

PENN ROAR, 359 Route 106 Greenfield Twp, PA 18407
pennroar@yahoo.com 570-267-4083 for advertising

Corbett's MSAC Announces Recommendations Affecting PA Royalty Owners

By: T. Walczak

The July 22nd submission of the final report of recommendations by Governor Corbett's Marcellus Shale Advisory Commission (MSAC) marked a bold advance in the way Pennsylvania's regulatory agencies address the natural gas drilling industry. The unanimously-adopted report contains 96 policy recommendations that include tougher regulations for drilling, doubling fines for violations, creating jobs in related industries and promoting the use of natural gas vehicles.

Many of the recommendations regarding drilling regulations represent a common sense look at revamping rules which were last overhauled in the 1984 Oil and Gas Act. Recommended changes like: expanding an operator's presumed liability for impaired water quality from within 1,000 feet of a well to within 2,500 feet of a well; from 6 months to 12 months of completion or alteration of the well; with the presumed liability also being applied to well stimulation; and greater bonding requirements; represent an admission that the larger, deeper wells need more attention than Pennsylvania's traditional production.

While all of the recommendations will have a tremendous impact on the future of exploration in the Marcellus, two suggested measures were previously opposed by the Corbett administration: a new tax and compulsory integration.

The MSAC's findings did support the need for the imposition of an impact fee to offset the added costs of the exploration borne by the local municipalities and the need to adopt "compulsory integration," or sometimes called "forced pooling," or "Conservation Law" to the Marcellus.

While the July issue of Penn ROAR tackled the details of the Impact Fee, as currently proposed, we are dedicating much of this issue to explaining compulsory integration.

The MSAC sites their support of expanding the "conservation law" in section 9.4.26, on page 118 of the report, suggesting Pennsylvania's statutes should be modernized in a timely manner to:

- Include the Marcellus Shale and other deep unconventional geologic formations currently excluded from existing conservation statutes;
- Conform with the best practices for shale gas development in the great majority of states with said production;
- Ensure the protection of property rights for both surface and mineral rights owners;
- Account for the opportunities afforded by advances in technology of natural gas extraction practices, including horizontal and directional drilling and well stimulation;
- Ensure the minimization of surface impact through the proper placement and spacing of well pads;
- Prevent the waste or stranding of natural gas so as to maximize job and revenue-generating opportunities for the Commonwealth and its citizens.

Take the time to read the full commission report by clicking here: http://files.dep.state.pa.us/PublicParticipation/MarcellusShaleAdvisoryCommission/MarcellusShaleAdvisoryPortalFiles/MSAC_Final_Report.pdf

Inside This Issue

Page 2...
Introducing
Compulsory
Integration

Page 4...
Why is it called
Conservation Law?

Page 5...
Legislative
Considerations for
Forced Pooling

Page 7 ...
Forced Pooling,
Compulsory
Integration, or
Eminent Domain?

Page 9...
Additional
Protections Give
Royalty Owners
Equal Footing in
Forced Pooling

Page 11...
Subsurface Trespass

Page 14...
Act 35 of 2011
Amends Clean and
Green Law Again

www.naro-us.org



Introducing Compulsory Integration

By: Lester Greevy & John Shoemaker, Greevy & Associates

“Forced pooling”, sometimes called “compulsory integration” has become a hot-button—and emotionally charged—issue among Pennsylvania’s royalty owners. In the state, the only mechanism for forced pooling is the Oil and Gas Conservation Law, 58 Pa.C.S.A. §§ 401 et seq. (the “Law”). But despite the Law, forced pooling is practically non-existent in Pennsylvania. This issue of PENN ROAR will summarize the Law, explore the advantages and disadvantages of a broadened forced-pooling statute, and present the characteristics of such a broadened statute which would be advantageous to royalty owners.

Summary of the Oil and Gas Conservation Law

The purpose of the Law is to protect the *correlative rights* of owners of oil and gas interests. Correlative rights are the rights of such persons “to have a fair and equitable opportunity to obtain and produce his fair and equitable share of the oil and gas” underlying a particular spacing unit (think production unit), “without being required to drill unnecessary wells or incur other unnecessary expense...”. 58 Pa.C.S.A. § 402(2).

The Law contemplates production from “pool[s]” or underground reservoirs—conventional plays. The Marcellus Shale contains “tight gas”, trapped in the shale and not accumulated in vast, hollow, underground reservoirs—it is an *unconventional* play.

The Law applies only to wells which do penetrate the Onondaga horizon—or where the Onondaga is not present, wells which exceed a depth of 3800 feet beneath the surface. Since the Marcellus Shale lies above the Onondaga horizon, Marcellus wells are exempt from the Law. Hence the severely limited applicability of the Law.

Any operator or unleased royalty owner having an interest in the proposed spacing unit may initiate proceedings to force pool tracts within that unit. Thus, operators may force pool other operators, and not just royalty owners. Similarly, an operator with an interest within a spacing unit to which that operator has not been voluntarily pooled may force its hand as against the dominant operator.

Continued to page 3

VALUABLE OFFER TO ROYALTY OWNERS

The need to accurately value Marcellus gas royalty interests is great, but the determination of value and the projection of future income from Marcellus gas wells in Pennsylvania has been and remains very imprecise. This is because there is a lack of firsthand month-by-month accurate production data. The result is that many royalty owners are having difficulty making decisions based on the limited information available.

In order to develop better data on which better decisions can be made, Greevy & Associates Law Office, in conjunction with Richard J. Miller & Associates Appraisals, Inc., makes the following offer to royalty owners with six (6) months or more production:

If a royalty owner agrees to send Greevy and Associates copies of their monthly royalty statements covering the first three (3) years of production (and longer if they are so inclined) Richard J. Miller & Associates will provide a projection of future production and revenue for each well or unit in which they have an interest (as of January 1, and July 1, of each year) up to three (3) years (or longer). There will be no charge for these projections as they will not be styled as appraisals. The projections will be helpful for financial planning purposes and will have the added benefit of making any future appraisals of their oil and gas interest more accurate.

