

MULTI-STATE ROUNDUP ON  
OIL AND GAS LAND AND LEASE ISSUES

Oil, Gas and Mineral Law Section  
Houston Bar Association

The Houston Club, Texas Room (10<sup>th</sup> Floor)  
February 22, 2011

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Member of the National Association of Division Order Analysts (NADOA), the Oklahoma City Chapter (CAPDOA) and the Tulsa Chapter (SADOA)  
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#### LAW RELATED PUBLICATIONS:

Significant Differences in Oil and Gas Principles between Producing States: From the Landman's Perspective - Texas and Oklahoma - Co-author - published in The Landman, 11-12/89 and 1-2/90 issues;  
Title Examination Refresher - Author/Speaker - Review of Oil and Gas Law V (1990)- Oil, Gas and Mineral Section of the Dallas Bar Association;  
Title Examination of Fee Lands (Constructive Notice Revisited) Author/speaker - Mineral Title Examination III (1992) Rocky Mountain Mineral Law Foundation, Denver, Colorado;  
Probate Estates in Texas, Oklahoma and Louisiana Author/Speaker - 19th Annual NADOA Institute (1992), Dallas, Texas;  
A Comparative Review of Oil & Gas Law: Texas-Oklahoma-Arkansas -Co-Author/Co-Speaker - Natural Resources Law Institute (1993), Hot Springs, Arkansas;  
Revenge Against the Title Nerds! (How Texas' proposed title standards can help you avoid technical title objections) -Author/Speaker - Review of Oil and Gas Law VIII(1993)- Energy Law Section of the Dallas Bar Association;  
Due Diligence Title Review: The Problem Areas, Where to Look and How to Solve. -Author/Speaker - Sixth Annual Dallas Energy Symposium (1994), Dallas, Texas;  
Suspense Issues that Affect the Division Order Analyst. - Author/Speaker - 21st Annual NADOA Institute (1994), San Antonio, Texas;  
Non-Consenting Mineral Owners. -Author/Speaker - 24th Annual NADOA Institute (1997), New Orleans, Louisiana;  
Drafting Tips For Oil & Gas Leases and Conveyance - Author/Speaker - University of Texas 24<sup>th</sup> Annual Oil, Gas and Mineral Law Institute (1998), Houston, Texas;  
State Royalty Payment Statute - State Check Stub Requirement Statutes - Author/Speaker - 2<sup>nd</sup> Annual National Oil & Gas Royalty Conference (1998), Houston, Texas;  
A Model Form Title Opinion Format - Is it Possible? Is it Practical? - Author -Vol. 25, No. 2 - Oil, Gas and Mineral Law Section Report (December, 2000) - State Bar of Texas;  
Basic Conveying Rules for Mineral Deeds and Assignments of Oil and Gas Leases - Co-Author/Speaker - 19<sup>th</sup> Annual Advanced Oil, Gas & Energy Resources Law Institute (2001), San Antonio, Texas;  
Shut-In Gas Royalty - How to Avoid a Train Wreck - Author/Speaker - St. Mary's University School of Law Mineral/Royalty Owners & Producers Institute (2002), Midland, Texas;  
Constructive Notice ( A Multi-state perspective) - Author/Speaker - 20<sup>th</sup> Annual Advanced Oil, Gas & Energy Resources Law Institute (2002), Dallas, Texas;  
Pooling - From A to Horizontal - Author/Speaker - St. Mary's University School of Law, Mine Fields & Minerals Institute (2003), Midland, Texas;  
Accessing Local Records - Preparing the Chain of Title - Author/Speaker - Mineral Title Examination IV (2007) Rocky Mountain Mineral Law Foundation, Denver, Colorado;  
Legal Descriptions and Wellbore Assignments - Co-Author/Speaker - 25<sup>th</sup> Annual Advanced Oil, Gas & Energy Resources Law Institute (2007), Houston, Texas.

.ARTICLES/SNELLBIOSKETCH.

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## George Snell

**From:**  
**Sent:**  
**To:**

Subject:

George, you are without mercy. All right, here is something you may say about Arkansas.

**--FLASH--**

### **ARKANSAS REGULATORY INNOVATION SOLVES THE "HORIZONTAL-WELL-IN-THE-LITTLE-BOX" DILEMA**

The development of unconventional oil and gas sources almost always involves the use of closely-spaced horizontal production wells, with multistage completed laterals extending far (well beyond a mile, in many cases) from surface locations. This technological advance, touted as a significant step toward weaning this country's foreign oil addiction, may, nevertheless, be retarded, in many jurisdictions, by legal issues surrounding the property rights of affected mineral owners. Often, in these horizontal well plays, neither the Common Law Rule of Capture (and of trespass liability for those who exceed their capturing license,) nor the system of square or rectangular units adopted by state regulatory agencies, adequately accomplishes the regulatory mantra: WE MUST SIMULTANEOUSLY PREVENT WASTE AND PROTECT THE CORRELATIVE RIGHTS OF ALL INTERESTED PARTIES. That is potentially tragic, because it suggests that our own precious state laws, as much as unfavorable commodity prices and the bungling EPA, threaten our objective of maximizing these resource plays.

BUT WAIT!!! (in the immortal words of pitchman, Billy Mays, Jr.), look what they are doing in Arkansas. In a two-step process, Arkansas has stumbled upon a solution.

Arkansas has always been a regulatory rectangles-and-squares state, though its 1939 enabling act (modeled upon the Interstate Oil and Gas Compact Model act of that vintage) suggests that the unit must have something to do with the area effectively drained by a single well. Arkansas also has long-employed force-pooling of non-consenting owners, in a process it calls "integration."

Step one of the process was a revision of the regulatory enabling statute. The revised statute provides a presumption that a unit is a 640 acre square, but gives license to the state's Oil and Gas Commission to form a larger or smaller unit, after notice and hearing. Geological and engineering concepts, like "Drainage," are no longer part of the process, unless, of course, the Commission finds them important, case-by-case. The same statute authorizes the Commission to determine, on a continuing basis, the number of wells per unit, and their placement. It also provides the Commission with the authority to provide remedies for the correlative right violations which might otherwise occur from the placement of a well close to (or, God forbid) across a unit line.

Step two was the invention of the cross-unit well. Led by Southwestern Energy Company, the first and largest developer of Arkansas' Fayetteville Shale Play, and motivated by its own need to regulate that play efficiently, the Arkansas Commission promulgated its General Rule B-43. Rule B-43 contains unitization and spacing provisions for the several counties covered by the play. Rule B-43 (o), provides the authority for the cross-unit well. Here is how it works:

When a cross-unit well is permitted, its tentative sharing area is defined as the area having a radius of 560 feet from the entire completed interval of the proposed well (the well's "band-aid.") That area is overlain upon the unit(s) plat, enabling a calculation of the band-aid's acreage within each affected unit. Each unit's share of the cross-unit well is its acreage contained within the band-aid, divided by the band-aid's total acreage. After the well is completed, the band-

aid is redrawn and interests are adjusted to reflect the well's actual, as-drilled, location. If you found that a little confusing, refer to Figure 1 below.

Applications for cross-unit wells may be approved administratively if they are supported by persons having at least 50% of the right to drill in each of the sharing units, subject to one other important requirement. The rule requires that each such unit ultimately have either an entirely in-unit well, at a non-exceptional location or, alternatively, 4,160 feet of completed lateral within the unit, in order to produce a cross-unit well affecting the unit. Applicants are given one year following the spud date of the cross-unit to comply with that requirement.

Cross-unit wells enable completion of every inch of each of multiple wells from common surface locations, and increasingly longer productive laterals (thus preventing economic waste), as well as simply preventing the waste of hydrocarbons, stranded near unit boundaries. The sharing formula then protects all owners' correlative rights. Indeed, **in 2010, less than six years after the first horizontal Fayetteville Shale well was drilled, over 50% of all Arkansas horizontal well permits issued were for cross-unit wells.** (The exact numbers are 927 horizontal well permits, 524 of which were for cross-unit wells.) Figure 2, below, is a copy of an exhibit which was presented to the Arkansas Commission, showing a hypothetical totally developed nine-section area, primarily utilizing cross-unit wells.

