OG Energy Education Series

Appalachia Title Update

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Overview

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West Virginia Cotenancy Statute: A Precursor to Unitization

- Effective as of July 1, 2018
- Requirements for cotenancy:
  - The oil or natural gas mineral property has seven or more royalty owners;
  - Operator engages in reasonable efforts to negotiate with all royalty owners in the oil or natural gas mineral property; and
  - At least three fourths of the royalty owners consent to the lawful use or development of the oil or natural gas mineral property.
- If the above criteria are met, then the operator's use or development of the oil or natural gas mineral property is permissible, is not waste, and is not trespass. W. Va. Code § 37B-1-4(a).

West Virginia Cotenancy Statute: A Precursor to Unitization

- Duty owed to non-consenting cotenants:
  - A non-consenting cotenant is entitled to receive (i) a pro rata share of production royalty; or (ii) a pro rata share of the revenue if the non-consenting cotenant elects to participate in the development. W. Va. Code § 37B-1-4(b)(1).
  - The non-consenting cotenant must select an option within forty-five (45) days of receiving the operator's final lease offer. If the non-consenting cotenant fails to select an option, they will receive a pro rata share of production royalty. W. Va. Code § 37B-1-4(b)(2).
- Duty owed to unknown or unlocatable interest owners:
  - Unknown or unlocatable interest owners will receive a pro rata share of production royalty. The operator must remit the amount reserved to the State Treasurer for seven (7) years. W. Va. Code § 37B-1-4(d), (g).

West Virginia Cotenancy Statute: A Precursor to Unitization (Cont.)

- Limitations of Cotenancy Statute:
  - Operators shall only develop the specifically targeted stratigraphic formation and 100 feet above and below said formation; nonconsenting cotenants and unknown or unlocatable interest owners will retain all rights to all other formations unless or until reasonable efforts are made to renegotiate under this section for each additional formation. W. Va. Code § 37B-1-4(e).

Requirements to Apply for Unitization in West Virginia

- Effective as of June 7, 2022.
- There are various criteria an applicant must meet to file a unitization application. If these criteria are met, the commission "shall authorize unitization of tracts." So, unitization is freely granted if the prerequisites are met. S. B. 694, 2022 Leg., 2nd Sess. (W. Va. 2022).
- An applicant must (i) control the horizontal well; **AND** (ii) comply with all application requirements. S. B. 694, 2022 Leg., 2nd Sess. (W. Va. 2022).

Requirement #1: Applicant Must Control the Horizontal Well Unit Under S. B. 694

Under S.B. 694, an applicant must satisfy (A), (B), AND (C) to control the horizontal well unit.

(A)

- "With respect to the royalty interest, for shallow horizontal wells and deep horizontal wells. . . the right, consent or agreement to pool or unitize the acreage to be included in the horizontal well unit from executory interest royalty owners of 75 percent or more of the net acreage in the target formation proposed to be included in the horizontal well unit. . ." S. B. 694, 2022 Leg., 2nd Sess. (W. Va. 2022).

Requirement #1: Applicant Must Control the Horizontal Well Unit Under S. B. 694 (Cont.)

(B)

- "With respect to the operator interest:
  - (i) For shallow horizontal wells. . . the right, consent or agreement to pool or unitize as to 55 percent or more of the net acreage in the target formation proposed to be included in the horizontal well unit owned, leased, or operated by operators and the applicant, collectively, by ownership, lease, farmout, assignment, contract or other agreement. . .; or
  - (ii) For deep horizontal wells. . . the right, consent or agreement to develop the acreage to be included in the horizontal well unit from executory interest royalty owners of 55 percent or more of the net acreage in the target formation proposed to be included in the horizontal well unit. . ." S. B. 694, 2022 Leg., 2nd Sess. (W. Va. 2022).

Requirement #1: Applicant Must Control the Horizontal Well Unit Under S. B. 694 (Cont.)

