *Crosby-Mississippi Resources, Ltd. v. Saga Petroleum U.S., Inc.*, 767 F.2d 143, 147 (5th Cir. 1985) ("Even if a joint venture were established, the duties pertaining thereto would not extend beyond a reasonable interpretation of the operating agreements."); *Frankfort Oil Co. v. Snakard*, 279 F.2d 436, 442 (10th Cir. 1960) (defendant operator not bound by fiduciary duty to furnish reports to nonoperator, because agreement only entitled nonoperator to access to information, and that right was not denied); *Tenneco Oil Co. v. Bogert*, 630 F. Supp. 961, 967 (W.D. Okla. 1986) (operating agreement did not impose fiduciary duty obligating operator to drill increased density well not required by the agreement); see also *British Am. Oil Producing Co. v. Midway Oil Co.*, 183 Okla. 475, 477-79, 82 P.2d 1049, 1052-53 (1938); *Luling Oil & Gas Co. v. Humble Oil & Ref. Co.*, 144 Tex. 475, 483-84, 191 S.W.2d 716, 722-23 (1945); *Andrau v. Michigan Wis. Pipe Line Co.*, 712 P.2d 372, 374 (Wyo. 1986).

In each of these cases, the courts refuted the nonoperators' claims of fiduciary duty by citing the controlling provisions of the operating agreements.

47. See, e.g., *Reserve Oil, Inc. v. Dixon*, 711 F.2d 951, 952-53 (10th Cir. 1983); *Young v. West Edmond Hutton Lime Unit*, 275 P.2d 304, 307, 310 (Okla. 1954), *appeal dismissed*, 349 U.S. 909 (1955); *Beadle v. Daniels*, 362 P.2d 128, 130 (Wyo. 1961).

All three cases could have been disposed of by resort to the operating agreements, but in each case the court chose to explore the duty issue. See *supra* note 41; *Young*, 275 P.2d at 309 (operator breached unitization plan by selling oil at less than prevailing market price); *Andrau*, 712 P.2d at 375 ("[T]he fiduciary duty claimed in the present case, like that in *Beadle*, is specifically dealt with in the operating agreement.") (emphasis added).

48. See *supra* note 46. A possible exception to this rule is that the operator may be bound to disclose information and opportunities it obtains solely because of its position and that, if not disclosed, would give the operator unfair advantage vis-a-vis the nonoperators. See *infra* notes 68-70 and accompanying text.

and transactions of the unit operation, and hence, the duty owed.⁴⁹ The opinions demonstrate that the operator has no duty regarding land outside the unitized area⁵⁰ or activities such as processing and marketing.⁵¹ Courts have used similar reasoning to hold that the operator can have arm's length dealings with nonoperators in transactions outside the unit operation.⁵² This rule precludes the establishment of a fiduciary or other duty extending beyond the transaction that originally created the duty. The cases show that the duty attaches not to the parties, but to their unit operation.

An important corollary to the rule that the operating agreement controls the parties' obligations is that courts honor the expressed intent to limit those obligations. Many operating agreements—including the most widely used form agreements—expressly disavow the intent to create a partnership or to have joint liability to third parties.⁵³ Disavowal of such relationships properly reflects the intent of the parties forming a unit operation.⁵⁴ When these provisions are consistent with the parties' actual relationship, courts unanimously uphold them.⁵⁵

49. See, e.g., *Opco, Inc. v. Scott*, 321 F.2d 471, 473 (10th Cir. 1963); *Foley v. Phillips*, 211 Kan. 735, 740, 508 P.2d 975, 979 (1973); *Colpitt v. Skelly Oil Co.*, 499 P.2d 415, 419 (Okla. 1972); *Rankin v. Naftalis*, 557 S.W.2d 940, 945-46 (Tex. 1977); cf. *British Am. Oil Producing Co. v. Midway Oil Co.*, 183 Okla. 475, 477, 82 P.2d 1049, 1052 (1938) (contract related to a specific area and did not bind either party with regard to any other territory).

