# **Legal Developments in 2014 Affecting the Oil and Gas Exploration and Production Industry**

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**Text**

As a preliminary qualification, the ongoing growth in the ***oil*** and gas industry has led to a significant increase in both the number of active ***oil*** and gas states and the number of new developments in the traditionally-active states. In view of space limitations, only certain of the more-significant developments are covered in this report.

I. ALASKA

*A. Legislative Developments*

A referendum to repeal SB 21

At the very end of the 2014 legislative session the Alaska State Legislature passed HB 287

In May 2014 the governor signed SB 138

*B. Judicial Developments*

In *Alaska* ***Oil*** *& Gas Ass'n v. PritzkerErignathus barbatus nauticus* subspecies) as threatened under the Endangered Species Act. In overturning the listing, the court said that NMFS had failed to identify threats to the seal that were immediate enough. The court held that the listing was arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law. The listing could have significantly impacted permits and authorizations for ***oil*** and gas development (including seismic exploration) in the Bering, Beaufort, and Chukchi seas.

In *Kunaknana v. U.S. Army Corps of Engineers*,

In *Native Village of Point Hope v. Jewell*,

In *Reese v. Malone*,

In *Shell Gulf of Mexico Inc. v. Ctr. for Biological Diversity, Inc.*,

In December 2014, the U.S Department of Justice announced that Noble Drilling LLC, the drilling operator of Shell's drill rig that ran aground south of Kodiak Island, Alaska, will plead guilty to eight felony offenses, and pay $ 12.2 million in fines and community service payments, stemming from environmental and safety violations aboard its vessels. Under the terms of the plea agreement, Noble admits that it knowingly made false entries and failed to record its collection, transfer, storage and disposal of ***oil*** in its drill ship Noble Discoverer and drill rig Kulluk's ***Oil*** Record Books.

In *BP Pipelines (Alaska) Inc. v. State, Dep't of Revenue*,

In *Denali Citizens Council v. State, Dep't of Natural Res*.

*C. Administrative Developments*

The Alaska ***Oil*** and Gas Conservation Commission adopted new regulations

II. ARKANSAS

*A. Judicial Developments*

The case of *Lewis v. EnerQuest* ***Oil*** *and Gas, LLC*

In *Hiser v. XTO Energy Inc.*,

An ***oil*** and gas lease contained lessor-drafted language obligating the lessee Pathfinder to drill five wells during the lease's primary term or pay liquidated damages. Pathfinder released the lease in order to avoid drilling those wells or paying the liquidated damages. The lessor sued, seeking judgment for the liquidated amount. The court awarded summary judgment to the lessee, which was affirmed on appeal in *First Tennessee Bank National Ass'n v. Pathfinder Exploration, LLC*, *Frein v. Windsor Weeping Mary, L.P*.

In *Chesapeake Exploration, LLC v. Whillock*,

*B. Administrative Developments*

As is its practice, the Arkansas ***oil*** and Gas Commission made minor revisions to several of its regulations during 2014. Since these regulations are constantly in revision, the practitioner is advised to regularly check these regulations, online at http://www.aogc.state.ar.us.

III. CALIFORNIA

*A. Legislative Developments*

The California Legislature passed two new bills to supplement Senate Bill 4,

In the interim, DOGGR adopted interim emergency regulations to allow hydraulic fracturing and other well stimulation operations pending the adoption of final regulations.

SB 861 deleted a prohibition, previously set forth in Public Resources Code section 3160(c)(2)(B), on additional environmental review or the imposition of additional mitigation measures for well stimulation activities if the Supervisor of DOGGR determined that the activities proposed in a well stimulation permit application met the requirements of the California Environmental Quality Act.

SB 861 also amended the Lempert-Keene-Seastrand ***Oil*** Spill Prevention and Response Act

Reflecting public concern regarding water usage in ***oil*** and gas operations, Section 3227 of the Public Resources Code was amended by SB 1281

*B. Judicial Developments*

The correct valuation method for property tax assessment purposes of replacement wells, that is, wells which are drilled to replace an existing producing well, was addressed in *Chevron U.S.A. Inc. v. County of* ***Kern***.

Chevron challenged the ***Kern*** County Assessor's use of a cost approach, which looks to the costs of drilling the well, in issuing a supplemental assessment with respect to Chevron's replacement wells. Chevron contended that the proper method was an income approach, based on the increase in income from the producing property attributable to the replacement wells. The court of appeal rejected Chevron's arguments, holding that a new well or a replacement well is valuable and taxable, regardless of whether it leads to the discovery of new reserves and that the cost method of appraising such wells was not in excess of the assessor's discretion and did not result in an unconstitutional double assessment. The court also rejected Chevron's argument that a replacement well should not be subject to a supplemental assessment and was not subject to the repair and maintenance exemption.

*C. Administrative Developments*

Following the enactment of Senate Bill 4 in 2013, DOGGR recommenced the administrative rulemaking process to develop and implement the new law. Since operators were required to comply with Senate Bill 4's requirements beginning January 1, 2014, DOGGR adopted emergency interim regulations effective January 1, 2014, pursuant to California Public Resources Code section 3161(b) and California Government Code section 11346.1(b), to govern ***oil*** and gas well stimulation treatment operations until its proposed permanent regulations are completed and become effective. On June 27, 2014, DOGGR readopted its SB 4 interim well stimulation treatment regulations. These interim regulations, which became effective on January 1, 2014, will remain in effect until DOGGR's final regulations become effective on or before July 1, 2015.

The interim regulations address hydraulic fracturing, acid fracturing and acid matrix stimulation.

DOGGR's permanent well stimulation regulations were scheduled to be completed by January 1, 2015 and effective by no later than July 1, 2015.

On December 8, 2014, DOGGR issued a "Notice to Operators" regarding the Division's implementation of the quarterly water reporting requirements of SB 1281, advising operators of DOGGR's new water reporting form.

As part of the implementation of Senate Bill 4, DOGGR and the State Water Resources Control Board have also drafted a Memorandum of Agreement

The Bureau of Land Management issued internal guidance through an Instructional Memorandum CA-2014-031 (IM), directing its field offices to require operators of federal ***oil*** and gas leases in California to submit to BLM the same information that is required by the State of California through SB 4 as part of their Application for Permit to Drill and related Sundry Notices.