(C)

- "(i) Made good-faith offers to consent or agree to pool or unitize, and has negotiated in good faith with, all known and locatable royalty owners having executory interests in the oil and gas in the target formation within the acreage to be included in the proposed horizontal well unit who have not previously consented or agreed to the pooling or unitization of the interests and whose interests are not subject to development under Section 37B-1-1, et seq. of this code; and

- (ii) Made good-faith offers to participate or consent or agree to the proposed horizontal well unit, and has negotiated in good faith with, all known and locatable operators who have not previously agreed to participate or consent or agree to pool or unitize the acreage to be included in a proposed horizontal well unit." S. B. 694, 2022 Leg., 2nd Sess. (W. Va. 2022).

Requirement #2: Application Requirements

- Under S.B. 694, an applicant must include the following in their unitization application:
- A description of the proposed horizontal well unit and identification of the target formation or formations;
- A statement of the nature of the operations contemplated;
- A plat that depicts the boundaries and acreage of the proposed horizontal well unit, the tracts in the horizontal well unit, the surface tax map and parcel numbers of the surface tracts above the tracts to be included in the horizontal well unit in accordance with county assessor's records, and the district(s) and county or counties where the proposed horizontal well unit is located;
- A listing of all oil and gas tracts, or portions thereof, within the proposed horizontal well unit, the size of each tract, and the extent to which each tract is leased;

Requirement #2: Application Requirements (Cont.)

- The names and last known addresses of royalty owners of the target formation of each tract within the proposed horizontal well unit, specifying:
  - Which, if any, of them are unknown and unlocatable;
  - Which of them hold executive rights; and
  - With respect to owners of an executory interest, whether they have consented to pooling or unitization of the acreage proposed to be included in the horizontal well unit;
- The names and last known addresses of operators of proposed horizontal well unit target formation acreage whose interest is of record in the county where the property is located, specifying:
  - Which, if any, of them are unknown and unlocatable; and
  - Which, if any of them, are bonded operators, and if a bonded operator, whether he or she has consented to pooling or unitization as to the acreage proposed to be included in the horizontal well unit;

Requirement #2: Application Requirements (Cont.)

- Information regarding the applicant's actions to identify and locate unknown and unlocatable interest owners of target formation acreage to be included in the horizontal well unit;
- The percentage of the net acreage in the proposed horizontal well unit owned by executory interest target formation royalty owners who have consented to pooling or unitization;
- The percentage of the net acreage in the proposed horizontal well unit held by bonded operators and the applicant, collectively, as to which consent or agreement to pool or unitize has been granted;
- A percentage allocation to the separately owned tracts, or portions thereof, in the proposed horizontal well unit of the oil and gas that will be produced from the horizontal well unit as determined by the proportion that each tract's net acreage within the horizontal well unit bears to the total net acreage in the horizontal well unit;

Requirement #2: Application Requirements (Cont.)

- A certification that the applicant meets the requirements of subsection (c) of this section with respect to the proposed horizontal well unit, a list of the instruments granting the control and a certification that the applicant has mailed a copy of the application to all known and locatable interested parties by United States certified mail, return receipt requested, to their last known address and to the most current address filed with the West Virginia Department of Environmental Protection, Office of Oil and Gas, if any;

- A statement whether the applicant has submitted, either previously or contemporaneously with the application filed pursuant to this section, an application for a well work permit with the Department of Environmental Protection for one or more horizontal wells to be completed within the boundaries of the proposed horizontal well unit; and

- A proposed joint operating agreement that will govern the contractual relationship between the applicant and any unleased royalty owners following an election by the executive interest owners to participate in the drilling in the horizontal well unit on a carried basis under Section 22C-9-7a(f)(9) of this code. S. B. 694, 2022 Leg., 2nd Sess. (W. Va. 2022).

Brief History of the MTA

- Effective September 29, 1961.
- Purpose of the MTA is to simplify and facilitate land title transactions by allowing a title examiner to search the record for title defects for only 40 years back in time.
- In 1961, the MTA did not bar or extinguish any right, title, estate, or interest in and to minerals.
- In 1973, the Ohio legislature amended the mineral interest exception so that only coal was excepted from operation of the MTA.