50. See *supra* note 49.

51. *Crosby-Mississippi*, 767 F.2d 143, 146 (5th Cir. 1985).

52. *Rankin*, 557 S.W.2d at 945; cf. *Armstrong v. Skelly Oil Co.*, 55 F.2d 1066, 1068 (5th Cir. 1932). In *Armstrong* the lessor of an oil and gas field sought to participate in the profits made by the lessee's refining of gas. In denying the lessor's claim, the court made the following statement: "Appellees were under no obligation to erect a plant to treat this gas. When they did so they were entitled to deal with the lessor the same as a stranger would have done." *Id.*

53. See, e.g., Model Form 610, *supra* note 5, art. VII-A; 6 W. SUMMERS, *supra* note 5, § 1328 para. 21.

54. See *infra* notes 81-82 and accompanying text.

55. See, e.g., *Cross v. Pasley*, 270 F.2d 88, 92 (8th Cir. 1959) (relationship of joint venture in drilling operations can arise only when the parties choose to so associate themselves); *Tenneco Oil Co. v. Bogert*, 630 F. Supp. 961, 966-67 (W.D. Okla. 1986) (disclaimer of joint or collective liability or partnership upheld; duties are controlled by the terms of the agreement); *Prentice v. Amax Petroleum Corp.*, 220 So. 2d 783, 787 (La. Ct. App. 1969) (negation of joint venture and fiducial obligation upheld; "The intent of the parties is explicit and we are bound to give it legal effect."); cf. *Garfield v. True Oil Co.*, 667 F.2d 942, 944 (10th Cir. 1982) (negation of joint venture and partnership among operator and net profits interest owners). But cf. *Envirogas, Inc. v. Walker Energy Partners*, 641 F. Supp. 1339, 1345 (W.D.N.Y. 1986) (reality of relationship refuted disclaimer of duty); *Oklahoma Co. v. O'Neil*, 440 P.2d 978, 986 (Okla. 1968) (agreement with lan-

The rule that the operating agreement creates and controls the operator's duty is illustrated in *Crosby-Mississippi Resources, Ltd. v. Saga Petroleum U.S., Inc.*⁵⁶ In *Crosby*, a gas unit produced both natural gas and condensate. The operator of the unit exercised its contract right to purchase all of the condensate,⁵⁷ crediting the non-operating working interest owners with wellhead sales at prices equal to or greater than the prevailing market price.⁵⁸ The condensate was refined and sold by the operator for the highest available price,⁵⁹ which was greater than the price the nonoperators received for the raw condensate.⁶⁰

The nonoperators brought suit alleging breach of contract, breach of fiduciary duty, and unjust enrichment.⁶¹ They argued that the operator had breached the operating agreement and the operators fiduciary duty by failing to credit them with the price received for the refined condensate.⁶²

The district court granted summary judgment for the operator, and the court of appeals affirmed, holding that the nonoperators had received all they were entitled under the operating agreement.⁶³ The court stated that had the parties intended that the nonoperators be credited with the price of refined rather than raw products, they could have drafted their contract accordingly.⁶⁴ The court's decision was based on the clear language

guage negating partnership or joint venture had been induced by fraud; parol evidence admitted to vary the contract terms).

Similarly, parties can limit their obligations by contract provisions authorizing acts that might otherwise violate traditional fiduciary duties. *Andrau v. Michigan Wis. Pipe Line Co.*, 712 P.2d 372, 376 (Wyo. 1986) (citing *Frankfort Oil Co. v. Snakard*, 279 F.2d 436 (10th Cir. 1960)).

56. 767 F.2d 143 (5th Cir. 1985).

57. *Id.* at 144. The operating agreement made the following provision:

"In the event any party shall fail to make the arrangements necessary to take in kind or separately dispose of its proportionate share of the oil and condensate produced from the Unit Area, Operator shall have the right, subject to revocation at will by the party owning it, but not the obligation to purchase such oil and condensate or sell it to others for the time being, at not less than the market price prevailing in the area, which shall in no event be less than the price which Operator receives for its portion of the oil and condensate produced from the Unit Area."

