



OFFICE OF ATTORNEY GENERAL
STATE OF OKLAHOMA

ATTORNEY GENERAL OPINION
2015-6

The Honorable Mike Sanders
State Representative, District 59
2300 N. Lincoln Blvd., Room 205
Oklahoma City, Oklahoma 73105

September 1, 2015

Dear Representative Sanders,

This office has received your request for an Attorney General Opinion in which you ask, in effect, the following question:

Title 52 O.S.2011, § 570.10(D) specifies an interest rate of 12 percent owed to non-operating owners of interest in an oil and gas well's production when the holders of the proceeds from the first sale of oil or gas fail to distribute the proceeds within the time periods required by statute, unless the interest owner's title is unmarketable, in which case the applicable interest rate is 6 percent. Does this statute violate the special laws prohibition in Article V, Section 46 of the Oklahoma Constitution?

I.
BACKGROUND

In most cases, the proceeds from an oil or gas well are divided between the operator of the well, which typically leases the mineral rights, and non-operating owners of interest in the well's production, including royalty interest owners and investors. *See In re SemCrude, L.P.*, 407 B.R. 140, 145-47 (Bankr. D. Del. 2009) (recounting the history of oil and gas production, and regulation thereof, in Oklahoma). When the petroleum production is first sold, either the lessee operator or the first purchaser generally has the responsibility to distribute the proceeds of that sale to the various interest owners. *See Si M. Bondurant, To Have and to Hold: The Use and Abuse of Oil and Gas Suspense Accounts*, 31 OKLA. CITY U. L. REV. 1, 4 (2006) [hereinafter Bondurant].

For decades, oil and gas producers or first purchasers would for various reasons delay or decline to distribute the proceeds from the first sale to interest owners and use those funds for their own purposes until they were ultimately distributed, if at all. *Id.* at 1. Defects in the interest owner's title, liens against the title, failure to execute a division order, or inability to locate the owner sometimes caused the holder of the proceeds to suspend payments. *Id.* at 6. Often, however, holders of the production proceeds would fail to make any reasonable efforts to locate the interest owners or notify them of their interest, suspending payments until they were demanded and, in the meanwhile, gaining the benefit of the possession of those funds. *Id.* When payment was finally made, the holders often refused to make interest payments on the funds withheld. *Id.* at 17-18. "In the inflationary times of the late 1970s and early 1980s when the prime interest rate soared to 21.5%, there was a great incentive to delay royalty payments" and "many producers routinely suspended royalties and delayed payment for many months and even years to take advantage of the interest earned during the float between the receipt of sales proceeds and disbursement of royalties." *Id.* at 18. This not only deprived interest owners of the time-value of the money owed to them, it also gave rise to "an ever increasing case load of litigation between royalty owners and purchasers . . . precipitated by the use of suspense accounts." *Hull v. Sun Refining & Mktg. Co.*, 1989 OK 168, ¶ 9, 789 P.2d 1272, 1277.

These practices led many states to enact statutes specifying payment timing after the first sale of oil or gas production and, in the event of untimely payment, the applicable rate of interest. Bondurant, at 18. Oklahoma passed such a statute in 1980, which is now codified at 52 O.S.2011, § 570.10 and was enacted "to ensure that those entitled to royalty payments would receive proceeds in a timely fashion," evincing legislative "intent that it shall be the public policy in Oklahoma for royalty owners to receive prompt payment from the sale of oil and gas products." *Hull*, 1989 OK ¶ 14, 789 P.2d at 1279.

As currently written,¹ Section 570.10 requires that:

Proceeds from the sale of oil or gas production from an oil or gas well shall be paid to persons legally entitled thereto:

- a. commencing not later than six (6) months after the date of first sale, and
- b. thereafter not later than the last day of the second succeeding month after the end of the month within which such production is sold.

52 O.S.2011, § 570.10(B)(1).² The statute also specifies the timing of payments when the amounts owed are small. For example, accumulated unpaid amounts less than ten dollars may be

¹ Section 570.10 was originally enacted in 1980 as 52 O.S.Supp.1980, § 540. As part of the Production Revenue Standards Act of 1992, which "provides a comprehensive regulatory structure governing how interest owners and operators work together at the wellhead, and serves to hold operators accountable to their interest owners," *In re SemCrude*, 407 B.R. at 154, the former Section 540 was rewritten and recodified as new Section 570.10. 1992 Okla. Sess. Laws ch. 190, § 28.

held until production ceases, while amounts between ten and one hundred dollars must be remitted at least annually. *Id.* § 570.10(B)(3). When proceeds are not “paid prior to the end of the applicable time periods provided in [the] section, that portion not timely paid shall earn interest at the rate of twelve percent (12%) per annum to be compounded annually, calculated from the end of the month in which such production is sold until the day paid,” unless the reason for nonpayment is because the title to the mineral interest is unmarketable, in which case the statutory interest rate is 6 percent compounded annually. *Id.* § 570.10(D).³ A “first purchaser or holder of proceeds who fails to remit proceeds from the sale of oil or gas production to owners legally entitled thereto within the time limitations set forth” in the statute “shall be liable to such owners for interest” as specified by the statute. *Id.* § 570.10(E)(1).