The MTA - Ohio Rev. Code § 5301.48

- Any person who has an unbroken chain of title of record to any interest in land for forty years or more has a marketable record title, subject to certain limitations set out in Ohio Rev. Code § 5301.49.
- The chain of title is unbroken if the official public records disclose a conveyance or other title transaction of record not less than forty years prior to the time marketability is being determined, so long as the conveyance or title transaction purports to create an interest in either:
  - The person claiming the interest; or
  - Some other person through whom the person claiming the interest can claim title; provided that nothing appears in the records divesting the claimant of the interest.

The MTA - Ohio Rev. Code § 5301.49

- Under Ohio Rev. Code § 5301.49, record marketable title is subject to:
- (A) All interests and defects which are inherent in the muniments for the chain of record title – however, a general reference in such muniments to easements, use restrictions, or other interests created prior to the root of title shall not preserve them, unless specific identification is made therein of a recorded title transaction which creates such easement, use restriction, or other interest;
- (B) All interests preserved by the filing of proper notice or by possession by the same owner continuously for forty years or more, in accordance with Ohio Rev. Code § 5301.51;

The MTA - Ohio Rev. Code § 5301.49 (Cont.)

- (C) The rights of any person arising from a period of adverse possession, which was in whole or in part after the effective date of the root of title;
- (D) Any interest arising out of a title transaction recorded after the effective date of the root of title; provided that such recording shall not revive or give validity to any interest extinguished prior to the time of the recording by the operation of Ohio Rev. Code § 5301.50;
- (E) The exceptions stated in Ohio Rev. Code § 5301.53.

The MTA - Ohio Rev. Code § 5301.50

- Subject to the limitations in Ohio Rev. Code § 5301.49, if an owner has record marketable title, then that title shall be taken by any person dealing with the land free and clear of all interests and claims that depends upon any act, transaction, event, or omission prior to the effective date of the root of title for its existence.
- All such interests and claims prior to the root of title are null and void.

Lucas v. Whyte (7th District Court of Appeals of Ohio, 2021)

- **Facts:** Surface owner brought a quiet title action concerning ½ of the oil and gas rights, claiming the interest had been both extinguished by the MTA and abandoned by the DMA.
- **Issue:** Will the MTA extinguish, or the DMA abandon, the severed interest?
- **Holding I:** There were no "title transactions" under Ohio Rev. Code § 5301.49(D); thus, the MTA extinguished the severed interest. Although an ancillary estate will preserve under Ohio Rev. Code § 5301.49(D), it must be filed in the county where the property is located.
- **Holding II:** Since the Court found that the severed interest had already been extinguished under the MTA, it did not deliberate as to the DMA.

Erickson v. Morrison (Supreme Court of Ohio, 2021)

- **Facts:** In 1926, landowners reserved the mineral rights in a deed with the following language: "[e]xcepting and reserving therefrom all coal, gas, and oil with the right of said first parties, their heirs and assigns, at any time to drill and operate for oil and gas and to mine all coal."
- **Issue:** Does a reference to a reservation in the root of title need to include the name of the person holding the interest in order to be specific under Ohio Rev. Code § 5301.49(A)?
- **Holding:** Although Blackstone held that a reference that identified both the nature of the interest and the name of the interest owner was specific, the Court clarified that its holding should not be read as requiring a reference to include the name of the interest owner in order to prevent extinguishment under the MTA.

Compare O'Kelley v. Rothenbhuler (7th District Court of Appeals of Ohio, 2021)

- **Facts:** Appellants asked the Court to reconsider their decision based on the Blackstone specificity requirements discussed in Erickson. The original severance deed excepted and reserved "[a]ll oil, gas and minerals (including coal) of whatsoever kinds."
- **Issue:** Is the reference "the oil and gas minerals including coal" in the root of title specific under Ohio Rev. Code § 5301.49(A)?
- **Holding:** The Court found the reference lacking because it neither specifically described the interest nor did it identify to whom it was granted/reserved. Additionally, compared to the references in Erickson, which were (almost) verbatim quotes of the original severance language, the reference here was insufficient: "[s]imply stated, the reference lacks any 'narrow precise considerations,' 'limited details,' or 'particulars' as described in Blackstone."

