UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF MISSOURI
EASTERN DIVISION

In re: **PATRIOT COAL CORPORATION, *et al.*,** **Debtors.**[1]	**Chapter 11** **Case No. 12-51502-659** **(Jointly Administered)** **Hearing Date:** **May 21, 2013 at 10:00 a.m.** **(prevailing Central Time)** **Hearing Location:** **Courtroom 7 North** **Re: ECF Nos. 1995, 2056, 3419, 3870, 3941**

PANTHER LLC'S MEMORANDUM OF LAW UPON THE DEBTORS' MOTION TO ASSUME LEASES AND CURE DEFAULTS AND IN OPPOSITION TO THE PAYNE-GALLATIN OBJECTION TO DEBTORS' MOTION FOR AUTHORIZATION TO (i) ASSUME OR (ii) REJECT UNEXPIRED LEASES OF NONRESIDENTIAL REAL PROPERTY WITH RESPECT TO DEBTORS' CONTRACT ID LND 323

[1] The Debtors are the entities listed on Schedule 1 to the Assumption Motion, as defined below. The employer tax identification numbers and addresses for each of the Debtors are set forth in the Debtors' chapter 11 petitions.

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Pursuant to the Agreed Scheduling Stipulation and Order Upon the Debtors' Motion to Assume Leases and Cure Defaults and the Objection of Payne-Gallatin Company ("**Payne-Gallatin**") [ECF No. 3870] (the "**Scheduling Order**"), Debtor Panther LLC ("**Panther**," and together with Payne-Gallatin, the "**Parties**"), one of the affiliated debtor entities in the above-captioned chapter 11 cases, respectfully submits this memorandum of law regarding the calculation of wheelage royalties under the lease executed on October 15, 1976 by and between Payne-Gallatin Mining Company and Ocamco (the "**Lease**"), and in opposition to the Payne-Gallatin Objection [ECF No. 2056] (the "**Objection**") to the Debtors' Motion for Authorization to (i) Assume or (ii) Reject Unexpired Leases of Nonresidential Property [ECF No. 1995] (the "**Assumption Motion**").

PRELIMINARY STATEMENT

This matter concerns the calculation of "wheelage royalties" under the Lease. A "wheelage royalty" is a royalty paid in exchange for the right to transport coal across a property.[2] Panther does not currently mine coal from the premises demised by the Lease (the "**Lease Premises**"), but instead transports coal mined from other lands to Panther's Coal Clean Preparation Plant Complex (as defined in the joint Stipulation of Facts [ECF No. 3941]) on the Lease Premises. At the Coal Clean Preparation Plant Complex, the coal that Panther transports across the Lease Premises (the "**Wheeled Coal**") is processed and then loaded onto trucks for transport to destinations beyond the Lease Premises.

Under Article II of the Lease, the wheelage royalty is a fixed percentage of the "gross sales price" of the Wheeled Coal. The Lease defines "gross sales price" to mean "the actual

[2] See, e.g., Ark Land Co. v. Harlan Lee Land, LLC, No. 10-09-GFVT, 2010 U.S. Dist. LEXIS 99390, at *10 (E.D. Ky. Sept. 22, 2010).

price paid for coal sold to a bona fide purchaser f.o.b. the loading plant after final preparation and loading" less certain deductions not at issue here. (Lease, Art. II.1. (emphasis added).) Therefore, as explained in detail below, the "gross sales price" is the price that Panther could obtain for the Wheeled Coal after it has been processed and loaded onto trucks for transportation off the Lease Premises at the Coal Clean Preparation Plant Complex – i.e., the "loading plant" on the Lease Premises. In short, the "gross sales price" is the price that Panther would obtain for the Wheeled Coal if sold to a customer immediately after it is loaded onto trucks at the Coal Clean Preparation Plant Complex.

An "f.o.b." term is a common and well-recognized industry term, defined in both the Uniform Commercial Code and the West Virginia Code. It means that the seller of the item to be delivered bears all the costs and risks related to the transportation of the item up to the specified location – in the Lease, the "loading plant" – and does not bear those costs and risks beyond that point. E.g., DiMare Homestead, Inc. v. Alphas Co. of N.Y., Inc., 2012 U.S. Dist. LEXIS 48546, at *5 (S.D.N.Y. Apr. 5, 2012). Thus, to calculate the "gross sales price" under the Lease, one deducts all transportation-related costs for the Wheeled Coal after it has been processed and loaded onto trucks at the Coal Clean Preparation Plant Complex from the price paid by a customer for the Wheeled Coal. That is precisely the way that Panther has always calculated the "gross sales price" of the Wheeled Coal when calculating the wheelage royalties owed to Payne-Gallatin under the Lease.