II. LEGAL PRINCIPLES

Article V, Section 46 of the Oklahoma Constitution prohibits the Legislature from passing “any local or special law . . . Fixing the rate of interest[.]” A law is a “special law” if it “single[s] out less than an entire class of similarly affected persons or things for different treatment.” *Reynolds v. Porter*, 1988 OK 88, ¶ 14, 760 P.2d 816, 822. Article V does not prohibit all legislative classifications; a law that creates “a proper and legitimate classification” is not special. *City of Enid v. Pub. Emps. Relations Bd.*, 2006 OK 16, ¶ 13, 133 P.3d 281, 287. If there is “some distinctive characteristic upon which a different treatment may be reasonably founded, and that furnishes a practical and real basis for discrimination,” the statute is not a special law. *Burks v. Walker*, 1909 OK 317, ¶ 23, 109 P. 544, 549; *see also EOG Res. Mktg., Inc. v. Okla. State Bd. of Equalization*, 2008 OK 95, ¶ 20, 196 P.3d 511, 520-21. Rather, a statute is a special law if the classification it creates “is arbitrary or capricious” or fails to “bear[] a reasonable relationship to the object to be accomplished” and thus is “wholly unrelated to the object of the Act.” *City of Enid*, 2006 OK 16, ¶¶ 13, 16, 133 P.3d at 287-88.

Under these standards, a statute that is a special law legislating one of the subjects listed in Article V, Section 46 is “absolutely and unequivocally prohibit[ed].” *Reynolds*, 1988 OK 88 ¶ 17, 760 P.2d at 822-23. In other words, in a Section 46 analysis, “the only issue to be resolved is whether a statute upon a subject enumerated in that section targets for different treatment less than an entire class of similarly situated persons or things.” *Id.*; *see also Lafalier v. Lead-Impacted Cmtys. Relocation Assistance Trust*, 2010 OK 48, ¶ 26, 237 P.3d 181, 192.

² For royalty proceeds from the sale of gas, proceeds after the initial distribution must be paid “not later than the last day of the third succeeding month after the end of the month within which such production is sold[.]” with some exceptions. *Id.* § 570.10(B)(2)(b).

³ “Marketability of title shall be determined in accordance with the then current title examination standards of the Oklahoma Bar Association.” *Id.* § 570.10(D)(2)(a); *see also Hull*, 1989 OK 168, ¶ 9, 789 P.2d at 1277.

III. ANALYSIS

Any constitutional analysis proceeds “with great caution” and starts with “a presumption that every statute is constitutional.” *Lafalier*, 2010 OK 48, ¶ 15, 237 P.3d at 188-89. Thus, courts “indulge every possible presumption that an act of the Legislature was constitutional.” *Adwon v. Okla. Retail Grocers Ass’n*, 1951 OK 43, ¶ 11, 228 P.2d 376, 379. “If there is any doubt as to the Legislature’s power to act in any given situation, the doubt should be resolved in favor of the validity of the action taken by the Legislature.” *Draper v. State*, 1980 OK 117, ¶ 10, 621 P.2d 1142, 1146. As a corollary, “[r]estrictions and limitations upon legislative power are to be construed strictly.” *Id.* A law will be deemed unconstitutional only if it “is clearly, palpably, and plainly inconsistent with the Constitution.” *Lafalier*, 2010 OK 48, ¶ 15, 237 P.3d at 188; *see also Zeier v. Zimmer, Inc.*, 2006 OK 98, ¶ 12, 152 P.3d 861, 866.

Section 570.10 specifies the time frames in which the holders of the proceeds from the first sale of oil and gas must pay the rightful interest owners. To encourage compliance with this statutory duty of prompt payment, Section 570.10(D) provides a 12 percent rate of interest compounded annually for nonpayment, unless the reason for nonpayment is because the title is unmarketable. The statute thus sets forth a higher rate of interest for a class of individuals—petroleum producers or first purchasers owing sums to royalty or other interest owners with marketable title—as distinct from others failing to make timely payment under contract. For all other contractual debts, “[t]he legal rate of interest shall be six percent (6%) in the absence of any contract as to the rate of interest,” unless otherwise provided for by valid law. 15 O.S.2011, § 266. The question of whether Section 570.10 violates Article V, Section 46 turns on whether the statute “embrace[s] all of the class that should naturally be embraced” or whether, instead, it “rest[s] on a false or deficient classification.” *City of Enid*, 2006 OK 16, ¶ 20, 133 P.3d at 310 (Opala, J., dissenting) (citation omitted).