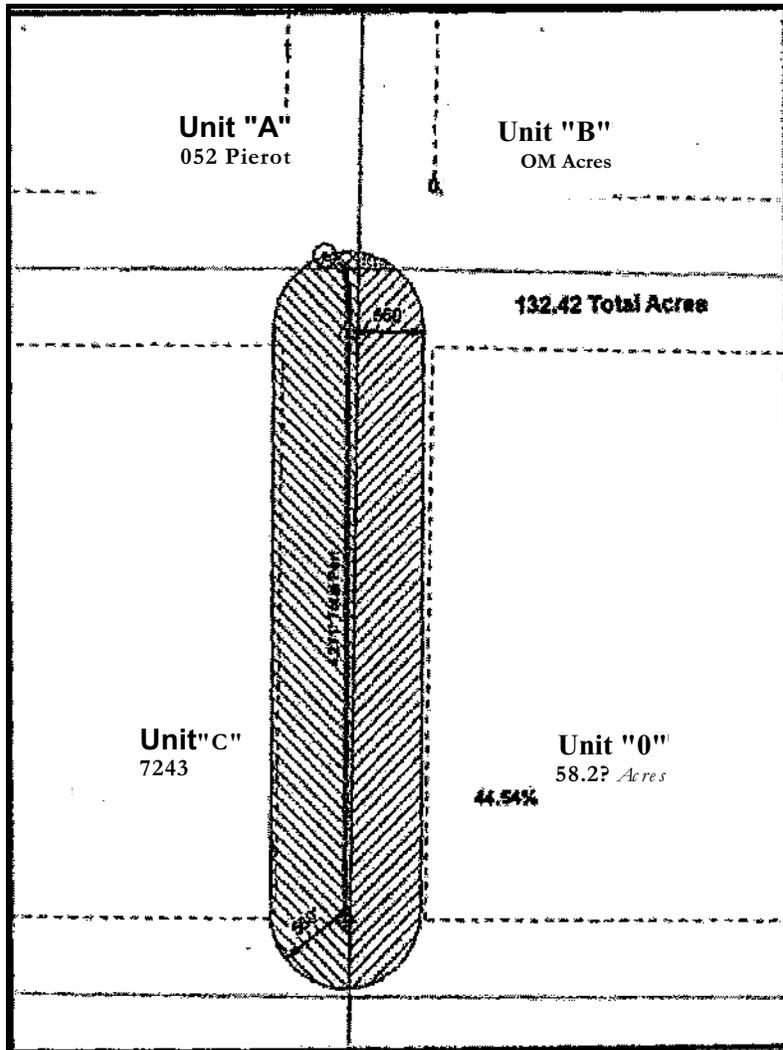
Other oil and gas producing states (Oklahoma and Louisiana, to name two) have taken notice and are actively considering their own variants of cross-unit well development. We should watch this particular wave with great interest.

Thomas A. Daily

### **Figure 1:**

# Hypothetical Band-aide Map with Four Affected Units

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Figure 2: Nine Section Drill-Out Plan, Using Cross-Unit

Wells



DAY · CARTER · MURPHY LLP

Joshua L. Baker  
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February 4, 2011

VIA ELECTRONIC MAIL'

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Re: Multi-State Luncheon, Oil and Gas Section – CALIFORNIA UPDATES

Dear George;

As you have requested, **below** is an overview of various issues currently affecting the oil and gas industry here in California.

Title Issues

While certainly not unique to California, one particular issue we are seeing with increasing frequency involves surface access disputes in severed estate situations. California is perhaps the only oil and gas producing state that has not adopted the accommodation doctrine and which does not have any surface-damage laws on the books. With more and more surface access issues arising, however, the courts and/or Legislature may be taking a new look at this issue soon.

A different but related issue we have also seen on several different occasions includes disputes between severed mineral owners/lessees and "surface only" energy operations, such as solar and wind developers. As with the rest of the country, we anticipate this to be an issue that will likely become more common with increased demand for alternative energy development.

Operational Issues

Over the past few years there has been an increase in interest, in heavy crude, which is fairly prevalent in quite a few areas throughout California. Interest was at a high a few years ago when the price of oil was breaking records, but we have seen interest pick up again recently as the price of oil has remained relatively high and steady..

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With regard to specific plays, perhaps the biggest draw right now is the Monterey-Shale. This emerging shale play, which consists of both oil and gas (but primarily oil), extends from parts of Northern California (Monterey County), through Central California (Kern, Santa Barbara and Ventura Counties) *and* down to Southern California (Orange County). Milling techniques common to shale-plays are being employed, including horizontal drilling. Reports indicate that this may be the largest oil-shale play in the United States with 300 million barrels of oil in place.

Political Issues

As many know, California *is* a hotbed for political issues. The one political issue that continues to affect the state oil and gas industry: is the on-going proposal for imposing a severance tax on oil production. Despite California being the third largest oil producer in the country, it is the only producing state— major or minor that does not, have a severance tax applicable to oil and/or natural gas. (Of course, California producers pay ether fees and taxes not applicable to companies in other states.) In 2006, the voters were asked to accept or reject a 6% severance tax on oil production by way of Proposition 87; the voters rejected it by a substantial margin. Nevertheless, a severance tax has been proposed several times since by various legislators, the most recent by way of Assembly Bill 656 in early 2010 (which appears to be sitting idle and not likely to go anywhere at this point).

Various rationales have been proposed for a severance tax since its re-introduction into California politics in 2006, ranging from the need to fund alternative energy development to helping to close California's growing budget deficit. So far, the various measures to implement such a severance tax have ultimately gone nowhere, but it still remains a viable threat to the industry in California. Interestingly, the last time an oil severance tax was such a big issue was when Jeny Brown was governor of California in 1981. He couldn't make it happen then, and the industry is likely hoping he can't, make it happen now that he is our governor again.

\*\*\*

Good luck with your luncheon, George. If there is an nig elSe we can do to assist you from a California perspective, please do not hesitate to contactus,

● Sincerely yours,

DAY CARTER & MURPHY LLP



Joshua L. Baker  
Sean B. Murphy  
James M. Day, Jr.



Davis Graham & Stubbs LLP

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MEMORANDUM

TO: George A. Snell, III

FROM: Davis Graham & Stubbs LLP  
Greg Danielson

Lara Griffith  
February 4, 2011

DATE:

SUBJECT: Houston Bar – Oil and Gas Section: Colorado Update

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This memorandum will report on current oil and gas issues in the state of Colorado.

Drill in& Updates

In 2010, Colorado proved to be the regional leader and among the national leaders with respect to drilling permits. Colorado issued 5,996 drilling permits during 2010, with Weld County leading the pack with 2,152 permits. The number of permits increased by 15% from 2009.<sup>1</sup> The Colorado Oil and Gas Conservation Commission's records indicate that 2,311 wells were started during 2010, and that well starts during the last six months of the year were up 54% from 2009.<sup>2</sup>

Beginning in 2009, drilling permits in Colorado are valid for two years, while previously they had been valid for one year only. The change to a two-year drilling permit provides consistency between federal and state permitting periods.

Niobrara

In the Colorado Niobrara shale play, there have been several permits approved for 1,280-acre spacing units, whereas up until recently, development has been on 640-acre units. Companies like Continental Resources plan to drill a 9,200-foot lateral section on a 1,280-acre unit, with a design that allows four wells from one single pad. Continental expects that: "benefits from the innovative approach include higher production from longer horizontal bores,

Dave Neslin, *Memorandum on Oil and Gas Activity in Colorado During 2010*, COLORADO OIL AND GAS CONSERVATION COMMISSION (January 11, 2011), <http://coloradoenergynews.com/2011/01/2010-oil-gas-activity-in-colorado-the-full-report/>.

<sup>2</sup>*Id.*

more efficient drilling and completion, and reduced environmental impact due to the smaller surface footprint, compared with four individual drilling sites."<sup>3</sup>

In early 2011, Chesapeake Energy Corporation announced the signing of a joint venture agreement to help develop the company's acreage prospective for the Niobrara. CNOOC Limited, a Chinese company, has agreed to pay \$570 million up front and fund two thirds of Chesapeake Energy's future drilling and completion costs until a \$697 million drilling carry has been reached.