Additionally, Greevy & Associates will, for no charge, offer a legal opinion as to whether or not the future revenue projection would indicate the need for federal estate tax planning on the part of the royalty owner.

Individual client information concerning production and revenue projections will be held entirely confidential.

To participate in this offer, please contact:

GREEVY & ASSOCIATES

PO BOX 328

Montoursville, PA 17754

(570) 435-2233 • (570) 435-2238 fax

Email: info@greevy.com

The Law provides for notice and a hearing before a tract becomes force pooled to any spacing unit. The purpose of the hearing is to attempt to reach agreement among consenting and non-consenting operators and royalty owners as to the terms and conditions of the operation of the proposed spacing unit, including which party will operate the unit. If no agreement is reached, a state bureaucracy makes a determination.

If a non-consenting lessee (gas company) becomes force pooled, the operator of the unit is entitled to seven-eighths of that non-consenting lessee's share of production from the unit until its share of the cost of drilling, equipping, and operating the well(s) is recouped. After the non-consenting lessee's share has been recouped, it is entitled to 100% of its proportional share of production. Of course, nothing in the Law relieves any lessee of its

duty to pay the agreed-upon royalties to its royalty owners.

If a non-consenting lessor (royalty owner) becomes force pooled, it is entitled to seven-eighths of its share of production from the unit until its share of the cost of drilling, equipping, and operating the well(s) is recouped, whereupon it is entitled to 100% of its proportional share of production.

The Oil and Gas Division of the Department of Mines and Mineral Industries of the Commonwealth of Pennsylvania administers the Law.●



the CLARK
Law Firm, PC
Protecting Pennsylvania's Landowners

Call us before you sign ANY Marcellus Shale Agreement!



Call: (570) 307-0702

Gas Leases
Pipeline and Water Line Agreements
Ponds and Compressors
ESTATE PLANNING & ROYALTY MANAGEMENT



TCLF



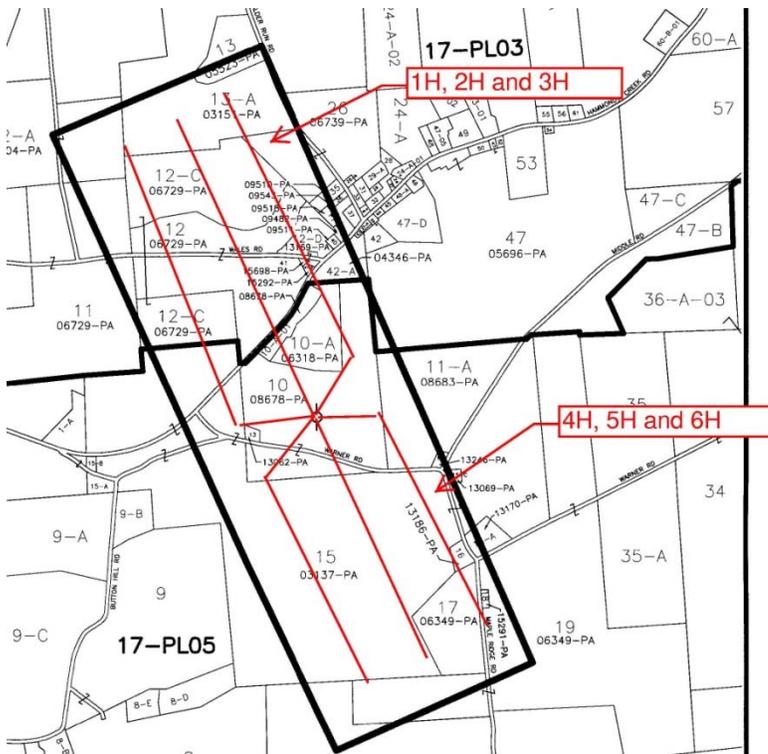
Attorney Clark's weekly radio show
"All Things Marcellus" archived
on our websites!



To access our site, use your smartphone to scan this QR code

Q: Why is it Called Conservation Law?

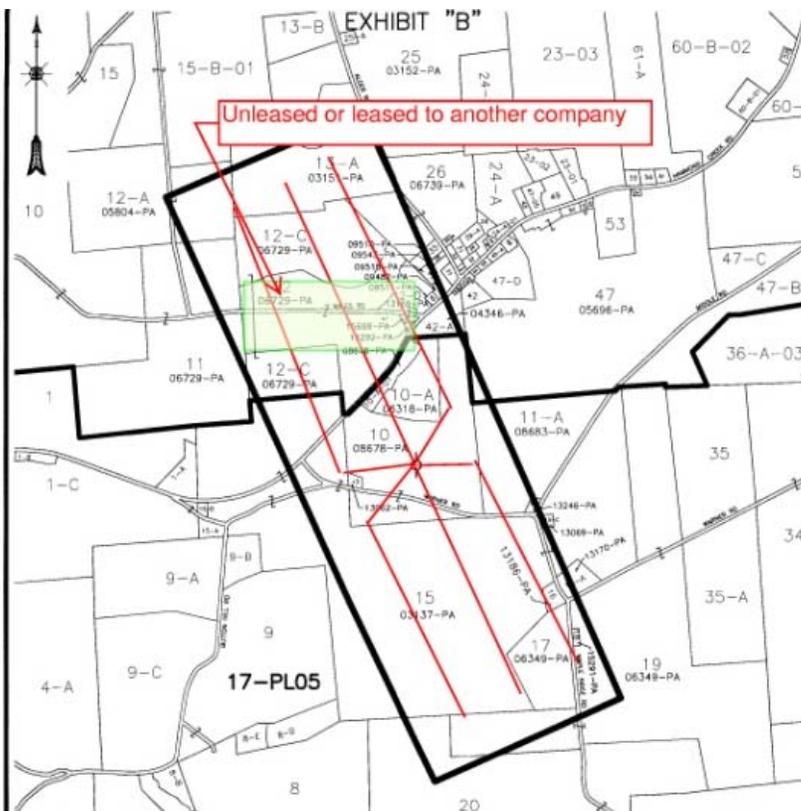
Jacqueline Root, NARO-PA Chapter President, R&R Energy Consulting



Scenario #1:

Company A drills 6 horizontal wells and all Lessors receive royalties based on their fractional interest.