Pernik v. Dallas (7th District Court of Appeals of Ohio, 2021)

- **Facts:** In a 1925 deed, Jasper Dallas reserved the oil and gas rights to the property. In 2018, George Pernik, et al., as surface owners, filed a complaint to quiet title to the oil and gas rights. Joanne Dallas, one of Jasper's heirs, argued that the surface owners' leasing of the oil and gas within the 40-year lookback period preserved her interest under the MTA.
- **Issue I:** Can an oil and gas lease by the surface owner within the 40-year lookback period preserve the severed interest under the MTA?
- **Issue II:** Is the 1962 deed a "proper" root of title?
- **Analysis I:** Where the severed interest owner enters into a lease within the 40 years immediately following the root of title, it will operate to prevent extinguishment under the MTA. Alternatively, where the surface owner enters into a lease within the 40 years immediately following the root of title, it will not operate to prevent extinguishment under the MTA.
- **Analysis II:** The 1962 deed was a proper root of title, however, it did not specifically reference the severed interest (Blackstone test).

Peppertree Farms, L.L.C. v. Thonen (Supreme Court of Ohio, 2022)

- **Facts:** Peppertree Farms, the surface owner, brought an action claiming that severed oil and gas **royalty** interests created in deeds in 1916 and 1921 did not include words of inheritance and thus terminated upon the death of the Grantor in the deeds. Peppertree also claimed that the MTA extinguished the severed royalty interests.
- Both deeds were recorded before Ohio abrogated the common law rule in 1925 that grants had to contain words of inheritance (e.g., "heirs and assigns").
- The Court applied the law in effect at that time (prior to 1925).

Peppertree Farms, L.L.C. v. Thonen (Supreme Court of Ohio, 2022), (Cont.)

- **Holding:** The Court made a distinction between accrued versus unaccrued royalties. The Court pointed out that "there is a recognized difference between royalties that have accrued, which are personal property, and the right to unaccrued royalties, which is real property." Additionally, "[t]he right to receive royalty in the future is one of the separately alienable incidents of ownership of the full mineral interest." Accordingly, unaccrued royalties are the retention of an interest that already exists rather than creation of a new interest.

- **Side Note:** In Peppertree II, the Court also addressed whether a handwritten, recorded will that neither expressly devised the testator's interest in oil and gas nor contained a residuary clause was a title transaction under the MTA. The Court held that it was not a title transaction.

MTA Analysis for Severed Oil and Gas Interests

- Identify the proper root of title.
- Is the oil and gas interest specifically referenced in the root of title?
- Is the oil and gas interest specifically referenced or identified in a muniment of the chain of title within forty years of the recording date of the root of title?
- Is the oil and gas interest protected by a notice to preserve?
- Is the oil and gas interest protected by one of the other limitations to record marketable title in Ohio Rev. Code § 5301.49?

The 2006 DMA – Ohio Rev. Code § 5301.56

- Applies to all claims after June 30, 2006.
- Process for reuniting severed oil and gas interests with surface owners; requires filing an affidavit of abandonment and proper notice.
- Abandonment procedure under the 2006 DMA:
  - Surface owner must confirm no exemptions or savings events.
  - Surface owner must serve notice of abandonment.
  - Surface owner must record affidavit of abandonment.
  - Surface owner must record notice of failure to file.

DMA Proper Notice – Holder of Interest is Known

- Proper notice can be achieved by sending notice of the surface owner's intent to declare the mineral interest abandoned, via certified mail, to each holder or each holder's successors or assignees, at the last known address of each with a return receipt requested. Ohio Rev. Code Ann. § 5301.56(E)(1).
- Under Ohio Rev. Code Ann. § 5301.56(F)(1)-(4), notice must contain:
  - Name of each holder and the holder's successors and assignees, as applicable;
  - Description of the mineral interest to be abandoned;
  - Statement attesting that nothing regarding a title transaction involving the mineral interest or that actual production of the mineral interests have occurred within the twenty (20) years preceding the date on which notice is served or published; and
  - Statement of the intent of the owner to file an affidavit of abandonment in the office of the county recorder.