#### Environmental

Based on the 2008 Ozone Action Plan, the Colorado Air Quality Control Commission adopted regulatory changes effective beginning in 2009 and carrying on through 2011. These measures include: increasing the system-wide control requirements for all condensate tanks to 90% by May 1, 2011, and removing current exemptions for selected small sources required to file air pollution emission notices and obtain permits.<sup>4</sup> The Ozone Action Plan includes elements that are federally-enforceable only, as well as elements that are state-enforceable only.

Based upon a lawsuit filed by WildEarth Guardians and the San Juan Citizens Alliance, EPA reviewed four air emission rules for oil and natural gas operations in Colorado.<sup>5</sup> The EPA reached a settlement in which it agreed to take final action by November 30, 2011. The final action will include, beyond a review of the air emissions standards, a "broad look at the oil and gas industry to identify and quantify sources of air pollutants, consider strategies for reducing them, and determine the environmental and economic effects of those strategies."<sup>6</sup>

<sup>3</sup> *Continental Resources Increases Production 20 Percent in Third Quarter of 2010, Compared With Third Quarter 2009*, BARRON'S (Nov. 3, 2010), <http://online.barrons.com/article/PR-00-20101103-912347.html>.

<sup>4</sup> *Denver Metro Area & North Front Range Ozone Action Plan*, (December 12, 2008), [www.cdphe.state.co.us/ap/ozone/RegDevelop/ozoneplan.pdf](http://www.cdphe.state.co.us/ap/ozone/RegDevelop/ozoneplan.pdf).

<sup>5</sup> *WildEarth Guardians et al. v. EPA*, (D.C. Cir. 2009) (complaint for declaratory and injunctive relief) available at <http://taberlaw.files.wordpress.com/2009/01/1-1.pdf>.

<sup>6</sup> Catherine Tsai, *EPA Reviews Oil and Gas Environmental Regulations After Lawsuit*, THE HUFFINGTON POST (August 3, 2010), [http://www.huffingtonpost.com/2010/08/04/epa-reviews-oil-and-gas-e\\_n\\_670217.html](http://www.huffingtonpost.com/2010/08/04/epa-reviews-oil-and-gas-e_n_670217.html).

**George Snell**

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Fw: Looking forward to receiving your updates tomorrow.

**Subject:**

----- Original Message -----

From: Richard W Revels Jr <mailto:rwrevels@OLiskow.com>  
Sent: Monday, February 14, 2011 7:37 AM  
To: George Snell  
Subject: RE: Looking forward to receiving your updates tomorrow.

On an activity note for La., you could mention the following:

The Haynesville Shale play in NW La. appears to be slowing down somewhat. The major operators are nearing having most of their acreage blocks maintained. The persistently low gas prices have been a disincentive to accelerate their development activities. Haynesville Shale gas wells produce virtually no liquids, so it is understandable that operators are looking elsewhere to take advantage of relatively favorable oil and condensate prices.

Several operators have been amassing large acreage positions in central Louisiana and the Feliciana parishes targeting the Austin Chalk and Tuscaloosa Marine Shale. Both of these intervals will require the drilling of long horizontal laterals similar to the Haynesville Shale; however, both produce considerable liquids though at a considerable cost of extraction.

Good luck on your presentation.

## Background on Michigan Lawsuits

In the spring of 2010, a test well was drilled into the Collingwood shale formation in Missaukee County, Michigan. The Collingwood Shale formation is almost 2 miles deep and can be rich in natural gas and oil. The Collingwood shale underlay's most of northern Michigan and is also a member of a family of shale formations found in Pennsylvania and Texas.

Known as the Pioneer well, this test well produced a reported 2.5 million cubic feet of natural gas per day in a 30 day test period. The initial test reports triggered the largest lease play the State of Michigan has ever experienced. On May 4, 2010, the State of Michigan held a mineral lease auction which generated \$178 million. Bidders paid an average of \$1,507 per acre for 118,000 acres across 22 counties. The May 4th sale generated more money for the State of Michigan than the past 81 years of mineral lease sales combined.

The May mineral lease auction also set in motion a rush by independent and major oil and gas companies to lease large blocks of private mineral acreage in Northern Michigan. Hundreds of Landmen descended on County courthouses researching tract indexes for available mineral acreage to lease. Minerals that heretofore had been leasing for \$25 per acre were now generating lease bonus payments of \$750-\$2,000 per mineral acre. Competition between the oil and gas companies for the mineral leases was extremely high. Informational seminars were conducted at Township halls, advertisements were placed in local newspapers and large massive lease signings were organized by the leasing companies, all in an effort to get the private sector minerals under control. It would not have been unusual for a perspective mineral owner to be visited by three or four Landmen on the same day, all offering attractive terms to lease.

Western Land Services, Inc., OIL Niagaran, Inc., and Silver Lake Energy LLC actively and aggressively leased large blocks of private mineral acreage in Northern Michigan. Perspective mineral owners were promised that they would receive the best price, amongst other things, for leasing their mineral acreage to them. In reliance on these representations, the mineral owners took their mineral acreage off the market and were precluded from leasing to other oil and gas companies when they leased to Western, Silver Lake, and OILN. This leasing **frenzy** continued until late July, 2010 when the leasing bonanza came to a screeching halt. A second test well was drilled which had poor results.

In October, 2010 the State of Michigan held a second mineral lease auction in which 450,000 acres were offered to lease. At the sale, 273,000 mineral acres were leased and \$10 million was generated as a result of the sale. The average lease price was less than \$40 per acre.

Shortly after the October mineral lease auction, hundreds of private mineral owners who had leased their minerals in good faith to Western Land Services, Inc., OIL Niagaran, Inc. or Silver Lake Energy LLC began receiving notices from Northern Michigan Exploration Company, LLC that their mineral lease had been voided and the accompanying order for payment for the **signing bonus would not be funded**. Western Land Services, Inc., OIL Niagaran, Inc. and Silver

Lake Energy LLC were directly or through third parties under the supervision and/or control of Chesapeake Energy Inc. The reasons given for cancellation of the leases fall into six categories:

- Outside the leasing area
- Signed too late (all leases were signed in the presence of the leasing agent, not mailed)
- Late payment on property taxes
- There is an existing mortgage on the property
- There is an unreleased lease in the chain of title (i.e. 1960's era)
- Signed the wrong lease form

In the same time period, Chesapeake Energy Inc. and OIL Niagaran Inc. notified other oil and gas companies, including but not limited to Frontier Energy Inc. and Continental Resources Inc., that they would not be honoring contractual obligations to purchase large lease acreage blocks totaling over \$100 million .

The suit being brought by Topp Law and Rolinski pertains to defrauding hundreds of mineral owners, by nonpayment of the lease signing bonus pursuant to a scheme and plan devised by the Defendants to control and manipulate the lease market in Michigan at the expense of the mineral owners and other oil and gas companies.

The legal issues arising out of this occurrence are as follows:

- When does the Prudent Operator Standard arise, upon execution of the lease or upon payment of the bonus?
- Is the approval of title subject to the Prudent Operator Standard?
- Is the standard for title approval curable title or perfect title?
- Is the payment under the order to pay a condition precedent or condition subsequent?

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February 14, 2011

**CARBON SEQUESTRATION LEGISLATION**

Lawmakers are considering bills to allow and regulate long-term underground carbon dioxide storage, a practice proponents say will help increase the state's oil production while reducing greenhouse gas emissions.

Mississippi oil fields have seen a resurgence in the last few years, primarily due to the use of carbon dioxide to coax out additional oil reserves. For more than a decade, companies have pumped a naturally occurring supply of carbon dioxide back underground to revive oil wells in south Mississippi. Shell Oil had used the method in the late 1970s and early 1980s, but more recently other companies started seeing results from major projects in the last 10 years.

The state Oil and Gas Board oversees the use of carbon dioxide in oil wells. Capturing manmade carbon dioxide and storing it underground could attract a long-term supply oil companies could use. There are major deposits of natural carbon dioxide located in Mississippi.