Id. (quoting operating agreement) (emphasis in original).

58. *Id.* at 145.

59. *Id.* at 144.

60. *Id.* at 145.

61. *Id.* at 144.

62. *Id.* at 145.

63. *Id.*

64. *Id.* at 146, 147.

of the operating agreement, and on the unfairness of allowing the nonoperators to share the fruits of the operator's industry without having shared the associated risk.⁶⁵

The nonoperators tried to expand the contract by alleging that a fiduciary duty required the operator to share its refining and marketing profits. They asserted that their relationship with the operator created a joint venture and concomitant fiduciary duty. In refuting that argument, the court of appeals held that "[e]ven if a joint venture were established, *the duties pertaining thereto would not extend beyond a reasonable interpretation of the operating agreements.*"⁶⁶ This statement defines the first prong of the operator's duty: The duty arises from and is circumscribed by the operating agreement. Thus, courts should look first to the parties' contract when setting the scope of the operator's duty.

B. The Operator May Not Use Its Position to Obtain Unfair Advantage

A synthesis of the case law reveals a second aspect of the operator's duty: The operator must eschew the unfair advantage obtainable from its position. The cases show that at a minimum, the operator cannot use its position to injure or to defraud the nonoperators.⁶⁷ In addition, some courts have held that the operator must disclose to the nonoperators information and opportunities that come to it as unit operator.⁶⁸ When courts recog-

65. *Id.*

66. *Id.* at 147 (footnote omitted) (emphasis added).

67. See, e.g., *Texas Oil & Gas v. Hawkins Oil & Gas*, 282 Ark. 268, 668 S.W.2d 16 (1984) (operator used nonoperator's abstracts to determine that the latter's title was defective, and subsequently bought the property for itself); *Oklahoma Co. v. O'Neil*, 440 P.2d 978, 988 (Okla. 1968) (operator found to have defrauded nonoperators in the purchase of leases to be included in the unit).

68. See *Young v. West Edmond Hunton Lime Unit*, 275 P.2d 304, 310 (Okla. 1954), *appeal dismissed*, 349 U.S. 909 (1955) (operator required to notify royalty interest owners of highest selling price available). But cf., *Tenneco Oil Co. v. Bogert*, 630 F. Supp. 961, 968 (W.D. Okla. 1986) (operator not bound to disclose information not required by operating agreement); *British Am. Oil Producing Co. v. Midway Oil Co.*, 82 P.2d 1049, 1052 (Okla. 1938) (operator not required to disclose information about value of adjacent property obtained during drilling).

The court in *British American* distinguished another Texas case, *Whatley v. Cato Oil Co.*, 115 S.W.2d 1205 (Tex. Civ. App. 1938). In *Whatley* the contract provided for all information acquired in drilling to be used for the parties' mutual benefit; the *British American* contract had no similar provision. 82 P.2d at 1051. The court in *British American* reasoned that in the absence of a sharing provision, the court could not assume that the parties were willing to be bound to mutual use of the information. *Id.* at 1052. This

nize this duty of disclosure, they limit it to the unitized area⁶⁹ and to information gained by the operator through the operator's position, as opposed to information obtained through independent efforts.⁷⁰ The level of duty recognized by these courts falls below that imposed on true trustees and fiduciaries.⁷¹

The duty to avoid unfair personal advantage is demonstrated in *Texas Oil & Gas Corp. v. Hawkins Oil & Gas, Inc.*⁷² A nonoperator turned over to the operator abstracts and title opinions pertaining to the unit area. The abstracts revealed that the nonoperator had defective title to some of the leased property; the operator discovered the defect and bought the property for itself.

The Arkansas Supreme Court found that the parties' joint operating agreement created a "relationship of trust and confidence" that was breached by the operator's use of the nonoperator's abstracts.⁷³ The operator's conduct could not have been foreseen or proscribed by the operating agreement. Though the acts were beyond the realm of the contract, the court required

judicial position has the additional advantage of decreasing ambiguity: a clear contract provision helps both the parties and courts determine what information is "valuable" and must be shared.