Scenario #2



Current Law	Compulsory Integration
3 horizontal legs deleted and no trespass is allowed	All 6 horizontals are drilled
40 un-leased and 110 leased acres excluded from the unit and potential for future development is limited	Well bore may travel under the 40 acres but no surface use is allowed
150 mineral acres receive no royalty income	Royalties paid to un-leased owner based on law
If the 40 acres is leased to Company B: Unless A&B choose to partner no royalties will be paid to the 150 mineral acres	If the 40 acres is leased to Company B: Company B is force pooled and the lessor receives royalties based on the lease agreement with Company B

A: Conservation is using best practices to maximize a resource without waste. Stranding of gas, as a result of incomplete leasing, leads to diminished potential yield from the field.

Legislative Considerations for Forced Pooling

By Dale Tice, Esq, Marshall Parker & Associates

Oil and gas leasing and Marcellus development are often perceived as controversial and divisive issues in Pennsylvania. While the large majority of landowners in the Marcellus fairway have been amenable to leasing their property for gas drilling, there is a vocal minority of landowners who vehemently oppose Marcellus development and have refused to proceed with an oil and gas lease for their property.

Readers of the PENNROAR are by now familiar with the operation of the pooling provision found in the gas leases used by Marcellus operators. It is readily apparent that these holdout landowners will make it difficult or impossible for the gas companies to proceed with development of a production unit in the area where the un-leased land is located. For the gas companies, the solution to this problem has been forced pooling – also sometimes referred to as “fair pooling” or compulsory integration.

Pennsylvania has previously enacted a forced pooling law known as the Oil and Gas Conservation Law, but as discussed in the analysis by Les Greevy, the current law does not apply to the Marcellus shale. As a result, there has been an ongoing, heated discussion among the various stakeholders about the possibility of drafting a new version of the Conservation Law that would allow compulsory integration of the Marcellus. At this time, it appears that forced pooling may be such a hot topic that legislators will refuse to touch it, but the issue is likely to resurface in future legislative sessions. It is not the purpose of this article to advocate for adoption of a new forced pooling law in the Commonwealth. Rather, the discussion below highlights a number of issues that should be addressed in the legislative discussion about a forced pooling law, in the event that such legislation is introduced in Pennsylvania.

Good Faith Offer

Texas has enacted a forced pooling law. However, the law requires that the oil and gas company first make a good faith lease offer to a holdout landowner before proceeding with a forced pooling proceeding. As a result, the forced pooling law has been rarely used in Texas. Pennsylvania legislators may

consider including such a requirement in any forced pooling proposal.

Minimum Leased Acreage

Some states with forced pooling laws have included a requirement that the operator have a certain minimum amount of acreage leased in the area of the proposed pooled unit. This type of requirement forces the gas company to lease some percentage of the landowners in the area intended for drilling before proceeding with compulsory integration. The percentage of land required to be leased may vary anywhere from 51% to 95%. Obviously, as the minimum percentage required increases, it will be increasingly difficult for the gas company to utilize forced pooling.

Risk Penalty

When an oil and gas company drills a well, there is always some risk that the well will be unproductive and the operator will be unable to recoup its drilling costs. The amount of risk will vary from well to well

continued to page 6

FREE ROYALTY OWNERS' WORKSHOP

Have You Signed a Gas Lease?
Join Us for a Free Royalty Owners' Workshop

Learn How:

- To Stay in Control
- To Protect Your Family From:
 - Long-term Care Costs
 - Taxes
 - Liability
- To Use Family Limited Partnerships, LLCs and Trusts

Register by calling

(800) 401-4552 or at **PAGasLaw.net**



Attorney
Dale Tice

**Marshall, Parker
& Associates, LLC**
Protecting Pennsylvania Gas Landowners

Williamsport, Jersey Shore
Scranton, Wilkes-Barre

and will also vary depending on the target formation being drilled.

The concept of the “risk penalty” recognizes that the non-participating landowner who is being forced-pooled should share in the risks involved in drilling. Forced pooling laws accomplish this risk sharing by providing that the non-participating landowner will not receive gas production payments until the gas company has recouped the landowner’s proportional share of the costs to drill the well, plus some additional percentage of the costs as compensation to the operator for undertaking the risk of drilling.

Pennsylvania’s current Conservation Law sets the risk penalty at 200% of the landowner’s proportional share of the drilling costs. Until the gas company recoups double the landowner’s share of the costs, the un-leased landowner will receive a royalty payment of 1/8 (12.5%) of his or her proportional share of production. After 200% of the landowner’s share of costs is recovered by the gas company, the non-participating landowner is then entitled to his or her entire proportional share of the total gas production. Legislators may also address the specific types of

drilling costs that may be charged against the landowner’s share.

The most recent forced pooling proposal discussed here in Pennsylvania set the risk penalty at 400%. It may be questioned whether the risks involved in Marcellus drilling justify a risk penalty in that range.