IV. COLORADO

*A. Legislative Developments*

During the 2014 session, the Colorado legislature passed a bill increasing the fines that the Colorado ***Oil*** and Gas Conservation Commission ("COGCC") can impose on ***oil*** and gas companies that violate the agency's regulations or a permit. House Bill 14-1356

*B. Judicial Developments*

In *Phathong v. Tesco Corp. (U.S.*), Colo. Rev. Stat. § 8-41-401, so the operator was not immune from liability for common law negligence. The Tenth Circuit reversed and ordered that judgment be entered for the operator because the work contracted out by the operator was an important, routine, and regular part of operator's casing and drilling services business and operator was entitled to immunity from common law negligence claims.

*Sinclair Transp. Co. v. Sandberg*

The court in *San Juan Citizens Alliance v. United States Dep't of Interior*

The court in *High Country Conservation Advocates v. United States Forest Serv*.

The Colorado Supreme Court considered the "infamous rule against perpetuities" in *Atl. Richfield Co. v. Whiting* ***Oil*** *& Gas Corp*.

In *Entek GRB, LLC v. Stull Ranches, LLC*,

In *Spring Creek Exploration & Prod. Co., LLC v. Hess Bakken Inv. II, LLC*,

In *Cook v. PenSa, Inc.*,

The court considered the access rights of a lessee of federal ***oil*** and gas interests in *Maralex Res., Inc. v. Chamberlain*.

In addition, in *BP Am. Prod. Co. v. Colorado Dep't of Revenue*,

Press reports also show that a decade-long legal battle over 19 leases of federal land northwest of Rifle, Colorado, issued in 2008 has been resolved. All but two of the 19 leases issued on the Roan Plateau will be cancelled, the government will reimburse the lessee, and drilling will be allowed on land in canyons and around the base of the plateau, once the BLM completes a large-scale plan for limiting surface impact.

In 2014, district court judges struck down three of the five local government bans on hydraulic fracturing that were approved by voters in 2012 and 2013 and challenged by the Colorado ***Oil*** and Gas Association (COGA), an industry group. In COGA's case against Longmont, the judge issued a summary judgment order

*C. Administrative Developments*

The COGCC amended Rule 906 relating to reporting of spills and releases, effective February 1, 2014. This rule implemented the bill passed by the Colorado legislature in 2013 that reduced the threshold for spills outside of berms or other secondary containment that must be reported to the COGCC and local authorities from five barrels to one barrel.

As evidenced by local government bans on hydraulic fracturing and related litigation discussed above, the extent to which local governments can control ***oil*** and gas development continues to be a very divisive issue in Colorado. Faced with the likelihood of numerous competing ballot measures proposed by environmentalists and the ***oil*** and gas industry relating to local control of ***oil*** and gas development and well setbacks,

V. KANSAS

*A. Judicial Developments*

As reported last year, gas injected into a gas storage reservoir that migrates beyond the authorized storage boundaries, and beyond "adjoining property" and into non-adjoining property, is not protected from the rule of capture by K.S.A. 55-1210(c).

In *Northern Natural Gas Co. v. Approximately 9117 Acres*, *Northern Natural Gas Co. v. ONEOK Field Services Co.*, K.S.A. 55-1210 recognized a present property interest in the migrated storage gas in place. Therefore, Northern was obligated to compensate the landowners for Northern's storage gas remaining beneath their land at the time of condemnation.

The court's holding appears questionable at two levels. First, if Northern is denied the protections of K.S.A. 55-1210, and the landowner is able to exercise its unrestrained capture rights recognized in the *Anderson* case, Northern should have the benefit of the *Union Gas* condemnation principles. Second, the "property right" possessed by the non-adjoining landowner has always been limited to the self-help remedy of "capture." This should not confer any right on the landowner to in-place storage gas it is unable to produce prior to condemnation.

In *Biery v. United States*

Last year's report noted that *Sieker v. Faye M. Stephens TrustNovy v. Woolsey Energy Corporation*. *Novy* the court held the lessor failed to carry its burden of proving the lessee did not act as a prudent operator in electing to forego further drilling operations on the leased land.

*In the Matter of the Protest of Barker*

The court in *Arkalon Grazing Association v. Chesapeake Operating, Inc.*

VI. LOUISIANA

*A. Judicial Developments*

In *Gatti v. State of Louisiana*,  La. Rev. Stat. § 30:12 for challenging unit orders was not exclusive. The Louisiana Supreme Court granted writs and reversed the court of appeal by reinstating the trial court's original decision. Because the case was dismissed on procedural grounds, the merits of Plaintiffs' claims were not reached.

*Hayes Fund for the First United Methodist Church of Welsh, LLC v. Kerr-McGee Rocky Mountain, LLC*La. Rev. Stat. § 31:122. The wells in question produced for several years and were reworked prior to ultimately ceasing production. One well ceased producing as a result of water zones mixing with ***oil*** and gas zones, while the other well ceased producing because extraneous water entered the well through casing leaks. Plaintiffs claimed both wells were imprudently operated and, as a result, Kerr-McGee left valuable hydrocarbons unrecoverable resulting in substantial pecuniary damages in the form of lost royalties for which plaintiffs asserted Kerr-McGee was responsible. After a lengthy trial, the district court dismissed all of plaintiffs' claims. The appellate court reversed and rendered a money judgment in favor of plaintiffs in the amount of $ 13,437,895. It found, *inter alia*, that the district court erroneously concluded that "industry-wide criteria for an effective cement job to assure zonal isolation did not apply to cementing drill pipe in the wellbore."

The subsequent purchaser doctrine in legacy lawsuits received further articulation and application by two appellate court decisions: *Boone v. Conoco Phillips Co.Global Marketing Solutions, LLC v. Blue Mill Farms, Inc.Boone* and *Global Marketing* involved subsequent purchasers who did not acquire the personal right to sue for property damage pre-dating their acquisitions in their original purchase of their property. The appellate courts concluded that the right to sue for property damage is a *personal* right for damages, not a *real* right that runs with the land. This was the result even though the Plaintiffs in *Boone* sought to resolve the lack of an express assignment by obtaining what the appellate court termed "eleventh hour assignments" *Boone* court found that the subsequent purchaser doctrine applies to both contract and tort, and there were no remaining personal claims to transfer in the latehour assignments. Both *Boone* and *Global Marketing* also rejected the claims that Plaintiffs were third party beneficiaries by noting that the pertinent contracts failed to evidence any stipulation *pour autrui*.