69. See, e.g., *Colpitt v. Skelly Oil Co.*, 499 P.2d 415, 419 (Okla. 1972).

70. See, e.g., *Frankfort Oil Co. v. Snakard*, 279 F.2d 436, 442 (10th Cir. 1960) (operator under no duty to disclose results of geophysical surveys done on the unitized property).

71. For example, in *Meinhard v. Salmon*, 249 N.Y. 458, 466, 164 N.E. 545, 547 (1928) the court held that a coadventurer "may not appropriate to his own use a renewal of a lease, though its term is to begin at the expiration of the partnership," and though it primarily covers land outside the original lease.

However, in *Colpitt*, the court held that an operator need not share title to or profits from a lease obtained adjacent to the unit, though production from the lease increased 25 times as a result of secondary recovery efforts in the unit, and though the lease previously belonged to a nonoperator who was unaware that it overlay the same reservoir as the unit. 499 P.2d at 417, 420. A similar result was reached in a case where the operator's adjacent well was draining gas from the unit; the court held that the operator had no duty to prevent the drainage, nor even a duty to inform the nonoperators of the drainage. *Tenneco Oil Co.*, 630 F. Supp. at 972.

Likewise, a court of appeals has denied nonoperators any share of the profits made by an operator who purchased condensate from the unit, refined it, and sold it at a price greater than that paid to the nonoperators. *Crosby-Mississippi Resources, Ltd. v. Saga Petroleum U.S., Inc.*, 767 F.2d 143, 145 (5th Cir. 1985). In each of these three cases, the courts reasoned that, whatever the duty owed, it could not extend beyond the specific land and activities encompassed by the operating agreement—it was not a fiduciary duty of disclosure and good faith among the parties, but a limited duty attached to the operating agreement. See *Crosby*, 630 F.2d at 146; *Tenneco*, 630 F. Supp. at 967; *Colpitt*, at 418, 419.

72. 282 Ark. 268, 668 S.W.2d 16 (1984).

73. *Id.* at 271, 668 S.W.2d at 17.

the operator to surrender the advantage it had gained by virtue of its position.

The duty to eschew unfair advantage is imposed in addition to the express duties of the operating agreement. However, the egregious conduct of the operator in *Hawkins* demonstrates that this additional duty is limited to extreme circumstances. These two aspects of the operator's duty—to observe the operating agreement and to avoid unfair advantage—are the only ones recognized in judicial opinions.⁷⁴

IV. DEFINING THE UNIT OPERATOR'S DUTY

The purpose of this comment is to propose that the duty of a unit operator be called simply the "operator's duty." The virtue of this term is that, unlike labels such as "fiduciary duty," it is unburdened with historical baggage. Moreover, by definition it accurately describes the operator's duty to nonoperators. The new term will force courts to inquire further about the nature of the operator's duty, rather than simply define the relationship or affix a fiduciary or trustee label and then impose a concomitant, perhaps inappropriate, duty.

A. *Direct Analysis of the Operator's Duty: A Two-Pronged Approach*

The proper legal analysis of the operator's obligations to nonoperators begins with a recognition that the operator owes an "operator's duty." That duty has not been expressly recognized by courts, but its two prongs can be derived from their decisions. First, the operator must observe the terms of the operating

74. The existing cases reveal only two aspects to the operator's duty. Circumstances might create other aspects of the duty. For example, an operating agreement might be so poorly drafted that a court would be forced to create the duties that would be embodied by a better agreement. Or an unfair agreement, executed by parties of unequal bargaining positions, might require additional duties.