Landowner Surface Protection

A forced pooling law should explicitly provide that the surface of the land of a non-participating landowner may not be used for drilling operations. Legislators may also consider a provision requiring that the operator provide compensation to the landowner in the event that there is some inadvertent impact on the un-leased landowner’s property or water supply.

Conclusion

This author does not intend to suggest that forced pooling is either good or bad for Pennsylvania landowners. But clearly, Pennsylvania royalty owners must understand that when evaluating any future forced pooling proposal, the devil is in the details. ●

Check out the NARO-PA Chapter website:

<http://www.naro-us.org/Pennsylvania>

NARO members can log in to the members only message board to get reliable information about natural gas drilling in Pennsylvania.

- Research archived PENNROAR newsletters.
- Post a story of interest
- Visit the NARO Store for gas & oil publications
- Browse other state chapters to find out what’s happening in other plays

Pa Marcellus Exploration: Origins

A well completion report on file with the Pennsylvania Department of Environmental Protection indicates that the Noble Drilling Company, a contractor for The California Company, began drilling a gas well on March 28, 1951, on the Arthur W. Bennett property near Sonestown, Sullivan County, Pennsylvania. The drillers determined the Marcellus Shale to be present at depths of 8,220 to 8,374 feet below the surface. “Slight traces” of gas were in “black, slightly calcareous shales” found at a depth of approximately 8,350 feet. The well was plugged on December 5, 1951.

Featured Editorial:

Forced Pooling, Compulsory Integration, or Eminent Domain?

By Jacqueline Root, R & R Energy Consulting

The Pennsylvania debate on this topic can quickly become very emotional. Should unleased mineral owners be subject to forced pooling? Is compulsory integration the equivalent of eminent domain? Will the unleased mineral /surface owner be forced to give up surface rights? Does compulsory integration have the potential to maintain a competitive leasing environment? Does compulsory integration already exist in PA? When this is bantered about in the media that last two questions rarely enter into the discussion.

Forced pooling already exists in PA under the Conservation Law and applies to formations below the Onondaga Horizon or below 3800' where the Onondaga is not present. Wells drilled in the Utica formation will be subject to the Conservation Law and it is clear to me that the law should also apply to the Marcellus. The Conservation Law includes the following as its "Declaration of Policy:" *It is hereby declared as an expression of policy to be in the public interest to foster, encourage, and promote the development, production, and utilization of the natural oil and gas resources in this Commonwealth, and especially those which may exist in the Lower Devonian Series and the Silurian and Cambro-Ordovician Geological Systems or from any formation below the Onondaga horizon, in such manner as will encourage discovery, exploration, and development without waste; and to provide for the drilling, equipping, locating, spacing and operating of oil and gas wells so as to protect correlative rights and prevent waste of oil or gas or loss in the ultimate recovery thereof, and to regulate such operations so as to protect fully the rights of royalty owners and producers of oil and gas to the end that the people of the Commonwealth shall realize and enjoy the maximum benefit of these natural resources, it being recognized, however, that the uninterrupted exploration and development of Pennsylvania and Mississippian Systems and the Upper and Middle Devonian Geological Series, being sands and strata above the Onondaga Horizon, both of a primary and subsequent methods have been carried on exhaustively since the discovery of oil in the Drake Well in 1850 without regulatory restriction or control to such an extent that at the present stage of development it would be*

impractical and detrimental to the operation of such shallow horizons to impose regulations under this act, particularly in view of the facts that the production therefrom, whether of primary or secondary nature is carried on without appreciable waste and that the methods of exploration, discovery, development and production above the Onondaga Horizon and in shallow horizons at a depth of less than three thousand eight hundred feet differ from methods of exploration, discovery, development and production below the Onondaga Horizon or below three thousand eight hundred feet in cost, methods, operating problems, and other important characteristics. Development of the Marcellus does not differ from that of formations below the Onondaga and so, the same reasoning pertaining to elimination of waste and protection of correlative rights should apply to the Marcellus and any other similar formation.

The Conservation Law should be updated not only to include the Marcellus but also to reflect new techniques and better protect the rights of mineral owners subject to compulsory integration.

The law does require that proposed units be based on geology but is rather vague in the details. Spacing requirements would further eliminate waste of the energy resource as well as surface disturbance.

Continued to page 5

**Natural Gas Leasing,
Pipeline ROW and Well Site
Negotiations**

*"Protecting landowner interests
and facilitating development"*

Jackie Root, CMM
Earle Robbins, CMM
Katie Root

WWW.Gaswellguru.com

Ph 570-537-3829 1871 Collums Rd
Fax 570-537-3836 Lawrenceville
PA 16929



Continued from page 4

Marcellus unitization is far from uniform and there is no protection other than a legal battle if the operator opts to include your acreage based on lease expiration rather than geology. If an operator wished to force pool an unleased mineral owner, the operator should have to control 80% or more of the proposed unit. The mineral owner should have clear guidelines to participate as an operator if that is their choice. What is a fair cost recovery percentage, should it be different depending on the formation, it is currently 200%. Should it be 150%? If you as a mineral owner chose to take a royalty percentage rather than participate should that number automatically be 12.5% or should there be a mechanism to arrive at a higher rate?

Okay, so you have made the decision not to lease. If you are force pooled does that give the operator access to your surface for roads, well pads or pipeline?

The answer is no. However, it does give the operator the right to drill under and frac' under your property and establishes rules under which you would receive compensation. If you decided not to lease because you believe this is the devil's work and you want nothing to do with oil and gas development, you certainly will

On the other hand, if you haven't leased because the Lessee is unwilling to meet your lease terms and monetary requests, you may find that a well written Conservation Law could be your best friend.