Supporters of the proposal also say it could help Mississippi be among the states at the forefront of the federal push for "clean coal" technology, an experimental technique to store underground the carbon emissions from coal-fired power plants and other sources. This legislation creates the framework of how that's going to take place and who's going to be handling which aspects of the process.

Under the bills, the Dept. of Environmental Quality would work out an agreement with the Mississippi Oil and Gas Board to store the gas in oil and gas fields and other locations.

A company monitoring the legislation is Mississippi Power Co., which is building a \$2.4 billion coal-fired plant in Kemper County that is expected to capture 65 percent of its carbon emissions through an innovative design and store the gases underground.

### **SHALE ACTIVITY**

Mainland Resources Inc is drilling an ultra deep 22,000 foot Haynesville Shale well in Mississippi's Jefferson County. Work on this well started some time back and it should now be nearing total depth.

A Mainland press release states, "The initial results from the core analysis provide very encouraging insights into the gas potential of the deep section of the Burkley-Phillips #1 well. The fact that we are over pressured lends itself to larger gas recoveries within smaller pore spaces and the laboratory measurement of gas filled porosity supports the multiple mud log gas shows seen while drilling the well through this interval. Simply put, this is exactly what we would look for in a productive shale gas well. We are looking forward to the ongoing assessments as they further refine the prospectivity of this well."

### **WHERE SURFACE AND MINERALS ARE COMPLETELY SEVERED MINERAL OWNER OWNS ABANDONED WELL BORE AND EQUIPMENT**

A judgment by the Chancery Court of Lincoln County, Mississippi in *Douglas v. Denbury*, Cause No. 2009-0178, dated February, 2010, held that where there has been a complete severance of the surface estate and the mineral estate, the abandoned well bores and

related downhole equipment are owned by the mineral owner as opposed to the surface owner and that the mineral lessee has the right to use plugged and abandoned well bores and a reasonable area of surface without compensation to the surface owner on the basis that the mineral estate is the dominate estate, together with the theory of the ownership of minerals in place. The judgment was appealed to the Mississippi Supreme Court, which assigned it to the Mississippi Court of Appeals, where, on January 4, 2011, it was submitted without oral argument.

### **ENERGY COMPANIES MAY BE LIABLE FOR GLOBAL WARMING**

A three judge panel of the U. S. Fifth Circuit held, two to one, that oil, mining and energy companies may be sued for contributing to global warming, even though the lower court had dismissed such claims. *Corner v. Murphy Oil USA*, 585 F.3d 855 (Oct. 16, 2009). This is one of a leading edge of cases which hold that producers of pollutants maybe liable for global warming weather changes. Two other cases are *Massachusetts v. Environmental Protection Agency*, 549 U.S. 497 (2007) and *State of Connecticut v. American Electric Power, Inc.*, 582 F.3d 309 (2009).

The Court's decision has been lost in a procedural black hole. The defendants asked the matter be heard by the entire panel. Before the motion was heard, several judges had recused themselves so that the motion was considered by only nine judges, who granted the motion. Afterwards, one of the nine judges recused himself resulting in the panel no longer having a quorum. Because it did not have a quorum to decide the matter the panel, with two dissents, dismissed the appeal, thus leaving the lower court's dismissal in place.

**SEVERMINERAL OWNERS NOT ENTITLED TO NOTICE IN EVERY INSTANCE**

A tax collector conducting a sale for delinquent taxes is not required to search the public records to locate owners of severed, fractional minerals so that a tax sale is valid even if the mineral owner did not have actual notice. *AARCO Oil and Gas Co. v. EOG Resources, Inc.*, 20 So.3d 662 (Miss. 2009). The court noted *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306 (1950) and *Mennonite Board v. Adams*, 462 U.S. 791 (1983) but held that the U.S. Supreme Court did not require actual notice in every instance and did not require a governmental body undertake extraordinary efforts to discover the identity or whereabouts of a mortgagee.

**RE: REMOTE ASSIGNEE OF LEASE ASSUMES ALL OBLIGATIONS IN PRIOR ASSIGNMENT; AGREEMENT FOR CONTINUATION OF OVERRIDE IN RENEWAL LEASE NOT VOID UNDER RULE AGAINST PERPETUITIES.**  
*Gill v. Gipson*, 982 So.2d 415 (Miss. App. 2007).

**MISSISSIPPI TAX DUE ON NATURAL GAS USED FOR PLANT AND LEASE FUEL.** *Pursue Energy Corp. v. State Tax Commission*, 968 So.2d 368 (Miss. 2007).

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ALSO ADMITTED IN COLORADO  
AND PENNSYLVANIA

February 7, 2011

George A. Snell, III  
Snell Law Firm  
2201 Civic Circle, Suite 508  
Amarillo, TX 79109

Re: Houston Bar Oil and Gas Section

Dear George:

In regard to your planned talk at the Houston Bar meeting, the following are some items relating to the situation in New York for your review and discussion.

Any discussion of New York must take into account the background of a disfunctional state government, former high officials including a governor either indicted or convicted of felonies and abysmal ignorance on the part of the legislators who are voting on these matters in craven submission to the more fanatical environmentalists. This includes the various parties and groups who claim to be working to preserve the purity of the New York City watershed as well as other watersheds while ignoring the impact of other threats such as agricultural operations, septic systems, storage tanks etc.

Title Issues:

1. Getting subordinations from lending institutions has always been a problem in New York outside of the old oil and gas producing areas in the southwest corner of the State. This continues to be a problem, especially in situations where foreclosures are pending. However, with the recent change in law relating to work-outs of mortgages the judges have appeared to have slowed down the foreclosure process in

order to give the borrowers an opportunity for a work-out.

2. An unfavorable decision has just been rendered by a court in the eastern part of the State relating to a request by the oil and gas operator that the assets of the debtor be "marshaled" in order to satisfy the foreclosure thus in effect segregating the oil and gas rights from the surface in order to allow the surface to be sold on its own to satisfy the mortgage. The operator is considering an appeal of this decision.

With regard to tax foreclosure proceedings, at least one County has made it their

3. policy to obtain a Judgment in a tax foreclosure proceeding without affecting the rights of the oil and gas operator. In other counties, the effect of a Tax Foreclosure Judgment is somewhat of a gray area, because operating oil and gas wells and their associated equipment and pipeline are separately taxed as real estate including a separate tax parcel number distinct from the landowners. Thus the effect of a tax foreclosure proceeding against the landowner alone would presumably not affect the operator's interest in the well. However, the effect on the lease itself is an open question.

#### Operational Issues:

I. All operational questions are overshadowed by the functional equivalent of a moratorium presently in force. See the discussion below under political issues.

Pursuant to the Executive Order only low volume fracking is permitted at this

2. time.

Traditional shallow oil operators continue to operate, as do the producers from

3. the rather shallow Medina gas wells primarily located in the southwestern portion of the State. Other zones of interest including the Trenton Black River and the Marcellus Shale are primarily of interest in the eastern portion of what is known as the southern tier of New York State along the Pennsylvania border. These newer areas of interest have been severely impacted by the moratorium.

#### Political Issues:

I. The situation in New York is unique in all of the United States in that no permits are being granted pursuant to an Executive Order signed by the Governor when he vetoed a law passed by the legislature to outlaw all but very low volume hydrofracking for a period of time for "further study". This has effectively shut down exploration activity in New York.

2. One of the most severe impacts of the moratorium has been upon the exploration of leases which can not be drilled to be extended beyond primary term. The Department of Environmental Conservation has been working on what is known as a "Generic Environmental Impact Statement" to satisfy a State law which required the same to be adopted in order to avoid the requirement for a specific environmental impact statement for every single well being drilled in the State. No other state has anything remotely approaching such a bureaucratic traffic jam which has held up most of the other work of the department for over two years.

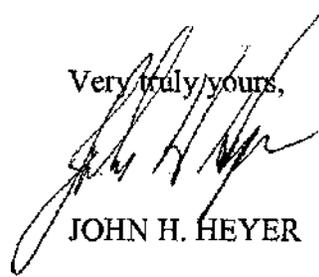
4. The propaganda being spewed out by parties such as the creator of the "gas land" video, and others have been swallowed by many of the public in the eastern part of the State as well as editorial writers for various newspapers.