However, the length and specificity of standard form operating agreements make these scenarios highly unlikely; in fact, the operator's duty can be limited to two prongs precisely because operating agreements are drafted so carefully, and because form agreements are employed even among parties of differing size and strength. See Young, *Oil and Gas Operating Agreements: Producers 88 Operating Agreements, Selected Problems and Suggested Solutions*, 20 ROCKY MTN. L. INST. 197, 199 (1975) ("It is presently believed that the Ross-Martin, now A.A.P.L. Form 610, has gained such general acceptance, even by major companies, that it may be considered a Standard Operating Agreement.").

The cases do not suggest any other duties, nor does this comment endorse them.

agreement, which places an outer bound on the operator's affirmative duties. The cases reveal that this prong of the duty is dispositive of almost all disputes⁷⁵ and that courts should look first to the operating agreements to resolve litigation among operators and nonoperators.⁷⁶

Second, the operator has a duty not to use its position to take advantage of the non-operators; the parties must be on equal footing in the unit operation. However, this aspect of the duty is limited—most courts censure only fraudulent or injurious conduct, and only some require that the operator share information and opportunities gained through its position.⁷⁷ Disclosure of this modicum of information promotes the formation of unit operations; without it, no one would likely consent to becoming a nonoperator, because to do so would be to give up unforeseen opportunities that might arise during operations. Therefore, the duty to share opportunities obtained through the operator's position probably should be part of the operator's duty.

The application of the operator's duty as defined above is direct; using this analysis, courts need not take the intermediate and inappropriate⁷⁸ step of defining the parties' relationship as a joint venture or partnership. Moreover, they need not describe the operator as a fiduciary or trustee, and in so doing encourage specious litigation by nonoperators seeking to impose strict fiduciary duties upon operators.

The nature of the two prongs suggests that the duty will be fact-specific, depending on the terms of the operating agreement and the parties' course of conduct. If their conduct significantly deviates from the terms of the operating agreement, the parties might indeed incur true fiduciary duties to one another.⁷⁹ Like-

75. See *supra* notes 46-47.

76. This conclusion was stated eloquently by the Tenth Circuit Court of Appeals in *Frankfort*:

The extent and effect of [a unit operating] relationship is determined by the written agreements between the parties defining and delineating the powers and rights of each. In such a situation it is presumed that they delegated all the powers they wished to confer upon each other and withheld all powers or authority not affirmatively delegated. The relationships between them are controlled by the terms of their agreements voluntarily made.

Frankfort Oil Co. v. Snakard, 279 F.2d 436, 443 (10th Cir. 1960) (footnotes omitted).

77. See *supra* notes 68-70 and accompanying text.

78. See *supra* notes 14-25 and accompanying text.

79. See *Envirogas, Inc. v. Walker Energy Partners*, 641 F. Supp. 1339, 1345 (W.D.N.Y. 1986) (contract disclaimed fiduciary duties, but court found that reality of

wise, they might engage in joint ventures or partnerships beyond the unit area and have concomitant duties in those activities. However, if the terms of the operating agreement are observed, the operator bears only an "operator's duty" with regard to the unit area.

B. Policy Reasons for a Two-Pronged Duty

Though rarely enunciated, sound policy reasons underlie the limitation of the operator's duty to observing the contract and avoiding personal advantage. Those reasons include (1) the usual intention of the parties to function as equals, (2) the nature of the operating agreement itself, and (3) the potential chilling effect of a full-fledged fiduciary or "trustee-type" duty.

First, the nature of the operator's duty recognizes the parties' usual intent to function as equals. In a typical unit, a group of adjacent lessees bands together to realize the advantages of unit operation.⁸⁰ One of them is designated unit operator. Because the operator reaps no "profit"⁸¹ from its position, the parties are situated equally—the goal of each is simply to maximize the amount of oil or gas extracted. The operator, receiving no additional benefit, should be subjected to no additional duty.⁸²

Second, the nature of the operating agreement defies typical fiduciary duties. Most agreements are lengthy contracts executed by sophisticated parties. Unlike joint ventures, agencies, or partnerships, which may arise inadvertently,⁸³ joint operation

relationship overrode disclaimer).

