LEGISLATIVE & REGULATORY UPDATE

By Nikolas Tysiak, Legislative and Regulatory Chairman

Hello MLBC friends, family and colleagues! This time around, you get a DOUBLE dose of statutes, regulations and cases because your friendly, neighborhood Legislative and Regulatory Committee Chair was too busy to get an article finalized for the last issue of the Wildcatter. Luckily for us, there has not been a lot of activity to report on, so hopefully this article will fill in the gap in your life with fascinating legal and legislative developments.

PENNSYLVANIA

In Pennsylvania Environmental Defense Foundation v. Commonwealth (255 A.3d 289 (Pa. 2021)), the Pennsylvania Supreme Court was asked to determine if allocations of bonuses, yearly rentals and interest penalties for late payments under oil and gas leases on state forest and game lands were improperly allocated to the Commonwealth General Fund under the Environmental Rights Amendment ("ERA") to the Pennsylvania Constitution (Art. I, Sec. 27). In a prior decision, the Supreme Court had determined that the ERA created a public trust subject to private trust principles, and that royalty revenue streams generated by the sale of gas extracted from Commonwealth lands represented the sale of trust assets that had to be returned to trust fund principal.

In that prior decision, it was determined that not enough information existed in the record to determine whether the bonuses, rentals and interest penalties were also improperly allocated. The issue regarding the non-royalty payments had been remanded to the Commonwealth Court, which decided these non-royalty revenue streams did not constitute the sale of trust assets and were instead "income" and were not required to be returned to the trust fund principal. The Supreme Court relied on contract principles to determine that the non-royalty payments were not compensation for trust assets (oil and gas in the ground), and therefore did not have to be returned to the trust fund principal in kind. Instead, the court designated the non-royalty payments as income streams. However, the court still found that the allocation of income streams to the general fund based on private trust principles and the language of the documents establishing the duty owed by the Commonwealth as fiduciary. In short, the Supreme Court found that the Pennsylvania constitution holds that the ERA effectively establishes a trust for conservation and environmental purposes for the benefit of all Pennsylvanians, whether currently living or not yet born. As such, all principal and income of the trust must be used for the stated purposes (conservation and maintenance of public natural resources), and cannot be allocated to the Commonwealth general fund, stating "to hold otherwise would permit the Commonwealth to use trust income to advance a non-trust purpose, an outcome we previously rejected." The Supreme Court ordered that the trust income assets (non-royalty payments under the leases) be returned to the trust, accordingly.

On September 14, 2021, the Sierra Club, PennFuture, Clean Air Council, Earthworks and other groups (Petitioners) submitted two parallel rulemaking petitions to Pennsylvania's Department of Environmental Protection (DEP) asking the Environmental Quality Board (EQB) to require full-cost bonding for conventional and unconventional oil and gas wells, for both new and existing wells. The petitions do not address or consider the permit surcharges and other funding mechanisms for plugging wells, including the federal infrastructure bill that is expected to provide millions of dollars to plug abandoned wells.

The Pennsylvania General Assembly addressed and increased bonding in 2012. Under Act 13, well owners/operators are required to file a bond for each well they operate or a blanket bond for multiple wells. Currently, the bond amount for conventional wells is $2,500 per well, with the option to post a $25,000 blanket bond for multiple wells. 72. P.S. §1606-E. For unconventional wells, the current bond amount required varies by the total well bore length and the number of wells, and is limited under the statute to a maximum of $600,000 for more than 150 wells with a total wellbore length of at least 6,000 feet. 58 Pa.C.S. §3225(a)(1)(ii). EQB has statutory authority to adjust these amounts every two years to reflect the projected costs to the Commonwealth of plugging the well.

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Per the EQB Petition Policy, as set forth in the regulations at 25 Pa. Code Chapter 23, DEP has 30 days from receipt of the petitions to determine whether the petitions are complete and if they request an action that can be taken by the EQB that does not conflict with federal law. If the DEP determines the petitions meet the above conditions, the EQB will be informed of the petition for rulemaking and the nature of the request. At the next EQB meeting occurring at least 15 days after the Department's determination, the Petitioners may make a brief oral presentation and DEP will make a recommendation whether the EQB should accept the petition.