The independent oil and gas association of New York is making valiant efforts

5.

to counteract the propaganda and educate the public in various forums, but it is a tiny organization in comparison to other states, and it is extremely shorthanded in trying to combat the many sources of misinformation and their use of various forums such as local legislatures and public venues to spread their propaganda. If IOGA can effectively counteract the misinformation, it will be of material benefit to other states in preventing the spread of the anti-drilling efforts which are primarily based upon erroneous or even libelous information by parties who are interested not only in stopping drilling activity but indeed stopping any type of development of natural resources.

Very truly yours,

A handwritten signature in black ink, appearing to read "John H. Heyer", written in a cursive style.

JOHN H. HEYER

JHH/ch

## George Snell

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**Subject:** FW: Houston Bar - Oil and Gas Section - Tuesday, February 22

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**From:** Timothy McKeen [fmailto:Timothy.McKeen@StepToe-Iohnson.com](mailto:Timothy.McKeen@StepToe-Iohnson.com)

**Sent:** Sunday, February 13, 2011 9:05 PM

To: 'George Snell'

**Subject:** RE: Houston Bar - Oil and Gas Section - Tuesday, February 22

The new year marks the start of a new government for Ohioans. Republican John Kasich has replaced Democrat Ted Strickland as the state's new governor and both houses of the state legislature are controlled by the Republican party. Oil and gas development is an important part of the new governor's agenda and the Utica Shale may be the perfect vehicle for that agenda. Located deeper than the Marcellus, the Utica Shale is found throughout the state, though some speculate it will be best developed in the Eastern part of the state, which is Ohio's traditional oil and gas territory. According to a spokesperson for Pittsburgh based Consol Energy, a vertical test well for the Utica Shale in Belmont County, Ohio produced 1.5 million cubic feet of gas in one day without using hydrofracturing or any other well stimulation technology. (*Dig Deep*, Williamsport Sun Gazette, December 19, 2010). Thus many speculate there could be great potential for Utica development.

As I mentioned in my article, Ohio does not have significant case law regarding oil and gas. I would predict that as the stakes continue to increase, there will certainly be increased litigation and a very real possibility of the Ohio Supreme Court having and the lower courts will have the opportunity to develop more case law in this area. In June of last year, a bipartisan government passed, significant updates to its oil and gas statutes, and I do not see the likelihood of much change in this area, as the oil and gas industry supported the changes.

Tim

McKeen

## NEWSLETTER

FEBRUARY 2011

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North Dakota's "dormant mineral act," located in North Dakota Century Code (N.D.C.C.) Chapter 38-18.1, allows a surface owner to acquire an abandoned mineral interest where the interest has not been used, as defined by the code, for a period of twenty years. The dormant mineral act is the subject of the first three cases in this newsletter.

*Sorenson v. Felton*

**2011 ND 33**

**Filed February 8, 2011**

### **Facts**

#### **I.**

Michael Sorenson is the surface owner of the land. Barbara Felton acquired an interest in the minerals pursuant to a personal representative's deed in 1984. From 1984 until January 2008 Felton did not lease the minerals or file a statement of claim. In January 2007, in accordance with North Dakota law, Sorenson published a notice of lapse in the newspaper in Mountrail County, ND and mailed a notice to Felton using the Florida address from the personal representative's deed. Sorenson also conducted a Yahoo! People search but found no address for Barbara Felton in Florida. On January 9, 2008 Felton leased her mineral interest to Schmitz Oil Properties. Sorenson filed a complaint to quiet title to the mineral interest in question.

#### **II. Holding**

N.D.C.C. § 38-18.1-06(2) requires notice of lapse by mail "if the address of the mineral interest owner is shown of record or can be determined upon reasonable inquiry." Paragraph 11. The Court held that because the phrases "shown of record" and "determined upon reasonable inquiry" are separated by the word "or" they are separate and alternative considerations for how a surface owner is to obtain the mineral owner's address for mailing the notice. Paragraph 13. Therefore, Sorenson was only required to conduct a reasonable inquiry if Felton's address was not shown of record. Since her address was shown of record on the 1984 conveyance, he was not required to conduct any further inquiry. Because an address appears of record and because the notice was sent to the address of record, Sorenson satisfied the requirements of the statute and successfully succeeded to the ownership of Felton's minerals.

Sorenson v. Alinder  
**2011 ND 36**  
**Filed February 8, 2011**

**I. Facts**

Michael Sorenson is the surface owner of the land. Russell and Edna Alinder acquired an interest in the minerals pursuant to a mineral deed recorded in 1953. Russell Alinder died in 1980 and Edna Alinder died in 1999 without ever leasing the minerals or filing a statement of claim. Under North Dakota law, the interest of Russell and Edna Alinder passed to their heirs on the dates of their death subject to administration of their estates. Ken Alinder, Robert Alinder and Sharon Dragland are the heirs of Russell and Edna Alinder. In accordance with North Dakota law, Sorenson published a notice of lapse in January 2007 and mailed the notice to Russell and Edna Alinder at their address of record in Buffalo, ND. Sorenson filed a complaint to quiet title to the mineral interest in question.

**H. Holding**

The issue is whether the district court erred in requiring Sorenson to conduct a reasonable inquiry when the address of Russell and Edna Alinder was shown of record. The Supreme Court cited their decision in *Sorenson v. Felton*, and held N.D.C.C. § 38-18.1-06(2) only requires a reasonable inquiry when the mineral owner's address is not shown of record. The Court held that Sorenson complied with the requirements of the statute by mailing the notice to Russell and Edna Alinder at their address shown of record and he was not required to conduct any further inquiry. Sorenson satisfied the requirements of the statute and successfully succeeded to the ownership of the Alinders' minerals.

Halvorson v. Starr  
**785 N.W.2d 248**  
**Filed July 13, 2010**

**Facts**

**I.**

The surface owners (Halvorsons) executed and published a notice of lapse of mineral interest asserting the Stan's mineral interest had been unused for twenty years and the Halvorsons sought to make claim to the mineral interest. As required by the act, the Halvorsons published the notice of lapse of mineral interest in March 7, 14 and 21, 1990. The Halvorsons mailed the notice of lapse to the Starrs on April 2, 1990, the twelfth calendar day after the notice of lapse was published.

In June 2009, the Halvorsons sued the Starrs to quiet title to the mineral interest in question. The district court granted summary judgment to the Starrs, noting that the notice of lapse was not mailed to the Starrs within ten days of last publication, as required by the act.

## II. Holding

The Halvorsons appealed the district court ruling arguing that the North Dakota Rules of Civil Procedure governs the computation of time for N.D.C.C. § 38-18.1-06. If the North Dakota Rules of Civil Procedure are applied, the Halvorsons mailed the notice of lapse on the tenth day, in compliance with the act, because Saturday, March 31 and Sunday, April 1 would not be counted in the ten days. If the version of N.D.C.C. § 1-02-15 in effect when the Halvorsons mailed their notice of lapse is applied, the Halvorson's mailing was not timely because Saturdays are counted in the ten day period.

The North Dakota Supreme Court held that because N.D.C.C. § 38-18.1-06 does not begin a civil action and is not part of a procedure in district court, the computation of time under that code section is governed by N.D.C.C. § 1-02-15, not by the North Dakota Rules of Civil Procedure. The Court further noted that after the Halvorsons executed the notice of lapse, N.D.C.C. § 1-02-15 was amended to also exclude Saturdays from the computation of time. Thus, under the amended version of N.D.C.C. § 1-02-15, the Halvorson's mailing was timely. However, the Court held the amended version of N.D.C.C. § 1-02-15 does not apply retroactively to claims made under N.D.C.C. § 38-18.1, prior to the amendments to N.D.C.C. § 1-02-15. Since the amended version does not apply retroactively, the Starrs retain their ownership of the minerals.

*Irish Oil and Gas, Inc. v. Riemer*

2011 ND 22

Filed February 8, 2011

## I. Facts

Irish Oil and Gas Inc. entered into oil and gas leases with Gerald C. Riemer, Doris E. Riemer, Lillie J. Riemer and Joanne Johnson (the "Riemers") in January and February 2008. A Letter Agreement accompanied each lease and provided an offer of bonus consideration of \$160 per net mineral acre and a 1/6 royalty in the event of production. The Letter Agreement also provided that within 60 days of receipt of the signed lease, "subject to approval of title, with right of payment extension of 30 additional days, in the event of title curative issues, from expiration of original 60 days" the Riemers would receive a check for \$10,640.