Another legacy suit, *Savoie v. Richard*, *excess* claims, for which they were awarded an additional $ 18 million by the jury and the trial court. The court explained that "[u]nder Act 312, landowners do not receive that portion of the remediation damages award needed to fund the statutorily mandated feasible plan; these funds must be deposited into the registry of the court."

VII. NEW MEXICO

*A. Judicial Developments*

In *T.H. McElvain* ***Oil*** *and Gas Ltd. Partnership v. Benson-Montin-Greer Drilling Corp., Inc.*,

The court inferred that Miller knew or should have known of Wilson's location because her residence appeared in the chain of title.   *T.H. McElvain*, title attorneys should review their state's title examination standards or form qualifications where quiet title judgments support the chain of title.

In *Amethyst Land Co. v. Terhune*,

In *First Baptist Church of Roswell v. Yates Petroleum Corp.*, the New Mexico Supreme Court reversed the court of appeals, which held in 2012

In *Anderson Living Trust v. WPX Energy Prod., LLC*,  *Elliot Industries LP v. BP America Prod. Co.* *Elliot Industries*, he believed the Supreme Court of New Mexico would imply the marketable condition rule as a matter of law in the future when it considered the issue ripe for review.

In *Abraham v. WPX Energy Prod., LLC*,

In an unpublished memorandum opinion and order issued on a motion to dismiss in *Harvey E. Yates Co. v. Cimarex Energy Co.*, *de novo* appeal, the Commission denied defendant's application, holding that drainage would be greater from the South Half (which had greater production potential than the North Half), violating the correlative rights of the South Half interest owners. Before the appeal was final, however, defendant drilled and began operations from the Penny Pincher No. 1. In the meantime, the Division entered orders approving compulsory pooling for the Penny Pincher No. 3 and the Penny Pincher No. 4 well, apparently with the participation of counsel for plaintiffs without objection.

First, Judge Herrera refused to dismiss the tort claims relating to the Penny Pincher No. 3 and the Penny Pincher No. 4 wells for lack of jurisdiction based on the exhaustion of remedies doctrine, holding that the doctrine does not apply to the tort claims because the Division and Commission lack jurisdiction to consider tort claims for damages, although she did hold that the doctrine applied to plaintiffs' claim for injunctive relief.

*B. Administrative Developments*

On April 14, 2014, the U.S. Fish and Wildlife Service (the FWS) issued a decision to list the candidate species Lesser Prairie-Chicken as a threatened species under the Endangered Species Act (the ESA).

VIII. NORTH DAKOTA

*A. Judicial Developments*

In *Reep v. State*,

N.D.C.C. § 47-16-39.1 authorizes cancellation of an ***oil*** and gas lease for failure to make timely payments of royalty when the equities support cancellation and imposes penalty interest in certain situations as well as prevailing party fees and costs. The statute contains a safe harbor provision that provides operators are not subject to lease cancellation or penalty interest if there is a legitimate dispute of title that would affect distribution of royalty payment. In *Tank v. Burlington Resources* ***Oil*** *and Gas Company, LP*, *i.e.*, creates a real risk that the royalty could be distributed to the wrong person(s); and (3) the dispute of ownership is 'existing,' *i.e.*, the dispute could not have been readily resolved and is expected to continue for some time into the future. The mere fact that an issue has been raised by a title attorney is not enough to invoke the safe harbor provision.

In *Capps v. Weflen*,

In *Peterson v. Jamanska ex rel. Clark*,

In *Golden Eye Resources, LLC v. Ganske*,

In *Tank v. Citation* ***Oil*** *& Gas Corp.*,

IX. OHIO

*A. Legislative Developments*

On May 15, 2014, the Ohio House of Representatives passed Substitute House Bill 375. This legislation proposed to levy a 2.5% severance tax on ***oil*** and natural gas production from horizontal wells to cover State regulatory efforts and idle and orphan well plugging. The Bill was supported by the ***oil*** and gas producers but died in the Ohio Senate. On November 19, 2014, the Ohio House of Representatives also passed Substitute House Bill 490 to address ***oil*** and gas regulatory updates in Ohio. This bill also died in the Ohio Senate.

*B. Judicial Developments*

In 2014, the most significant case impacting ***oil*** and gas operations in Ohio continues to be *State ex rel. Morrison v. Beck Energy Corp.*Ohio Revised Code § 1509.02 to regulate all aspects of ***oil*** and gas production operations in Ohio. The Court held that certain Munroe Falls' city ordinances, which required an operator to obtain from the city a drilling permit, certain zoning certificates, pay fees, and post a performance bond as a condition of drilling a well, were in direct conflict with R.C. § 1509.02, and were therefore preempted by state law. However, certain other ordinances pertaining to the care, supervision, and control of the city's rights-of-way were enforceable by the city, but could not be enforced in a way that discriminates against, unfairly impedes, or obstructs ***oil*** and gas activities and operations. The court had not yet issued a decision as of the time this paper was submitted for publication.

The court in *Hupp v. Beck Energy Corp.in the judgment of the lessee*," in the habendum clause, does not permit the lease to continue in perpetuity at the lessee's sole discretion. Rather, a good faith standard is imposed upon the lessee regarding the paying quantities requirement, with or without the phrase "in the judgment of the lessee." Accordingly, the lease would continue so long as there was an established ***oil*** or gas well that was actually producing or capable of producing in paying quantities.

The ***oil*** and gas lease in *Trico Land Co., LLC v. Kenoil Producing, LLC*,

In *Popa v. CNX Gas Co., LLC*,

The disputed clause stated that the lessor " . . . does hereby lease and let exclusively unto the Lessee, for the purpose of drilling, operating for, producing and removing ***oil*** and gas and all the constituents thereof . . . ." The court found that "the use of the term 'exclusively' is unrelated to the lessor's right to assign" and that it "lacks a specific reference to assignability." Ultimately, the court held that the granting clause language did not restrict assignments by the lessee.