DMA Proper Notice – Holder of Interest is Unknown

- If the holder of the interest is unknown or cannot be located, the owner shall publish notice of the owner's intent to declare the mineral interest abandoned at least once in a newspaper of general circulation in each county in which the subject land is located. Ohio Rev. Code Ann. § 5301.56(E)(1).
- Notice by publication is a last resort. A sincere, diligent effort by the researcher is required before service by publication is appropriate. Fonzi v. Miller, 7th Dist. Monroe No. 19 MO 0011, 2020-Ohio-3739.

Beckett v. Rosza
(7th District Court of Appeals of Ohio, 2021)

- **Facts:** Roy Beckett left 110.5 acres in Jefferson County to his children, Grace and Leroy II, by his will, which was probated in Jefferson County. The probate records reflected that Grace lived in Urbana, Illinois while Leroy II lived in Manchester, Connecticut. Thereafter, Grace and Leroy II conveyed the property in separate deeds, reserving the oil and gas. Grace's deed was notarized in Champaign County, Illinois (where Urbana is located).

- Rosza, the surface owner, sought to abandon the severed interest under the DMA. Rosza's attorney conducted searches of the public records in Jefferson County concerning any conveyance or preservation of the severed interest by the Beckett heirs. The attorney found no conveyances or preserving events, nor any ancillary estates for the Beckett heirs in Jefferson County. As a result, the attorney made no attempt to serve the holders through certified mail. The attorney published an intent to abandon in Jefferson County.

Beckett v. Rosza (7th District Court of Appeals of Ohio, 2021), (Cont.)

- **Issue:** Did Rosza use reasonable diligence in locating the Beckett heirs?
- **Holding:** Reasonable diligence is decided on a case-by-case basis. If independent knowledge or other information found leads the researcher to go out of county or state, reasonable diligence requires that lead to be followed. Here, Rosza's search was unreasonable as there was evidence in the Jefferson County probate records that showed Grace lived in Champaign County, Illinois and Leroy II lived in Manchester, Connecticut.

Production in "Paying Quantities" – General Rules

- A paying quantity is "quantity of oil or gas sufficient to yield a profit, even small, to the lessee over operating expenses even though the drilling costs, or equipping costs, are not received and even though the undertaking as a whole may result in a loss." *Blausey v. Stein*, 61 Ohio St. 264, 265, 400 N.E.2d 408, 410 (Ohio 1980).
- Production in "paying quantities" is that quantity which will bring a reasonable financial return in excess of the cost for production, regardless of any particular amount of profit derivable from the operation as well. *Litton v. Geisler*, 80 Ohio App. 491, 495, 76 N.E.2d 741, 744 (Ohio Ct. App. 4th 1975).
- Burden is on lessor to show that lessee has forfeited the lease because of failure to produce gas in paying quantities. Unless there was bad faith or selfish personal motive, the lessee's experience, interest, and judgment under the surrounding circumstances are controlling. *Id.* at 496.

Production in "Paying Quantities" – Temporary Cessation of Production

- A mere temporary cessation in the production of a gas or oil well will not terminate the lease under a habendum clause where the owner of a lease exercises reasonable diligence and good faith in attempting to resume production of the well. *RHDK Oil & Gas LLC v. Dye*, 7th Dist. Harrison No. 14 HA 0019, 2016-Ohio-4654, ¶ 20; citing *Wagner v. Smith*, 8 Ohio App.3d 90, 92, 8 Ohio B. 124, 456 N.E.2d 523 (5th Dist. 1982).

- Cessation of production is temporary when the cessation is for a short period of time. There is no case in Ohio where a court deemed a lease forfeited for less than two years of nonproduction. *Dye*, at ¶ 22.