Now, for the first time, Payne-Gallatin asserts that the "gross sales price" should include transportation-related costs that Panther incurs after the Wheeled Coal is loaded onto trucks at the Coal Clean Preparation Plant Complex. (Objection, at 2.) Payne-Gallatin's motivation is clear: if rail and other transportation-related costs are included in the "gross sales price," then

Payne-Gallatin's "wheelage royalty" would be higher. But while its motivation is clear, its legal basis for this novel claim is not. In fact, despite repeated requests from Panther and its counsel, Payne-Gallatin has refused to explain how the plain language of the Lease supports its newfound interpretation and its claim for additional wheelage royalties going back ten years. Panther will learn the basis for Payne-Gallatin's interpretation of the Lease at the same time that the Court does.

Payne-Gallatin's interpretation – whatever its basis may be – cannot be squared with the plain and unambiguous language of the Lease. The Lease expressly defines "gross sales price" to mean the price of the Wheeled Coal "f.o.b. the loading plant after final preparation and loading" – which means that, by definition, it excludes all transportation-related costs incurred after the Wheeled Coal has been processed and loaded onto trucks at the Coal Clean Preparation Plant Complex. Payne-Gallatin's contrary claim that "gross sales price" includes transportation costs after the Wheeled Coal leaves the loading plant requires reading the f.o.b. term out of the Lease.

The West Virginia Supreme Court's decision in U.S. Steel Mining Co. v. Helton, 631 S.E.2d 559 (W. Va. 2005), is directly on point. In that case, the court held that an 'F.O.B. ['Free on Board'] Mine' price" used to calculate coal severance taxes means that "any transportation costs from the preparation plant to the port and thereafter to the customer, if they are absorbed or paid by the seller, are deducted from the actual sales price." Id. at 561 (emphasis in original). That decision decides this case. Just as the f.o.b. provision in Helton permitted the coal producer to deduct all transportation-related costs beyond the preparation plant at the mine site, so too does the f.o.b. provision here permit Panther to deduct all transportation-related costs beyond the loading plant on the Lease Premises.

Payne-Gallatin's interpretation of the Lease is also inconsistent with the purpose of the wheelage royalty. A wheelage royalty is designed to compensate a lessor for the fact that heavy trucks are hauling coal from other lands across the leased premises. See Ark Land, 2010 U.S. Dist. LEXIS 99390, at *10. The f.o.b. term in the Lease thus fixes the royalty to the price of the Wheeled Coal at the location where it is loaded onto trucks for departure from the Lease Premises. See Lewis v. Bluefield, 188 S.E. 237, 240 (W. Va. 1936) (purpose of f.o.b. provision was "fixing the full price"). By contrast, under Payne-Gallatin's novel (and as yet unexplained) interpretation of the Lease, the "gross sales price" would also include rail and other transportation-related costs incurred after the Wheeled Coal leaves the Lease Premises, even though that transportation does not burden the Lease Premises.

Payne-Gallatin's Objection to the Debtors' Assumption Motion is baseless and is nothing more than an attempt to use the bankruptcy process as leverage to extract contractual concessions from a debtor. Payne-Gallatin's opportunistic attempt to rewrite the Lease should be rejected, and the Debtors' Assumption Motion with respect to the Lease should be granted.

STATEMENT OF FACTS

A. Background

Per the Stipulation of Facts [ECF No. 3941] (the "**Stipulation of Facts**") entered into among the Parties, Panther has been a lessee under the Lease since March 16, 1999. (Stipulation of Facts ¶¶ 6, 9.)[3]

In addition to rent and other royalties, the Lease calls for the payment of wheelage royalties by Panther to Payne-Gallatin for Wheeled Coal "transported over, through, under and

[3] On September 8, 2006, Panther and Payne-Gallatin renewed the Lease, on the same terms as the original Lease, for an additional 15 years.

upon the demised premises or processed through a cleaning plant on the demised premises." (Lease, Art. II.2.) The wheelage royalty owed by Panther to Payne-Gallatin under the Lease equals one half of one percent of the "gross sales price" of such coal. (Id.)[4]

The Lease defines the "gross sales price" as "the actual price paid for coal sold to a bona fide purchaser f.o.b. the loading plant after final preparation and loading" less certain deductions not at issue here. (Id. at II.1.) "[F]inal preparation and loading" occurs on the Lease Premises at the Coal Clean Preparation Plant Complex, which encompasses "a coal preparation plant and a truck loading facility," and at which the coal is "crushed, washed, and dried, then moved . . . to a clean coal stockpile" and ultimately "loaded onto trucks," which "haul the coal to various sites off the demised premises." (Stipulation of Facts ¶¶ 12-14.)