Ohio appellate courts have also dealt with the extension and perpetuation of ***oil*** and gas leases. In *Eastham v. Chesapeake Appalachia, L.L.C.*,

In *Baile-Bairead, LLC v. Magnum Land Servs. LLC*,

In *Henry v. Chesapeake Appalachia, L.L.C.*,

In *Yoder v. Artex* ***Oil*** *Co.*,

During the last year, the Ohio Dormant Mineral Act ("DMA"), R.C. 5301.56, has received considerable attention from Ohio's appellate and federal courts. Several decisions found that the 1989 version of the DMA was self-executing, *see, e.g., Walker v. Shondrick-Nau*, *Swartz v. Householder*;  *see Eisenbarth v. Reusser*; *Eisenbarth* found that notwithstanding whether or not an ***oil*** and gas lease conveys the fee title to ***oil*** and gas, it nonetheless affects title by encumbering the ***oil*** and gas akin to a mortgage (which is specifically enumerated as a title transaction). Additionally, Ohio courts have addressed whether a severed mineral interest was the "subject of" a title transaction under certain circumstances. In *Dodd v. Croskey*,

Several of these issues are likely to be addressed in the near future by the Ohio Supreme Court. For example, not only is *Dodd* currently pending before the Court, but the U.S. District Court for the Southern District of Ohio in *Chesapeake v. Buell* *Dodd* and *Buell* but a decision has yet to be issued in either case.

*C. Administrative Developments*

Effective January 1, 2014, storage, treatment and recycling facilities were required to obtain a permit or order issued by ODNR, pursuant to rules adopted by ODNR, in order to operate. 2014 AP 958, by the FreshWater Accountability Project and Food and Water Watch on November 19, 2014.

ODNR also announced new permit conditions for drilling near faults or areas of past seismic activity. New permits issued by ODNR for horizontal drilling within 3 miles of a known fault or area of seismic activity greater than a 2.0 magnitude would require companies to install sensitive seismic monitors. If those monitors detect a seismic event in excess of 1.0 magnitude, activities would pause while the cause is investigated. If the investigation reveals a probable connection to the hydraulic fracturing process, all well completion operations will be suspended. ODNR is currently developing new criteria and permit conditions for new applications in light of this change in policy. The department will also review previously issued permits that have not been drilled.

Throughout the year, ODNR has also been developing a rules package pertaining to well pad construction for horizontal wells. The current version sets forth a comprehensive set of regulations for well pad construction that include, among other things, plans for sediment and erosion control, requirements for a geotechnical report describing the conditions, design considerations and construction requirements of the proposed well site, the submission of a storm water hydraulic report, and the certification of a professional engineer.

Lastly, ODNR, together with Ohio EPA and the Ohio Department of Health recently released a joint letter purporting to clarify jurisdictional issues and management practices for ***oil*** and gas wastes entitled, "Subject: Landfill acceptance and disposal of waste substances from horizontal wells -- update." The letter addresses the acceptance and disposal of waste substances from horizontal wells at Ohio landfills. It also discusses the regulation of drilling wastes in light of the amendments to Ohio law under House Bill 59 (effective June 30, 2013), and addresses issues on waste stabilization, how to determine whether drill cuttings are earthen material or solid waste, and the applicability of NORM and TENORM regulations to drilling-related wastes. The Ohio EPA expects to release a rule package for interested party comments in the near future.

X. OKLAHOMA

*A. Judicial Developments*

The case of *Cynostar Energy, Inc. v. Chesapeake Exploration L.L.C.*,

[A]ny acreage acquired within the AMI and outside the Drillsite Sections after the closing date will be offered to the other Parties and those Parties shall have the option to take their proportionate share of the interest based on the percentages in Article I by paying their proportionate share of actual acquisition costs within fifteen (15) days of receipt of offering.

Chesapeake acquired ***oil*** and gas leasehold acreage within the AMI and, pursuant to the above contractual commitment, offered the leasehold acreage to the other parties. The Cynostar plaintiffs elected to purchase their proportionate shares of the leasehold acreage. However, another party to the agreement elected to decline the opportunity. The Cynostar plaintiffs filed the present lawsuit seeking a judicial declaration that the AMI provision of the Exploration Agreement required Chesapeake to offer to the other parties the right to acquire a proportionate share of the acreage declined by the other party. In affirming the ruling of the district court in favor of Chesapeake, the court of appeals found that the exploration agreement was clear and unambiguous on the issue in dispute. It noted that the AMI provision was entirely silent on subject of the rights of the others if one or more of the parties to the exploration agreement declined the offer of an interest in newly-acquired acreage.

In *Gaskins v. Texon, LP*,

[N]othing in the language of § 570.10(A) creates or suggests a duty on a downstream purchaser or applies to downstream purchasers of ***oil*** and gas after it reaches the stream of interstate commerce. Moreover, there is nothing in that language requiring the imposition of an implied trust.

The case of *Kirk v. Devon Energy Prod. Co., L.P.*,

In *Coastal Strategies Income Fund-C v. Mewbourne* ***Oil*** *Co.*, *prima facie* presumption of delivery arises until overcome by contradictory evidence. The jury found in favor of Mewbourne. In affirming the trial court's judgment, the court of appeals noted that the question of which party (*i.e.*, the payor or payee) has the responsibility to make good on a stolen or intercepted check is not often discussed in Oklahoma case law, and that the parties' motions contained scant citation to applicable cases. The court found that none of the statutes asserted by Coastal on appeal applied to this situation and affirmed the ruling in favor of Mewbourne based on the mailbox rule.

*B. Administrative Developments*

Documents filed in the rulemakings referred to below can be viewed on the Oklahoma Corporation Commission's (Commission's) website at www.occeweb.com.

Amendments to Title 165, Chapter 10 of the Oklahoma Administrative Code (OAC), which comprises the Commission's ***Oil*** and Gas Conservation Rules, were addressed in Cause RM No. 201400002. Some of the more notable amendments, which became effective on September 12, 2014, are as follows: The Commission amended OAC 165:10-3-15 regarding the venting and flaring of gas from wells; OAC 165:10-3-17 to require API numbers on well signs; OAC 165:10-3-26 to reflect changes in references in the rule from wireline surveys to formation evaluation type well logs and to allow for submission of copies of logs by digital image or paper to the Commission, and OAC 165:10-3-28 regarding the drilling of wells in horizontal well units.

