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Ohio Weighs Post-Production Costs, Royalty Calculations

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AUTHORED ARTICLE | 6.5.2015

Oil and Gas Journal

Greg Russell, Pete Lusenhop and Steven Chang, attorneys in the Vorys Columbus office, co-authored an article for the June 2015 edition of the *Oil and Gas Journal* titled “Ohio Weighs Post-Production Costs, Royalty Calculations.” The article provided an in-depth look at how the competing “at-the-well” and “marketable product” approaches square with Ohio contract law, and how Ohio courts, including the Ohio Supreme Court, may view post-production cost deductions.

The article states:

“Post-production cost deductions are a common source of royalty litigation. Local lease-interpretation rules determine whether particular deductions are proper and defensible in court. Different jurisdictions, however, follow different rules to different ends.

Historically, a lease calling for a royalty based on the value of production at the wellhead has allowed the lessee to net-back post-production costs when determining the value of production upon which royalty calculations are based.

A countervailing theory, however, has been urged in some jurisdictions which requires the lessee to bear the costs of converting natural gas extracted at the wellhead into a marketable condition. This theory reasons that production—the sole responsibility of the lessee—was not complete until the gas was in a form in which it could be sold.

Under the “marketable product” theory, the lessee alone bears the cost of common post-production expenses for treating, compressing, dehydrating, and in some states, transporting oil and gas to a viable market.

Ohio has a long history of oil and gas production stretching back to the 19th Century. Recently, however, the Utica shale has become a major contributor to US oil and gas production. Yet the state has not directly addressed whether it follows the “at-the-

well” approach or some version of the “marketable product” theory. The Supreme Court of Ohio, however, may rule on the dilemma soon. A federal court certified this question to the Supreme Court of Ohio on April 1, 2015.”

To read the entire article, visit the *Oil and Gas Journal* [website](#). (Subscription required).