Once an operator has significant leasehold in your area, Marcellus development can be fast, efficient, and most desirable if you are leased. The downside is reduced leasing competition for the unleased mineral owner, particularly those with small parcels. Whether leased to a third party or unleased, they risk be excluded from the unit and there is no protection under current PA law. Compulsory integration offers opportunity to the mineral owner who chooses to either take a personal risk or to lease to a third party willing to meet their terms.

The governor's Marcellus Shale Advisory Commission made the recommendation in July that the Oil and Gas Conservation Law be updated to reflect new technology and include the Marcellus formation. There have been whispers that the industry would like to see this outcome.

Mineral owners need to be part of this discussion to ensure that our rights are protected. ●



The Energy You Need.

Energy In Depth Northeast Marcellus Initiative is "the" resource for information on natural gas production in the twin tiers of Pennsylvania and New York.

The Facts You Demand.

Please visit us online and get involved today!

Contact John Krohn for additional information

 [Email Updates](#)

 [RSS Feed](#)

 [Facebook](#)

 [Twitter](#)

 [Youtube](#)

Additional Protections Give Royalty Owners Equal Footing in Forced Pooling

By Bill Wilson, NARO-PA, NE Regional Board Member

In his recommendation to The Economic and Workforce Development Subcommittee (Marcellus Shale Advisory Commission, Terry Engelder noted that, “rock splitting by hydraulic pressure is known to travel as much as 2000 feet from a horizontal well. Some gas may come from distances up to 2000 feet although the volumes from this distance are very low.” Further he says, “Fractures opened by hydraulic pressure generally drain a swath of a “PRODUCTION UNIT” about 300-500 feet either side of a well – This is a common drainage distance even under unleased land.”

Other industry reps have stated that they think the effective economic recovery distance from a horizontal well is as little as 130-150 feet, a number that is bolstered by the decreasing well spacing to 250 feet in parts of the Barnett Shale.

With the preceding in mind, if there is to be mandatory integration, wouldn't it make sense to structure the law so that a property could only be forced into a “PRODUCTION UNIT” for an individual well whose bore will pass directly beneath the property? If that well is to be part of a larger “POOLED UNIT” for other wells, it should not be assessed for the cost of the entire “POOLED UNIT”, but only for proportionate share of the costs of that well's “PRODUCTION UNIT”. The costs of the entire “POOLED UNIT” should be allocated to each “PRODUCTION UNIT” on the basis of the percentage that the “PRODUCTION UNIT” represents to the whole “POOLED UNIT”.

A property should not be forced into a planned “PRODUCTION UNIT” until 6 months prior to the planned date for drilling the well. Should the well not be drilled (by a drilling rig capable of drilling the entire planned total depth including horizontal component with bit turning) within that 6 months time frame, the royalty rate should increase by 1% for each month that the date is delayed.

Shouldn't a “PRODUCTION UNIT” be limited to 500' feet either side of the well bore, then a “POOLED UNIT” could be defined as a planned area including several “PRODUCTION UNITS” that can be drilled from the same drilling pad. Further, if a property is forced into a “PRODUCTION

UNIT” against the desires of the royalty owner and if the well is drilled but is not able to achieve the planned length, the property past the end of the actual well bore should be released.

The property to be integrated should be completely surrounded by leased property if the owner of the rights being forced into a “PRODUCTION UNIT” objects to the integration and a no surface use lease should be used.

If the property owner (owner of the Oil and Gas Rights) wishes to be leased and cannot reach agreement because of “Low Ball” offers and a company controls the surrounding acreage or 70% or more of the acreage in the township, then the property owner can apply to the Bureau of Oil and Gas Management to be integrated utilizing a state assigned arbitrator. The arbitrator should choose from 2 leases, one submitted by the property owner and one submitted by the company, thus forcing each side to put forth their most realistic offer for consideration.

If production company “A” controls 70% of the area in a given township and production company “B” has property interspersed within that acreage, then company “B” or the Lessor to company “B” can petition the Bureau of Oil and Gas Management to be integrated into “POOLED UNITS” of Company “A”

Once a property is integrated, the “PRODUCTION UNITS” should not be changed unless the well in that “PRODUCTION UNIT” does not reach the planned total depth or the well is abandoned. In no case should a company be allowed to redesignate “POOLED UNITS” or “PRODUCTION UNITS”, when such redesignation would create circumstances requiring forced integration of a property not otherwise meeting the criteria.

Should an unleased property owner be integrated then the property owner should be given the option of being a participating operator, a nonparticipating operator or a Lessor under the terms of a lease approved by the arbitrator. Should a leased property owner petition the Bureau for integration, the property should be integrated under the terms of the existing lease.

Any integration hearings should be held within 75 miles of the property being integrated.●

Some Thoughts on Compulsory Integration:

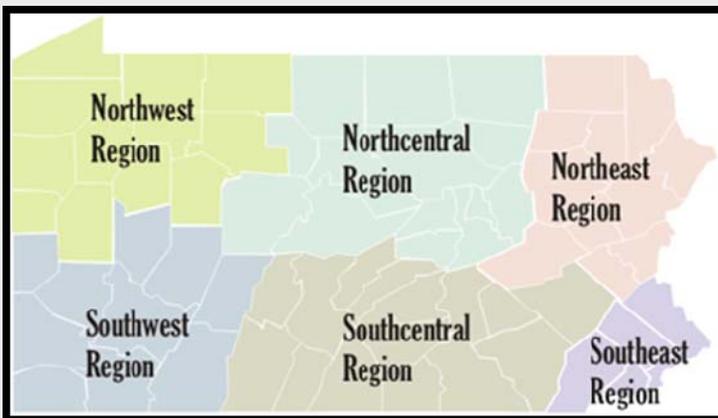
The race to lease property is over and the leasemap is a checker board of competing companies. No company has a dominant leasehold prolific enough to make horizontal drilling of 6 or 8 wells from one pad optimal. So the Lessors begin to work together or trade leases until one company controls the region. This is also beneficial to help reduce costs of infrastructure to produce natural gas from the area, as well as reduce surface disturbance from pipelines.