The Commission also amended OAC 165:10-5-5 to reorganize notice provisions for proposed noncommercial injection or disposal wells and commercial disposal wells, and to require mechanical integrity tests be performed on such wells within six months from the date of completion or conversion of the wells; OAC 165:10-5-6 to modify pressure test requirements for disposal wells permitted for injection at certain volumes or to require the installation of continuous pressure monitors on such wells; OAC 165:10-5-7 to require daily monitoring and recording of the volumes, casing tubing annulus pressure and the surface injection pressure for wells authorized to dispose into the Arbuckle formation and that operators of such wells maintain the required information for a minimum of three years, and OAC 165:10-7-33 is a new rule regarding truck wash pits.

Amendments to Title 165, Chapter 5 of the Oklahoma Administrative Code, which comprises the Commission's Rules of Practice, were addressed in Cause RM No. 201400001. Following is a brief summary of some of the more notable amendments which became effective on September 12, 2014: The Commission amended OAC 165:5-1-3 to modify the definition of Secretary; OAC 165:5-1-7 to modify language regarding emergency rulemakings, and to strike provisions regarding Petroleum Storage Tank Division (PSTD) rulemakings as such language unnecessarily repeats portions of 17 O.S. § 340; OAC 165:5-1-26 to change the means by which written acknowledgement of the receipt of pollution complaints is provided to relevant parties; OAC 165:5-3-1 to eliminate the fees for earthen or wash pit construction, enlargement or transfer applications, to provide for certification of documents by the Secretary, and to reflect the name change of the Oklahoma Office of State Finance to the Oklahoma Office of Management and Enterprise Services, and OAC 165:5-3-2 to change PSTD copying, certification, postage and search fees so that such fees are consistent with the fees charged by other Divisions appearing in OAC 165:5-3-1.

The Commission also amended OAC 165:5-3-21 regarding definitions pertaining to public utility assessment fees; OAC 165:5-3-22 concerning public utility assessment fee allocation; OAC 165:5-3-25 to change the date by which affected public utilities are to submit a report to the Public Utility Division (PUD) Director and the information required to be submitted in the report; OAC 165:5-7-6 concerning drilling and spacing unit establishment or modification; OAC 165:5-7-27 to reorganize notice provisions for proposed noncommercial injection or disposal wells and commercial disposal wells, and OAC 165:5-7-34 to correct a reference to the rule regarding exemption of an operator from responsibility for closure of a noncommercial pit and transfer to the surface owner responsibility for maintenance and closure of the pit.

In addition, the Commission amended OAC 165:5-11-1 regarding discovery in proceedings on the PUD docket; OAC 165:5-13-3 concerning order of proof during hearings; OAC 165:5-13-5 to provide that oral exceptions regarding motions and emergency matters shall be set for hearing before the Commission *en banc* unless referred to an ***Oil*** and Gas Appellate Referee or an Administrative Law Judge regarding matters involving issues addressed in Chapters 10, 15, 16, 20, 25, 26, 27, 28, 29, 30, and/or 32; and Appendix D regarding notice of application for waiver of pit closure is revoked and a new Appendix D proposed to correct grammatical errors.

XI. PENNSYLVANIA

*A. Legislative Developments*

On October 22, 2014, Governor Corbett signed House Bill 402, also known as the Recording of Surrender Documents from ***Oil*** and Natural Gas Lease Act. The Act allows a lessor to compel a lessee or its assignee to file surrender documents upon the expiration, termination, or cancelation of a lease. The lessee must dispute the expiration of the lease in writing within 30 days of receiving notice of termination, cancelation, or expiration from the lessor. If the lessee does not provide surrender paperwork or dispute the expiration, the lessor may record an affidavit of termination with the recorder of deeds.

Governor Corbett also signed House Bill 2278, The Unconventional Well Report Act, into law on October 22, 2014. The Act requires operators of unconventional wells to submit monthly reports to the Department of Environmental Protection specifying the amount of production on the most well-specific basis available. An unconventional well is defined as "a bore hole drilled or being drilled for the purpose of or to be used for the production of natural gas from an unconventional formation." Initial reports under this Act must be filed by March 31, 2015, and each subsequent monthly report is due 45 days after the close of the reporting period.

*Pending Legislation to Watch*: Pennsylvania governor-elect Tom Wolf strongly advocated for a severance tax on natural gas extraction during his 2014 campaign. While it is unclear whether he will be successful in passing the tax when he takes office in 2015, severance tax bills have already been introduced in the Pennsylvania legislature. House Bill 1947 would provide for a 5% tax on the gross value of units

House Bill 1684, which is aimed at ensuring that landowners receive fixed minimum royalties from unconventional gas leases, cleared the House Environment Resources and Energy Committee in March 2014. The bill would amend the ***Oil*** and Gas Lease Act of 1979, and prevent operators from deducting postproduction costs from lessor's 1/8th share of the royalties. The bill was removed from the table for 2014 in October. A trio of bills, SB 1236, SB 1238, and SB 1237 passed senate approval in April 2014. The bills would require ***oil*** and gas exploration companies to provide an itemized list of deductions taken out of royalty checks cut for landowners, more thorough record-keeping with county governments, and provide protection for landowners who question the accuracy of payments. The bills were referred to the House Environmental Resources and Energy Committee in May 2014.

House Bill 2350 and companion Senate Bill 1378 require the State's Environmental Quality Board to differentiate conventional ***oil*** and gas wells from unconventional wells when promulgating regulations. HB 2350 cleared the House Environmental Resources and Energy Committee in June. House Bill 2318 was introduced in June, and if passed, would require the Pennsylvania Department of Conservation and Natural Resources to provide notice and receive public input before leasing state forest lands for unconventional gas development. Senate Bill 411, which is currently on the Senate table, would amend Pennsylvania's Environmental Good Samaritan Act to enable energy companies to use mine drainage rather than fresh water without fear of the liability associated with cleaning up the mine drainage. Senate Bill 1359 would overhaul key requirements of Act 13, including amendments that would provide more stringent environmental and public health protections, and protect the restoration of local zoning powers. The bill would also repeal statewide zoning provisions imposed by Act 13. The bill was referred to the Environmental Resources and Energy Committee.