80. For a summary of these advantages, see *supra* notes 1-4 and accompanying text.

81. In other words, the operator charges nonoperators only for actual costs incurred in unit operations. See, e.g., *Beadle v. Daniels*, 362 P.2d 128, 130 (Wyo. 1961); 6 W. SUMMERS, *supra* note 5, § 1329 (Accounting Form to be Attached to Operating Agreements).

"Costs" may include salaries for the operator's employees; likewise, functioning as operator may create economies of size. However, the operator does not make a conventional accounting profit.

82. Benefit is not always requisite to establishing duty. However, in business settings, entities balance benefits and costs; the absence of benefit to the operator suggests that the operator does not expect special duties, nor have the nonoperators bargained for them.

83. See, e.g., *Opco, Inc. v. Scott*, 321 F.2d 471, 473 (10th Cir. 1963) (joint venture may arise out of acts and conduct); *Martin v. Peyton*, 246 N.Y. 213, 218, 158 N.E. 77, 78 (1927) (partnership may arise from any contract that "contemplates an association of two or more persons to carry on as co-owners a business for profit"); RESTATEMENT (SECOND) OF AGENCY § 1 comment b (1958) ("The relation which the law calls agency does not depend upon the intent of the parties to create it, nor their belief that they have done so.").

is recognized in the oil and gas industry as a formal relationship, defined carefully by the operating agreement. The duty owed is an aspect of the relationship that the courts expect the parties to specify in their agreement.⁸⁴

Moreover, the operating agreement is highly specific as to subject matter, time, and necessary functions. The geographic area covered by the operating agreement is specified precisely.⁸⁵ Further, because the underlying reservoir has a finite life, the duration of the relationship can be estimated.⁸⁶ Finally, the essential aspects of production are known by all the parties. Whether the agreement covers only production or encompasses processing and even joint marketing, the necessary activities can be anticipated and addressed in the parties' contract.

Furthermore, traditional fiduciary or trustee-type duties frequently would conflict with the express terms of the operating agreement.⁸⁷ For example, the agreement will often detail the

Under the law of partnership, partners are deemed to have fiduciary duties to one another, unless they agree otherwise. UNIF. PARTNERSHIP ACT §§ 18, 21 (1969). Thus, partners can agree specifically to limit their duties. The premise of this comment is that parties to an operating agreement do likewise; their lengthy, comprehensive agreement controls the duties to be imposed. See *supra* note 74.

84. In *Tenneco Oil Co. v. Bogert*, 630 F. Supp. 961 (W.D. Okla. 1986), a nonoperator alleged that the operator's activities on land adjoining the unit obligated it to drill offsetting density wells on the nonoperator's property. In holding that no such duty was created by the operating agreement, the district court noted: "Both of these parties are sophisticated participants in the business of developing oil and gas properties. It cannot be presumed that they were incapable of including an express provision in their agreement to create such a duty had they intended or desired to do so." *Id.* at 969. For a nearly identical conclusion, see *Crosby-Mississippi Resources, Ltd. v. Saga Petroleum U.S., Inc.*, 767 F.2d 143, 146 (5th Cir. 1985).

85. See Model Form 610, *supra* note 5, art. II (Exhibit "A"); 6 W. SUMMERS, *supra* note 5, § 1328 para. 4.

86. The term of many operating agreements is tied to the productive life of the unit. See, e.g. Model Form 610, *supra* note 5, art. XIII; 6 W. SUMMERS, *supra* note 5, § 1328 para. 10 (1967).

87. For an example of this problem, see *Andrau v. Michigan Wis. Pipe Line Co.*, 712 P.2d 372 (Wyo. 1986). In that case, the terms of the operating agreement granted the operator a lien on the working interests of the nonoperators for unpaid production expenses. *Id.* at 373. If a nonoperator failed to pay its proportionate share of production costs, the operator was empowered to foreclose on the nonoperator's entire working interest to satisfy the debts owed. *Id.* In addition, the operating agreement provided that any party who sold less than its full share of the gas produced would be credited with "gas in the bank." *Id.* In other words, that party would be treated as though it owned a greater proportion of the gas still in the reservoir, and could sell more than its share until the underproduction was eliminated.