But with the competition out of the way, unleased property owners have only one company left to negotiate with. Lease rates and royalties offered begin to fall. The quality of lease provisions also diminishes. These unleased landowners want to engage in the exploration but now fear they have missed their opportunity to maximize their benefits. Under current law, they may have...

With Compulsory Integration, a small competing company could begin leasing in the area. Not to drill, but for the expressed goal of being forced pooled or petition to be included in the production units of the dominant company exploring the region. With this unique opportunity, the unleased landowners have a chance to negotiate a better deal with a company eager to get in on the game.

The key is drafting a Conservation Law that does not treat all unleased landowners as recalcitrant individuals who are standing in the way of natural gas development.

Do you have some thoughts on Compulsory Integration you'd like to share with the legislative committee? Your thoughts are needed as we draft a NARO-PA policy on forced pooling. Send them to penroar@yahoo.com



Pa-NARO Officers Directory

Jacqueline Root, President

jackie@gaswellguru.com

Trevor Walczak, Vice-President

penroar@yahoo.com

Lester Greevy, Treasurer

les@greevy.com

Dale Tice, Secretary

dtice@paelderlaw.com

Pa-NARO Chapter Board of Directors

Northwest Region

Brian Pitell, brian_pitell@lifetimefinancialgrowth.com

Daniel Simonsen, dsimonsen@nwbcorp.com

Northcentral Region

Jacqueline Root, jackie@gaswellguru.com

Lester Greevy, les@greevy.com

Dale Tice, dtice@paelderlaw.com

Northeast Region

Trevor Walczak, penroar@yahoo.com

Kevin Downs, kdowns@epix.net

Bill Wilson, raynoldwilson@aol.com

Southwest Region

Alan Rank, alrank@verizon.net

Southcentral Region

Tom Hall, thos_hall@yahoo.com

Tim Sutherland, TSutherland@agchoice.com

Southeast Region

Donald Nielson Jr, [djnr@ceepllc.com](mailto:djnjr@ceepllc.com)

At Large

Charles Owen Frederick, cfred01@earthlink.net

Brian Pick, brian_pick@ml.com

Subsurface trespass – Can they take the gas under my property without a lease?

By Robert J. Burnett, Esquire, Houston Harbaugh

This is a familiar yet troubling question. Imagine that you own 150 acres in southwestern Pennsylvania. You have received offers from several prominent gas producers but have not yet signed a lease. Your neighbor, however, did sign a Marcellus lease a few years ago. A typical Marcellus well pad site was erected about 600 yards from your property line. Hydraulic fracturing operations are now complete and the horizontal well is now producing 15 mcf of gas per week. You were told that the horizontal well bore – which is approximately 6,000 feet below the ground – does not encroach or cross your surface boundary. Nonetheless, you are concerned that your neighbor could be draining gas from underneath your property. If so, can you stop your neighbor from taking “your” gas? As with many oil/gas issues, the answer to this question is based on a unique aspect of oil/gas law: the rule of capture.

The “rule of capture” is a well-established doctrine which holds that a landowner is entitled to extract the oil and gas beneath his land, as well as the oil and gas which flows or migrates from a common reservoir.

Oil and gas generally migrate to low pressure areas within a reservoir. As a result, production from one well may cause gas to migrate across property lines. The “rule of capture” recognizes this unique geologic phenomenon by allowing a landowner to “appropriate the oil and gas that have flowed from adjacent lands without the consent of the owner” of those adjacent lands. See, Ellif v. Texon Drilling Co., 210 S.W. 2d 558, 561 (Tex. 1948). Under this rule, there is no liability for “reasonable and legitimate drainage from the common pool.” Ellif, 201 S.W. 2d at 562. As the Texas Supreme Court once observed: “...the rule of capture can mean little more than that due to their fugitive nature, the hydrocarbons, when captured belongs to the owner of the well which they flowed, irrespective of where they may have been in place originally...”

See, Halbouty v. R.D. Commission, 357 S.W. 2d 364, 375 (Tex. 1962); see also, Occidental Permian Ltd. v. Helen Jones Foundation, 333 S.W. 3d 392, 409

(Tex. Ct. App. 2011) (“the rule of capture provides that a landowner owns all of the oil and gas produced by a legally drilled well located on his property, even though the well may be draining minerals from neighboring properties...”); Cowling v. Bd. of Oil, Gas & Mining, 830 P.2d 220, 224 (Utah 1991) (landowner not liable to adjacent landowner “even if the producing well [is] drilled next to the adjacent landowner’s boundary”). Thus, since gas in a continuous reservoir will flow to a point of low pressure, a landowner is not restricted to the particular gas that may underlie his property but is the owner of all “which he may legally recover.” See, Halbouty, 357 S.W. 2d at 375.

So long as the well is within the vertical boundaries of his or her property, all gas extracted from that well is lawfully owned by that landowner/operator. If the well bore “bottoms out” underneath the property of another and is a so-called “deviated well”, the operator has committed a subsurface trespass. See, Continental Resources Inc. v. Farrar Oil Co., 559 N.W. 2d 841, 844 (N.D. 1997) (“A subsurface trespass remains defined that way: the bottoming of a well on the land of another without his consent.”); see also, Hastings Oil Co. v. Texas Co., 234 S.W. 2d 389 (Tex. 1950) (enjoining a deviated well that bottomed under the land of another); Edwards v. Lachman, 534 P.2d 670 (Ok. 1974) (rule of capture does not apply to hydrocarbons removed as a result of a deviated well). The rule of capture only protects the operator from drainage liability if the gas produced has *migrated* from underneath the land of another. No such protection is afforded the operator of a deviated well.