Because he had not received a check for the bonus consideration, Gerald C. Riemer called Irish Oil and spoke with Tim Furlong, vice president of Irish Oil, regarding the bonus consideration. Following the conversation, Irish Oil sent a letter to Riemer purporting that Riemer agreed to extend the payment deadline to June 15. Irish Oil explained it needed more time because it had encountered title issues. Irish Oil ensured it would communicate with Riemer if the payment were to be delayed past June 15. Gerald C. Riemer claims he did not agree to extend the deadline for payment by Irish Oil, while Irish Oil claims Gerald Riemer agreed to an extension.

On April 30, 2008 Gerald C. Riemer leased the same mineral interest to Continental Oil Company. Subsequently, Irish Oil mailed the Riemers a check for the bonus consideration owed. The Riemers returned the check along with a letter indicating the minerals had been leased to another company. Irish Oil sued the Riemers alleging breach of contract.

## **IL Holding**

### **A. Lease Paragraph 16**

Paragraph 16 of the oil and gas leases provided:

"This lease shall not be terminated, forfeited, or canceled for failure by Lessee to perform in whole or in part any of its implied covenants, conditions, or stipulations until it shall have been first finally and judicially determined that the failure or default exists, and then Lessee shall be given a reasonable time to correct any default so determined, or at Lessee's election it may surrender the Lease with the option of reserving under the terms of this Lease each producing well and forty (40) acres surrounding it as selected by Lessee, together with the right of ingress and egress. Lessee shall not be liable in damages for breach of any implied covenant or obligation."

Irish argued this paragraph requires Riemer to obtain a judicial determination of a breach and allows the lessee a reasonable time to cure the breach. The Supreme Court affirmed the district court's decision that the phrase "implied covenants, conditions or stipulations" does not apply to express provisions of the lease. Thus, this provision applies to the implied covenants found in the oil and gas lease and not to the obligation to pay lease bonus.

### **B. Failure of Consideration**

The issue was whether consideration failed when Irish did not pay the bonus consideration when promised. The district court held there was a total failure of consideration and the Supreme Court reversed and remanded for a factual determination.

The Court held that it could not say, as a matter of law, that the potential for royalty is not sufficient consideration to support the lease. The Court also could not say that failure to timely pay bonus leaves the leases with a total failure of consideration that excuses Riemer's performance. Rather, the Court stated a fact issue exists as to whether the anticipated royalty payments provided for in the royalty clauses of the leases provide adequate consideration to uphold the contract even where the bonus consideration fails.

**Melchior v. Lystad**  
786 N.W.2d 8  
Filed July 13, 2010

**Facts**

**I.**

Walter and Edith Halvorson owned one-half of the minerals. The Halvorsons conveyed property to Kenneth and Hope Lystad pursuant to a contract for deed. The contract for deed and warranty deed both contained a reservation of one-half of the minerals. The Halvorsons later conveyed their mineral interest to Roger and Barbara Melchior. In 2009 the Melchiors sued to quiet title to one-fourth of the mineral interest in question.

**Holding**

**II.**

The district court ruled in favor of the Lystads citing the Duhig rule. The Melchiors did not dispute the Duhig rule. The issue on appeal was whether the warranty deed should be reformed based on mutual mistake. The Melchiors alleged that the deeds were based on mutual mistake and that the Halvorsons' and Lystads' intent was to reserve and convey one-half of the minerals owned by the Halvorsons, not one-half of the total.

For a mutual mistake to justify reformation of a contract, "it must be shown that at the time of the execution of the agreement...both parties intended to say something different from what was said in the instrument." The Court held that there was not sufficient evidence to prove that both parties intended to say something different from what was said in the instrument. The Court affirmed the district court's grant of summary judgment to the Lystads.

**Anderson v. Hess Corporation**  
2010 WL 3329399 (D.N.D.)  
August 25, 2010

**I. Facts**

The Andersons owned mineral rights and leased them to Diamond Resources, Inc. on May 3, 2004. Diamond transferred the leases to Duncan, who transferred them to Hess.

The leases contained a standard habendum clause which included the following language:

"If, at the expiration of the primary term of this lease, oil or gas is not being produced on the leased premises or on acreage pooled therewith but Lessee is **then engaged in drilling or reworking operations thereon**, then this lease shall continue in force so long as operations are being continuously prosecuted on the leased premises or on acreage pooled therewith." (emphasis added)

In October 2008 Hess began preparations for a well on the leased land. From January to May 2009, Hess moved equipment to the well, began to prepare the surface, leveled and lazed the pad, dug the drilling pit, widened the access road to the well, drilled the rat hole and made other preparations for drilling. Problems at another well prevented Hess from completing its plans to move a rig to the well prior to May 3, 2009. Hess spud the well on May 11, 2009, after which it was continuously drilled until total depth was reached on June 26, 2009. The well has produced continuously since June 30, 2009.

On May 7, 2009 Hess attempted to extend the lease term by offering to increase the royalty. The Andersons rejected the offer on May 8, 2009. The Andersons subsequently filed a complaint alleging the leases expired prior to the date the well was spud. Hess contends the leases did not expire because it was engaged in drilling operations prior to expiration of the primary term.

#### **H. Holding**

The issue was whether the habendum clause requirement that Lessee be engaged in drilling or reworking operations at the expiration of the primary term requires spudding of the well in order to extend the leases.

The Court reaffirmed its prior holding from *Murphy v. Amoco Prod. Co.*, that "drilling operations commence when (1) work is done preparatory to drilling, (2) the driller has the capability to do the actual drilling, and (3) there is a good faith intent to complete the well. It is not necessary that the drill bit actually penetrate the ground." Additionally, the Court found that "operations" modifies both "drilling" and "reworking" and the phrase "drilling or reworking operations" includes both "drilling operations" and "reworking operations."

The Court also stated that actual drilling is unnecessary to extend the lease term, but that "the location of wells, hauling lumber on the premises, erection of derricks, providing a water supply, moving machinery on the premises" and similar acts preceding the actual drilling, when paired with an actual intent to drill and subsequent drilling of a well, constitute drilling operations. The Court found that Hess engaged in drilling operations, effectively extending the leases beyond the primary term.

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February 11, 2011

TO: HOUSTON BAR ASSOCIATION — OIL AND GAS SECTION

This paper is designed to cover newly identified or unknown title issues.

In some of these issues that are addressed, there may not be a satisfactory resolution to the issue or the author does not have a recommendation to make. However, being aware of these issues could help the landman be aware of traps that he/she could fall into.

## 1. COVERALL LANGUAGE IN A DEED OR ASSIGNMENT.

**In order that** a conveyance be operative, it is essential that the premises granted and intended to be conveyed be described with enough certainty to be located and distinguished from other lands of the same kind. *Arbuckle Realty Trust v. Southern Rock Asphalt Co.*, 189 Okla. 304, 116 P.2d 912 (1941).

Oil and gas examiners frequently encounter conveyances that do not give a definite description, but specify that the grantor conveys all his interest in a described county, such as "all my interest in Roger Mills County" or all interest inherited from a specific person.

Decisions in cases in other states deciding the legal effectiveness of such conveyances are mixed depending on the specificity of the description. *Patton and Palomar on Land Titles* states that such conveyances are generally held to be effective if the deed contains sufficient information so that by reference to some document or instrument referred to in the deed, a true and accurate description can be ascertained. *Patton and Palomar on Land Titles*, § 125 (3d ed. 2010). However, since Oklahoma has a tract index system, the law may not be applicable.

The Kansas case of *Luthi v. Evans*, 576 P.2d 1064 (Kan. 1978) held that the conveyance would be considered valid between the parties even if the document does not constitute constructive notice.

There has been no decision in Oklahoma on this question. However, a recent bankruptcy case out of Texas interpreting Oklahoma law may provide the answer to this issue.