Given the immense importance of the industry and the unique legal relationships involved, “[t]he State of Oklahoma . . . has extensively and continuously regulated” the oil and gas industry. *Seal v. Corp. Comm’n*, 1986 OK 34, ¶ 45, 725 P.2d 278, 292; *see also Oryx Energy Co. v. Plains Res., Inc.*, 1994 OK CIV APP 185, ¶ 3, 918 P.2d 397, 399. The relationships and property interests involved in oil and gas leases are extraordinarily complex, involving numerous parties over long periods of time, and the disparities in economic power between oil producers or first purchasers and royalty or mineral interest owners is often very wide. Consequently, it is reasonable that the Legislature sought to “provide[] a comprehensive regulatory structure governing how interest owners and operators work together at the wellhead, and . . . to hold operators accountable to their interest owners.” *In re SemCrude*, 407 B.R. at 154.

As recounted above, the long history of petroleum producers or first purchasers wrongfully withholding production proceeds for their own profit led the Legislature to impose statutory timeframes within which payment must be made and a 12 percent rate to incentivize compliance with the statute. The holder of these proceeds thus possesses a “distinctive characteristic upon which a different treatment may be reasonably founded, and that furnishes a practical and real

basis for discrimination.” *Burks*, 1909 OK 317, ¶ 23, 109 P. at 549. This classification applies to all those similarly situated—those responsible for the distribution of petroleum production proceeds from the first sale—including both producers and first purchasers. Having created a right to prompt payment to combat the pervasive refusal to make contract payments to interest owners that was peculiar to first sales in the petroleum industry, the Legislature was free to impose a higher rate of interest to incentivize respect for that unique substantive right. *See State ex rel. Macy v. Bd. of Cnty. Comm’rs*, 1999 OK 53, ¶ 9, 986 P.2d 1130, 1143 (“[D]ifferent remedies may be based upon legislatively drawn criteria that distinguish different causes of action . . . based upon the nature of the substantive rights at issue.”). Thus, the class subject to the higher interest rate is not “false” or “deficient,” but rather embraces a natural and rational class of similarly situated persons. *City of Enid*, 2006 OK 16, ¶ 20, 133 P.3d at 297-98 (Watt, C.J., Opala, Taylor, Colbert JJ., dissenting) (citation omitted). For the same reasons, Section 570.10(D)’s rate of interest is not “arbitrary or capricious” and bears “a reasonable relationship to the object” of the statute. *Id.* (citation omitted). Accordingly, Section 570.10(D) is not a “special law” and, therefore, cannot be in violation of Article V, Section 46.⁴

Similarly, courts have upheld analogous laws setting a higher rate of interest in the face of special law challenges when those laws were justified by a rational and legitimate public policy. For example, a law allowing for a higher rate of interest for judgments in workers’ compensation suits is not an unconstitutional special law because the Legislature reasonably imposed that elevated rate to combat “frivolous appeals which . . . have often been prosecuted by less conscientious employers and insurance companies to ‘starve’ helpless victims of industrial injuries into early and cheap settlements.” *Cyrus v. Vierson & Cochran, Inc.*, 1981 OK CIV APP 40, ¶ 15, 631 P.2d 1349, 1354. In the case of Section 570.10, a similar history of abuse of modest interest owners by the holders of petroleum proceeds justifies the 12 percent interest rate. As another example, courts in other states with similar constitutional provisions have upheld elevated interest rate laws when rationally justified, permitting, for example, elevated interest rates on retail installment contracts because the costs of consumer lending (including increased risk of default, volume, and servicing costs) are higher than those for commercial loans to established businesses. *See Cesary v. Second Nat’l Bank of N. Miami*, 369 So.2d 917, 920-21 (Fla. 1979); *Cecil v. Allied Stores Corp.*, 513 P.2d 704, 710 (Mont. 1973); *but see Stanton v. Mattson*, 123 N.W.2d 844, 846-48 (Neb. 1963). Similarly, the common practice of unjustified impounding of proceeds in suspense accounts, often requiring interest owners to institute costly litigation, creates a greater risk of nonpayment that may justify a higher interest rate owed by oil and gas producers and first purchasers.⁵

⁴ Because this Opinion concerns the constitutionality of a statute, it should be considered advisory only. The Oklahoma Supreme Court “alone has the power to authoritatively determine the validity or invalidity of a statute.” *York v. Turpen*, 1984 OK 26, ¶¶ 10-12, 681 P.2d 763, 767.