B. Procedural History

On December 14, 2012, Payne-Gallatin filed a proof of claim [E.D. Mo. Claim No. 2257] (the "**Proof of Claim**"), contending for the first time that Panther had underpaid the wheelage royalty for the previous ten years as a result of "deduction of trucking and rail expenses from the gross sales price of coal crossing [the] Lease premises," and claiming $399,658 in royalties due. (Proof of Claim, at ii.)

On January 15, 2013, the Debtors filed the Assumption Motion requesting authorization to assume the Lease and numerous other real property leases. On January 22, 2013, Payne-Gallatin filed its Objection to the Assumption Motion, asserting again that Panther impermissibly took wheelage royalty "deduction[s] of trucking and rail expenses" of $399,658 over the past ten

[4] The royalty is also subject to a ten cent per net ton of Wheeled Coal minimum. (Lease, Art. II.2.) That minimum is not at issue here.

years, claiming that amount as cure necessary to assume the Lease.[5] Payne-Gallatin then moved to direct the Debtors to file a response to the Objection.[6] On April 30, 2013, the Court approved a Scheduling Order agreed by and between the Parties, which provides for initial resolution of the legal issue regarding the meaning of the term "gross sales price" under the Lease, to be followed, if necessary, by a determination by the Court of damages, if any, available to either Party. (Scheduling Order ¶¶ 1, 5(c).) On May 6, 2013, the Parties agreed to a Stipulation of Facts setting forth the Parties' relationship, the relevant provisions of the Lease, and the process by which coal is prepared and loaded on the Lease Premises.

ARGUMENT

A. The Plain Language of the Lease Permits Deduction of Transportation-Related Costs Beyond the Loading Plant

The sole issue in this case is whether or not the definition of the term "gross sales price" in the Lease permits Panther's deductions of transportation-related costs beyond the loading plant. Article II.1 of the Lease defines "gross sales price" to "mean the actual price paid for coal sold to a bona fide purchaser f.o.b. the loading plant after final preparation and loading" less certain additional deductions not at issue here. (Lease, Art. II.1 (emphasis added).)

The Lease is governed by the laws of the State of West Virginia. (See Lease, Arts. XI, XX.) Under West Virginia law, the "plain and unambiguous language" of a lease "should be applied and enforced according to its plain intent and should not be construed." Cabot Oil & Gas Corp. v. Pocahontas Land Corp., 376 S.E.2d 94, 96 (W. Va. 1988).

[5] Payne-Gallatin additionally claimed as cure certain other unpaid pre-petition property tax and wheelage royalty payments, which are not in dispute.

[6] Payne-Gallatin also moved for mediation of the dispute, to which the Debtors filed a limited objection [ECF No. 3664], but Payne-Gallatin subsequently withdrew its mediation request at the April 23, 2013 Status Hearing before the Court.

"F.o.b." is a common industry term with a defined meaning under both the Uniform Commercial Code (the "**UCC**"), and the West Virginia Code. The West Virginia Code adopts the UCC's definition of "f.o.b." verbatim:

> Unless otherwise agreed the term F.O.B. (which means 'free on board') at a named place, even though used only in connection with the stated price, is a delivery term under which . . . the seller must at his own expense and risk transport the goods to that place.

W. Va. Code § 46-2-319(1); U.C.C. § 2-319(1).[7]

As is plain from the Lease, the Parties have not specified a different definition of "f.o.b." than is supplied in the UCC and the West Virginia Code, and accordingly the standard definition applies here and establishes the point at which the "gross sales price" is calculated. Pursuant to that definition, costs related to the transportation of goods are at the seller's (Panther's) expense and therefore included in the "gross sales price" up to, and no further than, the location following the f.o.b. term, here "the loading plant." W. Va. Code § 46-2-319(1); see also Black's Law Dictionary 642 (6th ed. 1990) ("F.O.B.: Free on board some location (for example, FOB shipping point; FOB destination). A delivery term which requires a seller to ship goods and bear the expense and risk of loss to the F.O.B. point designated. The invoice price includes delivery at seller's expense to that location." (emphasis added)).