A recorded conveyance provides constructive notice when it is "recorded as prescribed by law." 16 O.S. §16. Oklahoma Statute Title 19 § 298 requires that every document offered for recording "shall by its own terms describe the property by its specific legal description, and provide such information as is necessary for indexing as required in Sections 287 and 291 of this title...." In turn, §§ 287 and 291 direct the clerk of each county to keep a grantor-grantee index and a tract index, respectively.

The United States Bankruptcy Court for the Northern District of Texas in *In Re: Cornerstone E&P Company, L.P.*, 2010 WL 3342037 (Bkrcty.ND.Tex), ruled that a deed may only be "recorded as prescribed *by* law" if it contains a specific legal description and provides sufficient information for indexing both in the grantor-grantee index and the tract index.

The *Cornerstone* court concluded that the language of the statute is unambiguous and that, therefore, to constitute constructive notice, the conveyance must provide a specific legal description sufficient for indexing both the county grantor-grantee index and the county tract index.

The *Cornerstone* court held that blanket conveyances would not be constructive notice and made a further distinction that both Kansas and Oklahoma, unlike Texas, utilize tract indices in addition to a grantor-grantee index for recording. The *Cornerstone* court indicated the distinction was important, because while a prospect purchaser would be able to locate a mortgage related to a particular real property indexed through a grantor-grantee index, that same mortgage could not be located through a tract index.

## **2. AFFIDAVIT OF POOLING UNDER 52 O.S § 87.4.**

Oklahoma Statute Title 52 § 87.4 recites the following:

An affidavit evidencing any election for the drilling of a well under a pooling order issued pursuant to the proceedings set out in subsection (e) of Section 87.1 of Title 52 of the Oklahoma Statutes shall constitute constructive notice of the rights under the election claimed by the affiant when the affidavit is filed of record in the office of the county clerk for the county in which the lands described in the pooling order are located. The affidavit shall, set out the name, address, if known, and election or deemed election for each pooled respondent included in the affidavit and shall have a copy of the pooling order attached. The affidavit may be filed by the operator designated in the pooling order or by any other interested

party with knowledge of any election made. Filing of the affidavit shall not affect notice provided by virtue of the pooling proceedings conducted by the Commission.

The statute recites that the affidavit shall constitute constructive notice of the rights. If this affidavit constitutes constructive notice, then in the absence of the affidavit, is the statute suggesting that the pooling is not constructive notice until such time as the affidavit is filed. Would a mortgage issued by a bank to a lessee or a mineral owner be superior to the pooled interest if the mortgage was recorded prior to the affidavit, or recorded in the absence of any affidavit?

### **3. MEMORANDUM OF LEASE — CONSTRUCTIVE NOTICE.**

Oklahoma Statute Title 16 § 16 recites "every conveyance of real property acknowledged or proved, certified and recorded as prescribed by law from the time it is filed with the register of deeds for record is constructive notice of the contents thereof to subsequent purchasers, mortgagees, encumbrances or creditors."

A memorandum of an oil and gas lease is not a conveyance. It is a memorandum of *a* conveyance. Therefore, the memorandum of lease may not constitute constructive notice.

If a lease broker examines the records and examines the memorandum of lease, then the broker is on actual notice or, at a minimum, "inquiry notice" to find out if the lessor executed a lease. However, in a race to the courthouse situation, a memorandum of lease may not be superior to an actual recorded lease to a rival lessee, as the memorandum may not be constructive notice.

A memorandum of lease could be constructed so as to show certain terms and so that it would rise to the level of a conveyance. For example, if the lease showed the name of the lessor and lessee, land description, contained words of grant, and referenced a letter agreement between the parties containing additional terms, then this would be considered to be a conveyance as it contains the essential elements of a conveyance. This type of memorandum would constitute constructive notice under the statute.

### **4. PREFERENTIAL RIGHTS IN TOP LEASES.**

A recent phenomenon in oil and gas leases in Oklahoma is the inclusion of a preferential right to purchase any top lease that is acceptable to the lessor. The clause typically states the following:

If, at any time within the primary term of this lease and while the same remains in force and effect, Lessor receives any bona fide offer, which Lessor is willing to accept from any party offering

consideration to Lessor for a lease (top lease) covering any or all of the substances covered by this lease or covering all or portion of the land described herein with the top lease becoming effective upon the expiration of this lease, Lessor hereby agrees to immediately notify Lessee in writing of said offer, setting forth the proposed Lessee's name, bonus consideration and royalty to be paid for such lease, and Lessor shall include a copy of the lease form to be utilized which form shall reflect all pertinent and relevant terms and conditions of the top lease.

One question that has arisen is who is to be given notice under the lease if the lease was acquired by a lease broker. Is the notice to be given only to the lease broker? If the third party top lessee is knowledgeable that the lease has been assigned from the broker to an oil company, then is the notice to be given to the surtcAssor lessee, or is it sufficient to only give it to the original lessee?

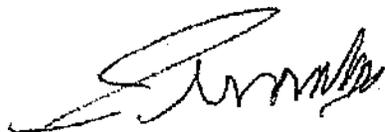
The author is unable to find any court decisions that resolves this question. However, it is my opinion that notice to the original lessee is sufficient in the absence of notice given to the lessor of a change in the lessee. In other words, it would not appear to be the lessor's duty to check records to determine whether this lease has been assigned to a third party. As this is a contract between the lessor and the lessee, the notice to the known lessee is adequate.

Further, another part of the lease typically recites that "No change in the ownership of the land or royalty shall be binding on the Lessee until after the Lessee has been furnished with a written transfer or assignment or a true copy thereof." It could be argued that this same provision would also be obligatory on the part of the lessee to notify the lessor as to the change of ownership.

Sincerely,

ELIAS, BOOKS, BROWN & NELSON

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Timothy C. Dowd



## MEMORANDUM

To: George A. Snell, Esq.

From: R. L. Schetroma, Steptoe & Johnson

J<sup>S</sup> R A<sup>L</sup>

PLLC Date: January 31, 2011

Re: Pennsylvania Update

ATTORNEYS AT LAW  
PLLC

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### Title Issues

**Continuance of leases** — paying quantities. Pennsylvania has ancient law defining "paying quantities" basically as anything over actual operating cost (without consideration of capital costs) subject to the continuing good faith of the operator in seeking to hold the lease. This concept was recognized in a 2008 Intermediate Appellate Court decision. *Phillips v. Jedlicka*. The Pennsylvania Supreme Court took up the decision on the question of whether the operator's subjective intent would continue to govern lease continuation. No decision has yet been reached.

Continuance of **the leases** — perpetual delay rentals/nature of lessee's interest in an oil and gas lease. In January 2011, the Pennsylvania Supreme Court recognized the potential for a valid perpetual lease supported only by perpetual delay rental payments. It held, however, that a clear intent to achieve such a result must be stated in the instrument and ruled that such intent was not present in the case before it. In order to avoid the otherwise plain language of the lease, the Supreme Court clarified that a Pennsylvania oil and gas lease does, in fact, grant a fee simple determinable in the oil and gas to the lessee but only from and after the time oil and gas is discovered on the leasehold by efforts of the lessee. Until that point a lessee's rights are "inchoate." *Hite v. Falcon Partners*.

### Operational Issues

Lack of legal infrastructure. Operations continue to be conducted in the absence of a complete legal infrastructure. For example, only four cases in Pennsylvania history use the words "pooling" or "unitization" and none of them decide a fundamental pooling issue. Many issues that have been decided are based upon 19<sup>th</sup> century and very early 20<sup>th</sup> century decisions including such fundamental matters as: a.) Pennsylvania's classification as an "apportionment" state for royalty payment and b.) The continued viability of Pennsylvania's *Dunham* rule holding that grants or reservations of

"minerals" do not include oil or gas. Pennsylvania does have a conservation statute but it is a creature of the 1960s, has only been used 15 times and does not apply to the Marcellus Shale.

### **Political Issues**

**Executive.** Pennsylvania has a new governor who it is hoped will be more reasonable with oil and gas issues than his Democratic predecessor. It is also hoped that the new administration's leadership in the Commonwealth's Department of Environmental Protection will demonstrate greater capacity to understand the technical issues related to oil and gas operations and less interest in appeasing irrational anti-development activists. It is also hoped that the new administration will recognize that continued development of Pennsylvania's shales, without the burden of a severance tax, will in fact, produce greater development and greater revenue for the Commonwealth.