Browne v. Artex Oil Co. (5th District Court of Appeals of Ohio, 2021)

- **Facts:** Browne owned 86 acres in Guernsey County, which was subject to a 1975 oil and gas lease. The lease's habendum clause had a secondary term for as "long thereafter as oil or gas, or either of them, is produced by lessee from said land." The Mercer No. 1 well was drilled on the property, which Artex operated from 1999 to 2014. Artex's records showed the well generated gross revenue of more than $100,000. Browne filed an action claiming that the lease had expired for failure to produce in paying quantities prior to 1999.

- **Issue:** Applying a 21-year statute of limitation, did the Mercer No. 1 well produce in paying quantities (PPQ) between 1993 and 1999?

- **Holding:** The Mercer No. 1 Well was PPQ during the relevant period. PPQ requires first-hand evidence and not just what the ODNR's well completions report shows. The burden of proof rests with the landowner.

Ullman v. Whitacre (7th District Court of Appeals of Ohio, 2021)

- **Facts:** Whitacre paid a flat monthly payment to one of its affiliates to manage and maintain wells. Whitacre's business records revealed only the flat monthly payment for each of its 350 wells. The flat monthly payment for each of Whitacre's 350 wells appeared to exceed its monthly revenue. As a result, the Ullmans believed that the well on their property was not PPQ. However, Whitacre argued that the flat monthly payment was spread across all the wells in its portfolio and that the "direct operating expenses" did not exceed the income gained from the Ullman well.

- **Issue:** Was the Ullman well PPQ?

- **Holding:** Only direct costs of production matter in a PPQ analysis. PPQ analysis is not limited to business records; testimony – and whatever else the Court deems relevant – all play a factor. The landowner also bears the burden of proof.

SLT Holdings, LLC v. Mitch-Well Energy Inc. (Supreme Court of Pennsylvania, 2021)

- **Facts:** Two parcels of land, consisting of 1,500 acres, were subject to identical oil and gas leases. The original Lessee transferred its interest to Mitch-Well Energy, which drilled one well on each of the parcels. These wells were PPQ until 1996. Afterwards, there was no production from these wells, nor any payments under the leases, for 16 years. Lessors brought suit seeking a judgment that the leases were abandoned.
- **Issue:** Were the leases abandoned for lack of PPQ?
- **Holding:** No. The Court here found that lower courts skipped an important step, namely the contractual remedies provided in the leases. Particularly, the Court focused on Paragraph 12 of the lease, which centers on curing a default. Since there was a built-in contractual remedy in the leases, the Court found that this should have been addressed before moving to the issue of abandonment. Ultimately, the Court found that the remedy provided by Paragraph 12 was the lessors' sole remedy.

Walters v. McIlvee (Superior Court of Pennsylvania, 2021)

- **Facts:** The Walters sold their land, being 220 acres, to the McIlvees in 2003. In the unrecorded agreement between the parties, the Walters excepted and reserved all oil, gas and mineral rights. However, the recorded deed did not include any exception or reservation of the oil, gas and mineral rights due to a scrivener's error.
- The McIlvees later conveyed 130 of the 220 acres to the Howells. In the unrecorded agreement between the parties, there was a handwritten note which stated that "if all mineral rights are excluded, buyer has the option to declare the contract null and void or choose to purchase as is." There was also a second handwritten note that stated "no mineral rights included in [the] purchase…." The recorded deed did not mention the oil and gas rights, but also did not except or reserve the oil, gas and mineral rights. As a result, the Howells assumed that the oil and gas rights, as opposed to the mineral rights, did transfer to them.
- The McIlvees entered into an oil and gas lease with Chesapeake.
- The Walters filed suit seeking reformation of the 2003 deed.

Walters v. McIlvee (Superior Court of Pennsylvania, 2021) (Cont.)

- **Issue:** Can oil and gas rights be severed by an unrecorded instrument in your chain of title?
- **Holding:** The Court found that the Howells were not bona fide purchasers. Although the handwritten note only discussed mineral rights, which typically does not include oil and gas rights in Pennsylvania, the Court exclusively relied upon the fact that oil and gas development was prevalent in the county where the land is located and that there was little or no coal development.

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I focus my practice on **oil and gas title opinions, transactions, and regulatory matters.**

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