When the rule applies, the only protection that a landowner has against the flow of migrating gas to a neighboring well is to drill an offset well. Such wells “interrupt the flow of oil and gas being drawn by neighboring wells.” See, INB Land; Lattle, LLL v. Kerr-McGee Rocky Mt. Corp., 190 P.3d 806, 808 (Colo. Ct. App. 2008). “[T]he rule of capture is justified because a landowner can protect himself from drainage by drilling his own well thereby avoiding the uncertainties of determining how gas is migrating through a reservoir.” Coastal Oil & Gas v. Garza Energy Trust, 268 S.W. 3d 1, 14

(Tex. 2008). Because the landowner generally has the right to drill offset wells, the rule of capture precludes claims of trespass or improper drainage against a neighboring well.

Does the “rule of capture” apply to gas extracted from Marcellus shale formations? The rule is based on the notion that gas within a common reservoir will freely migrate throughout that gas reservoir. Shale gas, such as the Marcellus, is considered a “tight” geologic formation – the gas is trapped within relatively nonporous and impermeable rock and does not migrate naturally. The natural gas in such formations cannot be produced without hydraulic fracturing stimulation or “fracing.” Fracing is accomplished by pumping fluid down a well at extremely high pressure so that it “cracks” natural fault lines in the rock formation. These fault lines, which are then “propped” open by certain proppants, allow the “trapped” natural gas to escape to the surface through the well bore. What happens when these subterranean fractures extend across surface property boundaries and release gas which would have otherwise remained in place?

The Texas Supreme Court recently addressed the issue of subsurface trespass by hydraulic fracturing in the landmark case of Coastal Oil and Gas Co. v. Garza Energy Trust, 268 S.W. 3d 1 (Tex. 2008). In Garza, the plaintiff argued that drainage caused by fracing was analogous to a suit for trespass caused by drilling a slant or deviated well. The plaintiff contended that fracing operations, like a deviated well, unlawfully remove gas located beneath another’s property.

The Garza court rejected this argument under the auspices of the rule of capture and opined that “the rule of capture determines title to gas that drains from property owned by one person onto property owned by another.” Garza, 268 S.W. 3d at 14. The court further observed that the gas produced through a deviated well, unlike fracing operations, “does not migrate to the wellbore from another’s property; it is already on another’s property.” Id. at 14. Since fracing operations create a new reservoir by loosening the rock formation, the court implicitly reasoned that such gas “migrated” onto the defendant’s property. As such, the plaintiff’s claim for unlawful drainage caused by the adjacent fracing operations was precluded by the rule of capture.

The Pennsylvania Supreme Court has yet to address the issue of subsurface trespass by hydraulic fracturing. It is unclear how the Pennsylvania Supreme Court will decide this issue.

Hydraulic fracturing is a legitimate, widely used recovery method which is essential to the economical production of non-conventional gas resources such as the Marcellus shale. Nonetheless, there are some that believe Garza was wrongfully decided since the gas itself did not “migrate” naturally and drained only because of an artificially created channel. *e.g.* Peterson v. Grayce Oil Co., 37 S.W. 2d 367, 370-371 (Tex. Civ. App.

1936) (suggesting over seventy years ago that rule of capture does not apply to artificially induced flows).

Given this fact, opponents argue that the rule of capture should not insulate or protect fracing operations. This debate will certainly continue in the months ahead as fracing operations escalate throughout the Commonwealth. ●



SIGNING THE MARCELLUS LEASE IS ONLY THE BEGINNING...

Landowners often face complicated and troubling issues after the lease is signed. Royalty disputes, non-productive leases and surface access issues can impact your lease investment. We can help you navigate these issues.

HOUSTON HARBAUGH PROTECTING AND PRESERVING THE MINERAL OWNER'S INVESTMENT



For more information, contact:
Robert J. Bumett, Esq.
412.288.2221
rbumett@hh-law.com



Houston Harbaugh
ATTORNEYS AT LAW

www.hh-law.com/practice/oilandgas.aspx

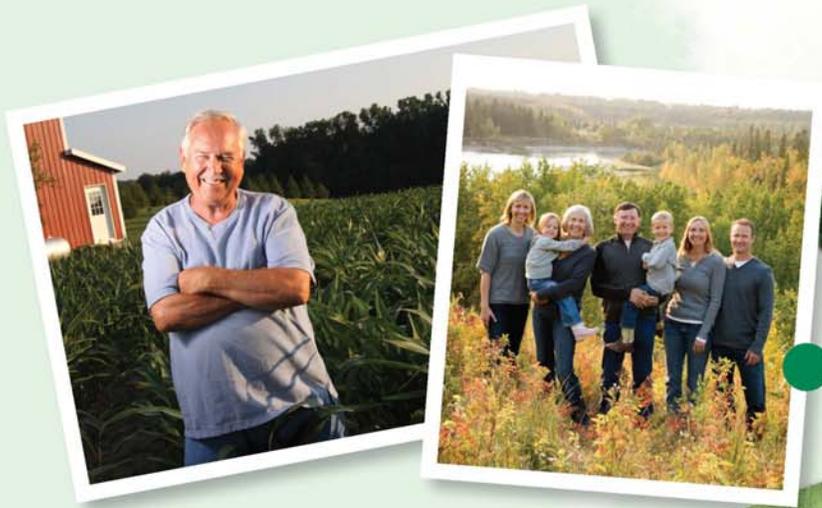
Oil and Gas Lease Planning and Management

4 Steps to securing your lease income

- Step 1 Pre-Lease Planning
- Step 2 Leasing Preparation
- Step 3 Managing Lease Income
- Step 4 Continuing Support

A trusted, local resource and “no cost advisor,” Northwest does not charge an hourly fee for oil and gas lease planning and guidance.