⁵ In 1985, the Legislature deleted from the statute the phrase “as the penalty,” which originally appeared after the specification of the 12 percent rate. *See* 1985 Okla. Sess. Laws ch. 141, § 1; *see also Fleet v. Sanguine, Ltd.*, 1993 OK 76, ¶ 5 n.14, 854 P.2d 892, 895 n.14. As a result, courts have recognized that Section 570.10(D) is no longer construed as a penalty for certain purposes, such as determining the statute of limitations for a claim for the 12 percent interest or deciding whether the 12% rate precludes a punitive

For similar reasons, the disparate interest rates owed to those with and without marketable title does not create a special law in violation of Article V, Section 46, because the two groups are not similarly situated and the Legislature has rationally decided that liability for nonpayment of proceeds should be lower when the reason for nonpayment is legitimate questions concerning title. *See Tulsa Energy, Inc. v. KPL Prod. Co. (In re Tulsa Energy)*, 111 F.3d 88, 90 (when title is unmarketable, “[p]ublic policy requiring prompt payment of proceeds cannot spur on the party responsible for payment, because he cannot be, and is not, required to pay until the other party has cleared up his title”). Nor can it be said that those in the oil and gas industry are subject to a special law on interest rates as compared to other industries because other industries are not characterized by the same potential, incentives, and history of refusal to timely pay sums due and the frequent litigation that ensued. Even within the oil and gas industry, the special relationships and problems of distribution of proceeds at the wellhead pursuant to mineral leases sets these relationships in a different class than other contracts for petroleum products. Finally, that Section 570.10 specifies different time periods during which proceeds must be paid to interest owners does not create a special law fixing a rate of interest because, though the *amount* of interest due under the statute may vary depending on when various dollar thresholds are met (*e.g.*, \$10, \$25, or \$100), when interest does begin to accumulate, it does so at the same *rate* across classes.

Even if there were doubt about the purposes of the statute, the effect of its revisions, or the unique situation of the oil and gas industry that by nature justifies its regulation as a class, those doubts must “be resolved in favor of the validity of the action taken by the Legislature.” *Draper*, 1980 OK 117, ¶ 10, 621 P.2d at 1146. Indulging “every possible presumption that [this] act of the Legislature was constitutional,” *Adwon*, 1951 OK 43, ¶ 11, 228 P.2d at 379, it cannot be said that Section 570.10(D) is “clearly, palpably, and plainly inconsistent with the Constitution,” *Lafalier*, 2010 OK 48, ¶ 15, 237 P.3d at 188. Section 570.10(D) does not “single out less than an entire class of similarly affected persons or things for different treatment.” *Reynolds*, 1988 OK 88, ¶ 14, 760 P.2d at 822. Rather, in light of the unique history, relationships, and importance of the use of suspense accounts by oil and gas producers and first purchasers to unjustifiably delay payment to interest owners, the Legislature has recognized “a proper and legitimate classification” by providing for a higher rate of interest when the holder of proceeds delays distribution of sums to the rightful owner in violation of the statute. *City of Enid*, 2006 OK 16, ¶ 13, 133 P.3d at 287. The elevated rate of interest is not “arbitrary or capricious,” but rather facilitates compliance with the prompt payment requirements of the statute, “bear[ing] a reasonable relationship to the object to be accomplished.” *Id.* ¶¶ 13-16, 133 P.3d at 287-88 (citation omitted).

damages award. *See Purcell v. Santa Fe Minerals, Inc.*, 1998 OK 45, ¶¶ 15-22, 961 P.2d 188, 192-93; *Hebble v. Shell Western E & P, Inc.*, 2010 OK CIV APP 61, ¶ 22, 238 P.3d 939, 946. But it is clear from the text and history of the statute, which has seen its core provisions maintained despite several revisions, that the Legislature still intends that Section 570.10(D) promote timely distribution of proceeds to oil and gas interest owners. *See Hull*, 1989 OK 168, ¶ 14, 789 P.2d at 1279. Deletion of the phrase “as a penalty” does not change the purposes of and justifications for Section 570.10(D) and does not render it an irrational classification prohibited by Article V, Section 46. Mere removal of three words does not render the law unconstitutional.

It is, therefore, the official Opinion of the Attorney General that:

Title 52 O.S.2011, § 570.10(D) is not a special law fixing the rate of interest in violation of Article V, Section 46 of the Oklahoma Constitution because it does not single out similarly affected persons for disparate treatment, but rather rests on a proper and legitimate classification.



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