Accordingly, the f.o.b. term means that transportation of the good (here, coal) beyond the designated point (here, the loading plant) is not at the seller's expense. See, e.g., DiMare Homestead, 2012 U.S. Dist. LEXIS 48546, at *5 ("A sales contract containing F.O.B. shipping terms indicates that transportation expenses and the risk of loss for the goods passes from the seller to the buyer at the specified location."). Thus, because the Lease specifies that the "gross

[7] The location after the "f.o.b." term may refer to either the place of shipment or the place of destination. W. Va Code § 46-2-319(1)(a)-(b). Either way, however, the seller bears the expense and risk only until the location specified. Id.

sales price" used to calculate the wheelage royalty must include Panther's transportation-related costs up to the "loading plant after final preparation and loading," any such costs thereafter are necessarily excluded from the "gross sales price" calculation and must be deducted. See, e.g., Conoco, Inc. v. Inman Oil Co., 774 F.2d 895, 901 (8th Cir. 1985) ("Conoco began pricing its gasoline f.o.b. the terminal and its packaged lubricants f.o.b. the supply point. The price of these products was accordingly reduced to reflect the cost of transportation only as far as the f.o.b. point . . . .").

Indeed, the West Virginia Supreme Court expressly addressed the meaning of an f.o.b. price in U.S. Steel Mining Co. v. Helton. There, the court held that, in order to obtain what "is referred to in industry parlance as the coal's 'F.O.B. ['Free on Board'] Mine' price" to determine state severance tax collections, "any transportation costs from the preparation plant to the port and thereafter to the customer, if they are absorbed or paid by the seller, are deducted from the actual sales price." U.S. Steel Mining, 631 S.E.2d at 561 (emphasis in original). Precisely the same is true here with respect to any transportation costs from the loading plant to the customer. Helton alone decides this case.

Indeed, Payne-Gallatin's interpretation would read the term "f.o.b. the loading plant" entirely out of the Lease. Under Payne-Gallatin's interpretation, according to which Panther may not deduct any transportation-related costs in calculating "gross sales price" under the Lease, the f.o.b. term is meaningless. It is an elementary rule of contractual interpretation that contracts will not be interpreted to render a word or clause completely meaningless. E.g., Moore v. Johnson Serv. Co., 219 S.E.2d 315, 321 (W. Va. 1975) (holding that it is a "rule of general application that, in the construction of contracts, words or clauses are not to be treated as

meaningless or discarded if any reasonable meaning consistent with the other parts of the contract can be given them").

By contrast, Panther's interpretation of the Lease is perfectly sensible. The purpose of a wheelage royalty is to compensate the lessor for "the right to transport coal across the [demised premises]." Ark Land, 2010 U.S. Dist. LEXIS 99390, at *10. The f.o.b. provision serves this objective by fixing the royalty to the price of the coal at the precise location at which the coal is loaded onto trucks for departure from the Lease Premises, i.e., the loading plant. See (Stipulation of Facts ¶¶ 12-14 (stipulating that trucks loaded at the "Coal Clean Preparation Plant Complex" then "haul the coal to various sites off the demised premises")); Lewis, 188 S.E. at 240 (purpose of f.o.b. provision was "fixing the full price" of the contract on which to calculate a sales tax).

Under Payne-Gallatin's interpretation of the Lease, Payne-Gallatin's wheelage royalty would vary for reasons that have nothing to do with compensating Payne-Gallatin for Panther's use of the Lease Premises. Payne-Gallatin would simply receive a windfall royalty from any transportation-related costs incurred by Panther to deliver coal after it leaves the Lease Premises, transportation that by definition does not burden Payne-Gallatin's premises at all. Indeed, the further away from the Lease Premises that Panther must deliver the Wheeled Coal, the greater Payne-Gallatin's royalty would be. Such an interpretation defies the plain language of the Lease and is contrary to the very purpose of the wheelage royalty, which is to compensate Payne-Gallatin for the use of its Lease Premises.

CONCLUSION

For the foregoing reasons, Panther respectfully requests that the Court deny Payne-Gallatin's Objection with prejudice and grant the Debtors' Assumption Motion with respect to the Lease.

Dated: New York, New York
May 8, 2013

Respectfully Submitted,

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