*B. Judicial Developments*

In *Shedden v. Anadarko E & P Co., L.P.*,

In *Pennsylvania Game Commission v. Seneca Resources Corp.*,

In *Pennsylvania Services Corp. v. Texas Eastern Transmission, LP*,

In March 2014, in *Allegheny Enterprises Inc. v. J-W Operating Co.*,

In *Neuhard v. Range Resources-Appalachia LLC*,

In *Danko Holdings, L.P. v EXCO Resources (PA), LLC*,

The court in *Warren v. Equitable Gas Company, LLCPenneco Pipeline v. Dominion Transmission*,

In *Smith v. Steckman Ridge, LP*, *Hite v. Falcon Partners*

In July of 2014 an *en banc* panel of the Commonwealth Court decided several issues remaining after the Pennsylvania Supreme Court's landmark decision in December of 2013, striking down parts of Act 13.

In *Herder Spring Hunting Club v. Keller*,

A Lycoming County judge authorized a natural gas public utility to use its eminent domain power in condemning easements for the construction and maintenance of a pipeline to supply gas to a private power plant.

In *Sabella v. Appalachian Development Corp.*,

XII. SOUTH DAKOTA

In *Holsti v. Kimber*,

Over forty years later, in 2012, believing that Kvalheim's reserved mineral interest had lapsed and was abandoned because of non-use, the surface owner completed the notice of lapse procedure under South Dakota's abandoned mineral interest law. After completing the notice of lapse procedure, the surface owner commenced a quiet title action in May 2012.

South Dakota's abandoned mineral interest law states that a severed mineral interest will be deemed abandoned if it is unused for twenty-three years.

A mineral interest is deemed to be used if:

. . . .

(4) Any conveyance, valid lease, . . . or decree that makes specific reference to the mineral interest is recorded in the office of the register of deeds for the county in which the mineral interest is located;

. . . .

(7) A statement of claim is recorded in compliance with § 43-30A-4;

. . . .

No statement of claim was recorded when the surface owner conducted the notice of lapse procedure in 2012.

While the Kvalheim mineral interest was never distributed or conveyed to any of the eight heirs, two of them recorded documents relating to the mineral interest in the twenty-three years preceding the commencement of the quiet title action. In 2011, one of the heirs conveyed his interest to his spouse, and she then conveyed to her children. Another heir recorded a statement of claim in 1994 relating to the mineral interest.

The Circuit Court ruled that the documents recorded by the heirs did not constitute use, because the Kvalheim mineral interest was never conveyed to any of the heirs "by a written, recorded document."

The South Dakota Supreme Court reversed and remanded the case for further proceedings. It ruled that the heirs became owners of Kvalheim's mineral interest upon his death, even though the mineral interest was never probated in South Dakota. The recordings of documents by the two heirs in 2011 and 1994 therefore constituted use of the mineral interest.

The case was remanded to the Circuit Court to determine whether the use of the mineral interest by two of the eight heirs constituted use of the mineral interest by all of the heirs. On remand, the Circuit Court granted judgment in favor of the surface owner, ruling that use of the mineral interest by two of the heirs did not constitute use of the mineral interest by all of the heirs.

In response to a petition by Luff Exploration, the Secretary of the South Dakota Department of Environment and Natural Resources ("SD DENR") issued an uncontested ***Oil*** & Gas Order (***Oil*** & Gas Case No. 16-2013) on July 1, 2013, establishing a 960-acre spacing unit.

Golden was an unleased mineral owner in the spacing unit. When Luff contacted Golden in June 2013 about leasing her mineral interest, she did not respond. Luff contacted Golden again, and advised her that if she did not lease her mineral interest and did not elect to participate in the drilling of the well, Luff intended to petition the SD DENR Board of Minerals and Environment for a compulsory pooling order. Golden responded to Luff that she wanted to continue her status as an unleased mineral interest owner.

Luff petitioned the Board on July 23, 2013 for a compulsory pooling order for the spacing unit. Copies of the petition and notice of hearing were mailed to Golden. On July 28, 2013, the drilling of the well on the spacing unit commenced. Golden petitioned to intervene in the hearing on the petition for compulsory pooling order.

The Board found that Luff had made an unsuccessful, good faith attempt to have Golden execute a lease or participate in the risk and cost of drilling the well, as required by Administrative Rule of South Dakota 74:12:10:01.

XIII. TEXAS

*A. Judicial Developments*

Texas courts spent a great deal of time this year resolving disputes related to the interpretation of ***oil*** and gas lease terms. A number of cases focused on the role of continuous drilling provisions in leases and whether certain operations perpetuated the leases beyond their primary terms. For example, in *W.H. Sutton v. SM Energy Co.*,

In *Community Bank of Raymore v. Chesapeake Exploration, L.L.C.*,

In *EnerQuest* ***Oil*** *& Gas, LLC v. Plains Exploration & Production Co.*,

In *PNP Petroleum I, LP v. Taylor*,

*Unit Petroleum Co. v. David Pond Well Service, Inc.*

In 2014, at least four significant cases addressed the distribution of royalty proceeds and the deduction of post-production costs in the calculation of royalties. *Chesapeake Exploration, L.L.C. v. Hyder*

In *Warren v. Chesapeake Exploration, L.L.C.*,

The court issued a similar decision in *Potts v. Chesapeake Exploration, L.L.C*. *Potts*, the royalty clause in the lease provided that (i) royalties would be calculated based on the market value at the point of sale, (ii) royalties would be based on sales of leased substances to unrelated third parties arrived at through arms-length negotiations, and (iii) royalties on leased substances not sold in an arms-length transaction shall be determined based on prevailing values at the time in the area. Chesapeake sold the gas produced from the lease to an affiliate at the wellhead. The court held that Chesapeake could arrive at the market value at the wellhead by deducting post-production costs incurred between the wellhead and downstream points at which the gas was sold to unaffiliated purchasers. Further, the court held that the lease did not prevent the point of sale from being at the wellhead if the lessee sold the gas to an affiliated entity.