**Legislative.** Radical anti-development bills continue to be introduced in the Pennsylvania legislature. The potential for the adoption of the essential new legislation for the continued development of the industry in the Commonwealth has not yet been determined. Among the most important legislative needs are a.) The adoption of a reasonable statutory pooling and unitization law focused upon shale development and b.) an amendment to the Oil and Gas Act or the Municipalities Planning Code to properly clarify the preemption of local municipal regulation in oil and gas matters. It is important to remember that Pennsylvania has more than 2,000 municipal entities, many of which are capable of adopting and enforcing separate and different land-use regulatory regimes.

*Note.* Any opinions stated in this update are those only of the Author and not necessarily those of the Author's firm or any clients of the firm.



N.

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February 11, 2011

George A. Snell, M  
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Dear George:

In response to your request for news of new or interesting developments, the most recent noteworthy development in Wyoming is the approval by the Wyoming Oil and Gas Conservation Commission of **some** 1280-acre drilling and spacing units for horizontal oil wells with proposed horizontal laterals in excess of 9,000 feet long for the Niobrara and Frontier Formations in the Southern Powder River Basin. The drilling units created are rectangles, two miles long, one mile wide, consisting of two full governmental sections, oriented North-south direction. These drilling units were created by the Commission, this past Tuesday, February 9, 2011, after a hearing in which I represented the Applicant, Helis Oil & Gas Company, LLC.

Such large drilling units and long horizontal wells are old-hat in North Dakota's Bakken, but new for Wyoming's Niobrara play.

Best to you in your talk.

Very truly yours,

  
CRAIG NEWMAN



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Writer's Contact Information:

**Current Natural Gas Issues in West Virginia**  
**By Richard Gottlieb, Lewis, Glasser, Casey & Rollins, PLLC**

With the current focus on Marcellus Shale resources and the technology of horizontal drilling, the biggest issue in West Virginia is regulatory reform to address what is essentially a new kind of industry and interest. Lawmakers and interest groups seem to be in agreement that a new category of well, the shallow horizontal well, must be recognized and dealt with. Significantly, this has led to a movement away from the law of capture for shallow horizontal wells and the development of forced or statutory pooling.

West Virginia's current regulatory system divides wells into two categories: shallow and deep. A shallow well is defined as any well drilled and completed in a formation above the top of the uppermost member of the Onondaga Group, however, the operator may penetrate into the Onondaga Group to a reasonable depth, not in excess of twenty feet, in order to allow for logging and completion operations. A deep well is defined as any well, other than a shallow well, drilled and completed in a formation at or below the top of the uppermost member of the Onondaga Group.

The Marcellus Shale is a shallow formation. Shallow wells are much less regulated than deep wells, but do not have a provision that allows for forced or statutory pooling. There are also no spacing rules for shallow gas wells, unless a coal interest objects to the well drilling application. However, in order to effectively and efficiently produce from the Marcellus Shale, producers may have to penetrate further than the statutory limit of twenty feet into the Onondaga Group, for logging. Nevertheless, production is all from a shallow formation. Accordingly, the Marcellus Shale wells have presented producers with challenges on the permitting front. As the law stands today, a deep well permit is required if production requires drilling for "rat holes" and logging that exceed the maximum penetration of twenty feet into the Onondaga Group, regardless of the depth of the producing formation.

Other major issues that have come up with Marcellus Shale production include water issues and surface use. To address concerns related to water usage and disposal, the West Virginia Department of Environmental Protection ("WV DEP") has issued new regulations. The WV DEP maintains that water availability, and the manner of delivery of water to the well site, should be considered as part of the exploration and development strategy. Water issues now

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more of a focus in erosion control plans and in the context of construction stormwater issues. The DEP has primarily focused on water disposal of frac fluids as the greatest challenge facing Marcellus development and has issued new regulations with special requirements for large water volume operations (a 5,000 barrel threshold of liquid disposal production) whether deep or shallow. For example, if 5,000 barrel liquid disposal of production is anticipated, the corresponding pit must be designed by an engineer and the water disposal program fairly detailed in its layout. There is a new addendum to well work permits that expressly addresses some of these issues. Further, the WV DEP has stated that the only acceptable disposal methods for completion returns for Marcellus Shale wells are recycling, reuse and UIC. Land application as a disposal method has been prohibited for current permit applicants.

Surface owner issues and complaints have also increased with Marcellus Shale production. Horizontal drilling and fracturing generally require much more surface disturbance than traditional drilling. Increased traffic and equipment necessary for fracturing have also become areas of contention. In response; WV DEP has required that permit applications, specifically the construction and reclamation plans, must provide an estimate of the amount of acreage to be disturbed, the **location** of the pits at the drill site — with dimensions — and the land application area if applicable. As set forth above, professional engineers are becoming more important in designing well sites and pads as well and are required in all proposed legislation. Further, in all proposed legislation, surface owner interests are taking a more prominent position.

To better address all these new challenges, various interest groups and the WV DEP have presented proposed bills to the Legislature. In all cases, it is recognized that shallow horizontal wells require new rules and regulations that will encourage production while protecting the environment. Surface owners are being heard on these issues as well. In an interesting coalition, surface owners and industry appear to be in agreement that, generally speaking, forced or statutory pooling, not the rule of capture, is the appropriate rule for shallow horizontal wells. The WV DEP has put forth a bill for consideration during this Legislative session that essentially tracks the current statutory pooling and unitization requirements for deep wells, with minor adjustments.

The WV DEP Bill provides for the formation of drilling units and statutory pooling. In order to form a unit or pool interests in the unit, the standard notice and hearing for all interested parties applies. For unitization purposes, any interested owner or operator can file an application to pool. To establish a drilling unit, the applicant must control, by ownership, lease or contract, at least 75% of the net acreage (calculating partial interests on a pro rata, net acreage basis). When pooling two or more interests in a drilling unit, or when there are separately owned interests in all or part of a drilling unit, the operator having the majority

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Interest in the unit may seek a pooling order after notice to the interested parties and a hearing.

The Oil and Gas Commission, a board set by statute, determines the acreage, shape and minimum distance from the outside boundary of the unit, considering all the factors set forth in the deep well pooling statute, in addition to the specific design of the azimuth of the horizontal shallow wells, the location of the drilling pad within the drilling unit, and the number of horizontal shallow wells to be drilled on the pad, and any established or proposed drilling units for the same formation that are adjacent to the proposed unit. In no event shall drilling be initiated on the tract of an unleased owner without the owners written consent. Finally, the operator shall be the person who controls 75% or more of the acreage in the pooled unit. If no one owns more than 75%, the commission will designate the operator.

Under this proposal, each order shall specify the activities that the operator may conduct on the surface of the tracts subject to whether the mineral interest subject to pooling order is leased or unleased. Where unleased, surface disturbance may not be conducted without consent from the owner or by a showing of the operator that there is no other feasible location within the drilling unit to locate the drilling pad or access road or pipeline incidental to the drilling activities. Where the mineral interest is leased, drilling activities may be conducted on the surface of the lease tract and the operator may construct and operate access roads and pipelines incidental to the drilling activities on the surface of all property subject to the order in accordance with the terms of the lease governing surface activity. The operator must provide notice to the owners of the surface estate and pay damages. Leased interest owners have no election rights and, other than the operator having the right to pool the interests, their interests shall be governed by the terms of the lease. Unleased interest owners may elect from one of three options. The WV DEP Bill also provides for the holding in a suspense account of any unlocated Interest owner's share of the proceeds until the owner is located or the property is deemed abandoned and disposed of in accordance with the provisions of the Uniform Unclaimed Property Act.

The WV DEP Bill is the only bill before the Legislature currently that provides for statutory pooling. Given the support of industry and surface owners for this type of provisions, it seems likely that statutory pooling will become an option for horizontal shallow gas wells at some point. In addition to statutory pooling, other issues such as very specific provisions related water use, surface disturbance, and reclamation, have also been put forward.