We fully understand the “Life Cycle” of a lease and can guide you through each step to help you make good money decisions with specialized knowledge, top-level service, and integrity.



Bud Shuffstall
Senior Oil and Gas Banking Officer
(814) 282-8304
bshuffstall@nwbcorp.com



Daniel Simonsen
Oil and Gas Banking Officer
(814) 547-2819
dsimonsen@nwbcorp.com



Christopher Junker
Oil and Gas Banking Officer
(814) 282-8305
cjunker@nwbcorp.com

Develop your plan, keep it simple, and start now.



Where people make the difference.

Northwest Direct: 1-877-672-5678 • www.northwestsavingsbank.com

MEMBER FDIC



Act 35 of 2011 Amends Clean and Green Law Again

By John A. Shoemaker, Esq., Greevy & Associates



The governor signed Act 35 of 2011 (“Act 35”) into law on July 7, 2011. Act 35 amends the Pennsylvania Farmland and Forest Land Assessment Act of 1974 (the “Clean and Green Act”).

The Clean and Green Act had previously been amended by Act 88 of 2010 (“Act 88”), sponsored by Sen. Gene Yaw (R-23rd District).

Prior to the Act 88 and Act 35 amendment, the Clean and Green Act did not address the consequences of construction of natural gas well pads on lands subject to preferential assessment. Consequently, various counties throughout the state reacted differently—some counties imposed a rollback taxes on the entire parcel, while others imposed the penalty only as to the portion of the land actually devoted to gas drilling.

The legislature addressed this issue last year by passing Act 88. Under the Act 88 amendment to the Clean and Green Act, counties were required to impose rollback taxes uniformly and only as to the area occupied by the restored well site. Act 88 further provided that no rollback could be imposed until the gas company filed a well site restoration report with the Pennsylvania Department of Environmental Protection (“DEP”), an event that was unlikely to occur for several years.

Thus, landowners who might have been facing a substantial rollback tax bill would have time to come up with funds to pay the taxes.

Act 35, a bill sponsored by Rep. Tina Pickett (R-Bradford/Sullivan/Susquehanna) modifies the Act 88 amendment to such that counties may impose rollback taxes as to a somewhat greater portion of the land. Also under the Act 35 amendment, counties may impose rollback taxes when a well production report is first due to DEP—much sooner than under the Act 88 amendment. The rollback tax would not be due until the following tax year.

Otherwise, Act 35 does not modify the Clean and Green Act as amended by Act 88.

Under both the Act 88 amendment and the Act 35 amendment, counties may not impose rollback taxes upon portions of preferentially

assessed lands which are devoted to subsurface transmission or gathering lines.

Under the Clean and Green Act, as amended, where rollback taxes are authorized, counties may recover the difference between the preferential assessment and the ordinary assessment for the most recent seven years, plus interest at the rate 6% annually. ●

Thomas M. Hall, CRPC®
Financial Advisor

(814) 231-8905 • (877) 299-8905

120 Regent Court, Suite 200
State College, PA 16801

Merrill Lynch Wealth Management is a registered trademark of Bank of America Corporation. Merrill Lynch Wealth Management makes available products and services offered by Merrill Lynch, Pierce, Fenner & Smith Incorporated, a registered broker-dealer and member SIPC, and other subsidiaries of Bank of America Corporation. Investment products:



Are Not FDIC Insured | Are Not Bank Guaranteed | May Lose Value

© 2011 Bank of America Corporation. All rights reserved.



Yaw's Oil and Gas 'Invoice Itemization' Bill Passes Senate

Currently, Pennsylvania does not require gas companies to list deductions from royalties paid to landowners on monthly payments.

Senate Bill 460 now moves to the House of Representatives for consideration.

For more information about SB 460, see the archived March 2011 & May 2011 Penn Roar @

www.naro-us.org



PENNSYLVANIA CHAPTER OF NARO INVITES YOU TO
JOIN US FOR AN EXCLUSIVE EVENT ON MARCELLUS SHALE!!!

Town Hall Meeting

Thursday, November 10, 2011

at

The Greater Philadelphia Expo Center at Oaks
100 Station Avenue; Oaks, PA 19456
phillyexpocenter.com

Beginning at **4:30 pm**: Visit with Vendor Sponsors and Business Partners

6:00 pm: Educational Seminars

Entrance fee for Attendees: \$20

Free for NARO members

Refreshments

Speakers to include representatives from:

NARO

HAMBURG, RUBIN, MULLIN, MAXWELL & LUPIN, Attorneys at Law

DEPARTMENT OF ENVIRONMENTAL PROTECTION

PENN STATE UNIVERSITY

SENATOR JOHN RAFFERTY, JR.

And more. . .

- ◆ Come and find out about NARO, the only national organization representing, solely and without compromise, oil & gas royalty owners' interests.
- ◆ Hear about legal updates impacting Marcellus Shale and Gas Leasing.
 - ◆ Receive information regarding Royalties.
- ◆ Obtain Wealth Management guidance and assistance.

For further information about NARO, visit www.naro-us.org/Pennsylvania,
send email to lawyers@hrmml.com or call 215-661-0400.

To register now, send below portion, with payment, to:
Hamburg, Rubin, Mullin, Maxwell & Lupin; Attn.: Joan Wean; 375 Morris Road; Lansdale, PA 19446

Yes, I will attend. Enclosed is my check, payable to "PA NARO" in the amount of \$20, per person.

Name(s) _____

Company Name: _____

Address: _____

City/State/Zip: _____

Email: _____ Telephone no.: _____