OHIO

A public hearing on HB 152, designed to amend Ohio's forced pooling statutes and accompanying regulations, was held on June In Estella Roberts v. Roy C. Roberts, 2021-Ohio-3857 (6th Dist. Ct. App. 2021), the Court of Appeals was asked to adjudicate a dispute arising from an 1895 oil and gas lease in Sandusky County, Ohio. The lease had been in continuous operation until approximately 1979, after which production ceased until Roy C. Roberts re-commenced operations and sent royalty checks to Estella Roberts, which were accepted and cashed. In 2015, Estella asserted that the lease had expired and was operating the wells in question without a valid lease, requesting the negotiation of a new lease. At trial, it was determined that the lessee held a fee interest (fee simple determinable) the parties presented arguments on whether the interest created in 1895 constituted a lease that had expired due to lack of production, or whether the interest was saved by the Dormant Mineral Act. The trial court declined to decide on the nature of interest (fee vs. lease) but held that the Dormant Mineral Act applied and the interest held by Roy was saved by actual production. The Court of Appeals agreed with the trial court's analysis. It appears that Estella also failed to properly argue the Ohio's lease forfeiture law, ORC 5301.332, applied, as the Court indicated that the record contained insufficient allegations or pleadings that would allow for a decision on that basis. The Court upheld the trial court decision that Dormant Mineral Act preserved the Roy Roberts interest, but overturned on issues regarding payment of attorneys' fees by Estella.

In 4 Quarters, LLC v. Hunter, 2021-Ohio-3586 (7th Dist. Ct. App. 2021), the Court of Appeals heard (yet another) claim relating to the Ohio Marketable Title Act. In 1922, Hunter conveyed a tract of 78.9 acres in Belmont County to Carpenter, effectively reserving a ½ non-participating royalty interest. In August of 2019, 4 Quarters obtained the surface to the 78.9 acres and immediately filed a complaint under the MTA to extinguish the Hunter reservation. In October of 2019, Ruble, purported to be the sole successor to Hunter, was informed that he may be the sole successor to Hunter. In March of 2020, Ruble received notice from an oil and gas operator selected by 4 Quarters that his interest had been granted to 4 Quarters by default judgment and that royalties had been disbursed to 4 Quarters. In July 2020, Ruble brought an action to vacate the prior judgment in favor of 4 Quarters, which was denied. At issue on appeal was the reasonableness of 4 Quarters attempts to locate heirs or successors of Hunter for notice purposes as required by the MTA. The Court found that the search for Hunter and successors was reasonable under existing Ohio law and guidelines. Although Ruble claims there was ample evidence of his succession from Hunter in Marshall County, WV (adjacent to Belmont County) the Court found no evidence in the Belmont County records that Hunter, or any of his heirs, successors or assigns, may be found in a different locality. Consequently, a search limited to Belmont County was reasonable. Ruble's contentions were found without merit, and the trial court decision affirmed.

A similar fact pattern arose, also in Belmont County, in Mammone v. Reynolds, 2021-Ohio-3248 (7th Dist. Ct. App. 2021). In 2013, surface owners sought to regain title to severed oil and gas under their land but were unable to locate current owners of the interest (also known as the "Huddleston heirs"). Notice of the proceedings was served on the Huddleston Heirs by publication. Because the Huddleston Heirs never responded to the lawsuit, the trial court granted default judgment in September 2013 to the surface owners. In 2020, the Huddleston Heirs sought to have the 2013 judgment vacated, which was overruled by the trial court. On appeal by the Huddleston Heirs, the Court of Appeals agreed with the trial court and affirmed its judgment.

WEST VIRGINA

The West Virginia Supreme Court of Appeals has accepted four questions certified to it by The United States District Court for the Northern District of West Virginia in Charles Kellam, et al. v. SWN Production Company, LLC, et al., No. 5:20-CV-85. The Court will hear oral argument during the January 2022 term. The Court will address four questions: (1) Is Estate of Tawney v. Columbia Natural Resources, LLC, 219 W.Va. 266, 633 S.E.2d 22 (2006) (Tawney) still good law in West Virginia; (2) What is meant by the "method of calculating" the amount of post-production costs to be deducted; (3) Is a simple listing of the types of costs which may be deducted sufficient to satisfy Tawney; and (4) If post-production costs are to be deducted, are they limited to direct costs or may indirect costs be deducted as well?

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At the time of the District Court's certification in Kellam, defendants' Motion for Judgment on the Pleadings asserting that the Kellams' lease complied with Tawney and that the District Court was bound by the decision in Young v. Equinor USA Onshore Properties, Inc., 982 F.3d 201 (4th Cir. 2020) was pending. In Young, the 4th Circuit Court of Appeals reversed Judge Bailey and held the lease clearly and unambiguously allowed the deduction of post-production expenses and noted that "Tawney doesn't demand that an oil and gas lease set out an Einsteinian proof for calculating post-production costs. By its plain language, the case merely requires that an oil and gas lease that expressly allocates some post-production costs to the lessor identify which costs and how much of those costs will be deducted from the lessor's royalties." Young, 982 F.3d at 208. Moreover, the 4th Circuit noted recent criticism of Tawney by the West Virginia Supreme Court of Appeals. See Leggett v. EQT Prod. Co., 239 W. Va. 264, 800 S.E.2d 850 (2017).

Until next time,

MLBC Legislative and Regulatory Committee
Nik Tysiak, Chair

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