Finally, the Texas Supreme Court decided whether carbon dioxide (CO2) removal qualifies as a post-production expense. In *French v. Occidental Permian Ltd.*,

Interpreting language from a 1953 assignment, the court held in *McDaniel Partners, Ltd. v. Apache Deepwater, LLC*

In *Tipton v. Brock*,

Several cases this year analyzed industry agreements. *ZK Drilling Co., LLC v. Lavaca River Operating Co., LLC*,

In *XH, LLC v. Cabot* ***Oil*** *& Gas Corp.*,

The court considered whether the accommodation doctrine applies to groundwater in *City of Lubbock v. Coyote Lake Ranch, LLC*.

In *Key Operating & Equipment, Inc. v. Hegar*,

In *Contango Operators, Inc. v. United States*,

The Fifth Circuit Court of Appeals addressed attachment of mineral liens in the bankruptcy context in *In re T.S.C. Seiber Services, L.C*.

The Fifth Circuit Court of Appeals recently addressed whether subsequent contracting by a mineral interest owner and a well operator could preclude a subcontractors' mineral lien, and the case has a good discussion of how a working interest owner can be both an owner and a contractor, and how a service company can perfect both a subcontractor's lien and a contractor's lien. In *In re Heritage Consol., L.L.C.*,

*Newco Energy v. Energytec, Inc.*

XIV. WEST VIRGINIA

*A. Legislative Developments*

The Aboveground Storage Tank Act, W. Va. Code § 22-30-1, *et seq.* and the Public Water Supply Protection Act, W. Va. Code § 22-31-1, *et seq.*, were signed into law on April 1, 2014 and became effective June 6, 2014. These statutes establish new regulations related to aboveground storage tanks (AST), or any device made to contain an accumulation of more than 1,320 gallons of fluids that are liquids at standard temperature and pressure that has more than 90% of its capacity aboveground. An AST includes all ancillary aboveground pipes and dispensing systems up to the first point of isolation and all ancillary underground pipes and dispensing systems connected to the aboveground containers to the first point of isolation. All mobile devices that remain in one location continuously for 60 or more days, and which otherwise meet the definition criteria, are also AST.

Under § 22-30-25, certain aboveground storage tanks used in the ***oil*** and gas industry are exempt from the permitting process, but are still required to participate in the inventory and registration process. Additionally, every owner or operator of an AST must have an annual inspection performed by a qualified, registered professional engineer or someone working under supervision of one; by an individual certified by the American Petroleum Institute to perform inspections; or by an individual certified under another program approved by the secretary. The inspection form shall certify that each AST, associated equipment, leak detection system, and secondary containment system meets the minimum standards established in the law or by the WVDEP in legislative rule.

The West Virginia legislature passed H.B. 107 on March 14, 2014, amending W. Va. Code §§ 22-15-8 and 11, creating requirements for legal disposal of drill cuttings and associated drilling waste from well sites. The new legislation requires that drill cuttings be stored in a separate cell in a landfill dedicated to such waste, and imposes monitoring requirements and additional fees for disposal sites. This waste disposal is regulated by the WVDEP. The legislation imposes an additional solid waste assessment fee on drill cuttings and waste of $ 1 per ton, in addition to all other fees and taxes levied against the waste.

*B. Judicial Developments*

*Trans Energy, Inc. v. EQT Production Co.gas rights* were never transferred to Trans Energy's predecessors because of a notation in an exhibit to a 1966 memorandum that denoted "***oil***" in reference to the Blackshere wells being conveyed in the transaction. EQT's other primary contention was that Trans Energy's predecessor was not a bona fide purchaser for value.

The appellate court adopted the district court's findings and held that the memorandum's granting language plainly stated that the leases being transferred were ***oil*** and gas leases. The court also noted that EQT's argument required the ***oil*** well exhibit to be read in isolation of the memorandum's other exhibit, which clearly included the unsevered 1892 Blackshere Lease. The court also disposed of EQT's bona fide purchaser argument finding: (1) no language in the conveyances to Trans Energy's predecessors would have required additional title searching; (2) that all reasonable inquiries in due diligence would nevertheless have failed to uncover a competing claim; (3) that legend and lore regarding the severance of the gas rights in the early 1900s had no legal significance; (4) that two wells on the 3,800-acre, heavily forested tract did not constitute constructive notice; and (5) the unique circumstances in the price and the unknown potential of natural gas development in that area at the time of the purchase accounted for the difference in purchase price and value at the time of the litigation.

In *Braden v. Chesapeake Appalachia, Inc.*,

Plaintiff argued that the pooling was "pretextual" and that the lease was "artificially" extended through "backhanded" tactics. The court disagreed. After finding that the habendum clause and the pooling provision in the lease were unambiguous, the court rejected the implication that the pooling clause should be interpreted against the lessee because it was allegedly "one-sided." The court found the plain meaning of the pooling provision allowed the lessee to pool the lease and that operations anywhere in the unit were deemed to be operations on plaintiff's property. The court's holding reaffirmed the *FlemingHenry*

*Barber v. Magnum Land Services, LLC*,

The court granted defendants summary judgment as to the fraudulent inducement claim, finding:

none of the plaintiffs was justified in relying on such a blatant misrepresentation of the law of trespass and conversion. It is unreasonable to believe that the law would permit gas companies to drill into anyone's land and take that person's gas without his or her permission. Even if one did believe that the law permits such conduct, it is even more unreasonable to believe that gas companies would spend money on leases unnecessarily. Finally, no reasonable person would accept such a representation as true and sign the lease without first looking into the validity of the statement or consulting someone knowledgeable in the ***oil*** and gas field.

The court also found plaintiffs failed to establish any concerted action by the two defendants to advise landowners that deviated wells were lawful in support of their civil conspiracy claim. Finally, the court granted defendants summary judgment as to the declaratory rescission claim finding: (1) plaintiffs failed to return or offer to return their bonus money in accordance with the restoration rule; (2) that there was no substantial procedural or substantive unconscionability relating to the negotiations or the leases themselves; and (3) that plaintiffs' claims were time-barred by the equitable doctrine of laches.

In *W. W. McDonald Land Co. v. EQT Production Company*, *e.g.*, the first place downstream of well where gas can be sold and title passed.

As to whether the lessees had to pay royalties based upon volumes at the wellhead, the court held that requiring lessees to pay royalties on unsold gas was illogical and inequitable. It held volume losses were not "deductions" of costs in the same sense as marketing or transportation costs; thus, the defendant-lessees had no obligation to pay royalties on the volume at the wellhead.