One of the nonoperators, Andrau, failed to pay the invoices sent to him; the operator sought to foreclose on Andrau's working interest to satisfy the debt. Andrau protested, making an argument that might have been sound had the operator been a traditional

operator's duty to disclose information to the nonoperators;⁸⁸ however, the obligation so created may be below the duty of disclosure imposed on a traditional fiduciary.⁸⁹ To find true fiduciary duties, courts likewise would have to find a waiver of those duties wherever the operating agreement created lesser obligations.

Third, the operator's duty is limited because the prospect of a fiduciary duty would have a chilling effect on the formation of oil and gas units. Generally, the role of operator is assumed by the largest working interest owner. However, the largest owners are most capable of achieving efficient production outside of unit operation. The result of imposing fiduciary or trustee-type duties on the operator, with the accompanying prospect of "self-abnegation"⁹⁰ and astronomical liability, would be to drive large owners away from unitization. The small working interest owners, for whose benefit this strict duty would be imposed, could

fiduciary or trustee. Andrau asserted that the operator was bound to satisfy the debt by the least onerous means—in this case, by taking Andrau's "gas in the bank." *Id.* at 374.

However, the express terms of the operating agreement negated such a duty. If the court had placed the operator in the position of a true fiduciary, a concomitant duty to satisfy the debt in the least onerous manner would have conflicted with the specific provisions of the operating agreement. *Id.* at 376. The court refused to create that duty, holding that "[a]ppellant [Andrau] would have this court rewrite the agreement by limiting the operator's remedies because of a claimed fiduciary duty. . . . We refuse to do so." *Id.*

88. See, e.g., Model Form 610, *supra* note 5, art. VI-D; 6 W. SUMMERS, *supra* note 5, § 1328 para. 14.

89. See, e.g., *Frankfort Oil Co. v. Snakard*, 279 F.2d 436 (10th Cir. 1960), where a nonoperator alleged that the operator had breached a fiduciary duty by failing to disclose to the nonoperator certain information about the pooled area. However, the court of appeals held that the operator had satisfied its duty by simply making the information available for inspection, because the operating agreement required only that the operator provide access to the information. *Id.* at 442-43.

This result is consistent with the rule that the operator's duty may be limited in the operating agreement, both by broad disclaimers and by provisions authorizing specific acts. Moreover, the result is not inconsistent with the rule that the operator cannot use its position to gain unfair advantage over the nonoperators. The operator was bound in this case to disclose the information about the drilling operations; however, the operator's duty of disclosure was satisfied by compliance with the terms of the operating agreement.

90. See *supra* note 29.

not efficiently recognize the value of their interests.⁹¹ The clear public policy favoring unitization⁹² would be defeated.

IV. CONCLUSION

In conclusion, the operating agreement is the key to the operator's duty. In controlling the operator's duty, many courts have ventured beyond the operating agreements and have foundered on terms such as "joint venture," "fiduciary," and "trustee." As a result, though the cases are consistently resolved, potential litigants and the majority of commentators⁹³ have supposed that the operator's duty extends far beyond the scope of the operating agreement.

In substance, however, the operator is subject only to a two-pronged duty: (1) To observe the terms of the agreement and (2) to refrain from using the position to gain unfair advantage over the nonoperators. To ensure that courts do not encourage the unfounded expansion of this duty, the simple term "operator's duty," should be used to describe and apply the operator's unique, limited obligation to nonoperators.

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91. This argument seems to beg the question, "Wouldn't a small owner be willing to assume the operator's role, with its accompanying high duties?" The answer may be yes. However, in many instances, the small working interest owner is a minor player not just in the unit, but in the oil and gas industry as well. The small owner is likely incapable of operating the unit efficiently, if at all.

92. See *supra* note 2.

93. See, e.g., Boigon, *supra* note 7; Lane & Boggs, *supra* note 7; Williams, *supra* note 14.