*C. Administrative Developments*

Permit Number GP-WV-1-88, a General Water Pollution Control Permit authorizing the disposal of drilling wastes by land application, was scheduled to expire on July 31, 2014. Pursuant to its authority under W. Va. Code § 22-6-2(c), the West Virginia Department of Environmental Protection's (WVDEP) Office of ***Oil*** and Gas extended the expiration date for GP-WV-1-88 to July 31, 2015, or until the issuance of the new general permit, whichever occurs first.

On June 30, 2014, the WVDEP filed emergency rules relating to the disposal of drill cuttings and related waste. W. Va. Code R. § 33-1-1, *et seq.* The rules modify the definition of drill cuttings by narrowing it to "the broken bits of solid material and drilling mud removed from a borehole drilled by rotary, percussion or auger methods."    *all* wastes generated in the exploration, production and development of ***oil*** and natural gas and associated activities must be evaluated by this equipment.

On October 21, 2014, WVDEP filed with the Secretary of State an Interpretive Rule providing guidance and clarification for complying with the initial inspection and certification requirements of the Aboveground Storage Tank Act (W. Va. Code §§ 22-30-1, *et seq.*). The Interpretive Rule became effective on November 20, 2014, and is codified in Title 47, Series 62 of the West Virginia Code of State Rules.

XV. WYOMING

*A. Legislative Developments*

In 2005, the Wyoming Legislature enacted statutes regulating the authority of ***oil*** and gas operators to enter lands to conduct operations.

Effective January 1, 2015, the Wyoming Legislature lowered the interest rate on delinquent *ad valorem*/gross products taxes on mineral production from 18% per annum to the average prime interest rate, as determined by the State Treasurer, plus 4%. The Legislature set a floor and cap for the new interest rate; the rate shall not be less than 12% or exceed 18% on any mineral produced on or after January 1, 2015. This interest rate reduction is applicable to ***oil*** and gas, as well as all other severed minerals.

The Legislature also instituted a new fuel tax on liquefied and non-liquefied natural gas, at a tax rate equivalent to the existing gasoline and diesel fuel tax.

*B. Judicial Developments*

In *Powder River Basin Resource Council v.* ***Oil*** *& Gas Conserv. Comm'n*,

The environmental groups then appealed the district court's decision to the Wyoming Supreme Court. On March 12, 2014, the Supreme Court analyzed the protection of trade secrets under the Wyoming Public Records Act (WPRA) and overturned the district court's order. The Supreme Court concluded it was "unable to determine whether the identity of individual chemicals may be trade secrets in the context of hydraulic fracturing operations based upon the information in the record," and therefore remanded the case to the district court for further examination. The Supreme Court did not reach the question of whether the chemical information qualified as trade secrets, but instead required the district court to review the information on a case-by-case, record-by-record, or operator-by-operator basis applying the Supreme Court's description of the WPRA trade secret exemption from public disclosure.

In *Black Diamond Energy, Inc. v. Encana* ***Oil*** *& Gas (USA) Inc.*,

Following trial in the *Black Diamond* case, a jury determined the operator had breached the farmout agreement, but awarded the lessee no damages on its counterclaim.

In *Merit Energy Co. v. Department of Revenue*,

The operator in *Merit* appealed the SBOE's dismissal order to the Wyoming Supreme Court. The Supreme Court affirmed the dismissal, concluding the original take-in-kind discrepancy letters were final appealable administrative decisions and the operator's failure to appeal those letters prevented an appeal of the NOVC.

*C. Administrative Developments*

The WOGCC promulgated new rules, effective March 1, 2014, requiring groundwater sampling around ***oil*** and gas wells. Under the rules, operators must sample, analyze and monitor groundwater following detailed Sampling and Analysis Procedures as part of the ***oil*** and gas well permitting process.

The WOGCC also revised its well location rules, effective July 24, 2014. For horizontal wells, the revised rules created permanent -- as opposed to temporary -- six hundred forty (640) acre spacing units, which may be enlarged or contracted by application.

In May 2013 and again in October 2014, a group of Wyoming citizens petitioned the WOGCC to change its rules to require a setback of at least 1,320 feet from any occupied structure. At its November 18, 2014 hearing, the WOGCC reviewed the proposed rule change and denied the application. However, the Commissioners decided to open a rule-making case and propose revisions to its setback rules. The WOGCC announced the new rules would require a 500-foot setback from any occupied structure and increased notice requirements.

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1. 1The lead editor for this report is Mark D. Christiansen of McAfee & Taft, Oklahoma City, OK. The contributors of the state reports are: George R. Lyle and Nicholas Ostrovsky of Guess & Rudd P.C., Anchorage & Fairbanks, AK; Thomas A. Daily of Daily & Woods, P.L.L.C., Fort Smith, AR; John J. Harris of Locke Lord LLP, Los Angeles, CA; Jean Feriancek and Barry C. Bartel of Holland & Hart LLP, Denver, CO; David E. Pierce, Professor, Washburn Univ. School of Law, Topeka, KS; April L. Rolen-Ogden of Liskow & Lewis, Lafayette, LA; Alex Ritchie, Professor, Univ. of New Mexico School of Law, Albuquerque, NM; North Dakota report by Adam Olschlager of Crowley Fleck PLLP, Billings, MT; W. Jonathan Airey, Gregory D. Russell, and Timothy J. Cole of Vorys, Sater, Seymour and Pease LLP, Columbus, OH; Mark D. Christiansen of McAfee & Taft, Oklahoma City, OK (Part A) and Susan Dennehy Conrad of the Oklahoma Corporation Commission, Oklahoma City, OK (Part B); Kevin C. Abbott, Nicolle R. Snyder Bagnell and Thomas J. Galligan of Reed Smith LLP, Pittsburgh, PA; Max Main of Bennett, Main & Gubbrud, P.C., Belle Fourche, SD; Jolisa Dobbs, Gaye White and Arthur Wright of Thompson & Knight LLP, Dallas and Austin, TX; Rodney W. Stieger, Kelley Goes and J. Matthew Davis of Jackson Kelly PLLC, Charleston, WV; and Walter F. Eggers, III and Sami Falzone of Holland & Hart LLP, Cheyenne, WY. [↑](#footnote-ref-2)