

Pennsylvania Oil and Gas Litigation Update

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OVERVIEW

- Delay Rental Litigation
- Flat-Rate Payment Litigation
- “Paying Quantities” Litigation
- Minimum Royalty Litigation
- “Operations” Litigation
- Fraudulent Leasing Litigation
- Future Litigation and Undecided Issues
 - Implied Covenant to Develop
 - Butler v. Powers
 - Hydraulic Fracturing and Strict Liability

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2

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Delay Rental Litigation

- Hite v. Falcon Partners
13 A.3d 942 (Pa. Super. 2011)
 - One-year “primary” term.
 - “As long thereafter” as oil or gas is produced, as operations continue, or as delay rental is paid, or until all oil and gas has been removed – whichever shall occur last.

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3

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Delay Rental Litigation

- Hite v. Falcon Partners
13 A.3d 942 (Pa. Super. 2011)

The court held:

 - “Lease will not be construed to create a perpetual term” unless the intent to do so is clearly stated.
 - The language of the clause in this lease only allowed Falcon one year in which to begin operations – even if Falcon paid delay rentals.

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4

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Flat-Rate Payment Litigation

- Heasley v. KSM Energy, Inc.
52 A.3d 341 (Pa. Super. July 2012)
 - Leases had 20 year primary terms, which had expired.
 - Lessees admitted that neither oil nor gas was being produced.
 - Lessee paid rental payment of \$100.00 if flow was less than 100,000 cubic feet per 24 hours, **while the gas from said well is being used.**

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5

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Flat-Rate Payment Litigation

- Heasley v. KSM Energy, Inc.
52 A.3d 341 (Pa. Super. July 2012)

The court held:

“The Lease Agreement, by its terms, remained in effect only so long as production continued. When production ceased, the lease became an at-will tenancy, subject to termination by the lessor at any time.”

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6

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“Paying Quantities” Litigation

- T.W. Phillips Gas & Oil Co. v. Jedlicka
42 A.3d 261 (Pa. March 2012)
 - Lessor claimed that the lease terminated because production was not “in paying quantities.”

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7

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“Paying Quantities” Litigation

- T.W. Phillips Gas & Oil Co. v. Jedlicka
42 A.3d 261 (Pa. March 2012)
 - (1) If a well consistently pays a profit, **however small**, over operating expenses, it will be deemed to have produced in paying quantities.
 - (2) Where production on a well has been marginal or sporadic, such that over some period the well's profits do not exceed its operating expenses, a determination of whether the well has produced in paying quantities requires consideration of the **operator's good faith judgment** in maintaining operation of the well.

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8

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Minimum Royalty Litigation

- Kilmer v. Elexco Land Services, Inc.
990 A.2d 1147 (Pa. 2010)
 - Lessors asserted that their leases were invalid because it did not provide for 1/8th royalty as guaranteed by the Guaranteed Minimum Royalty Act.
 - Post-production costs were specifically enumerated in the lease.
 - Supreme Court concluded that such deductions did not violate the Guaranteed Minimum Royalty Act.

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9

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Minimum Royalty Litigation

- Kilmer v. Elexco Land Services, Inc.
990 A.2d 1147 (Pa. 2010)

Open Question:

 - **What if the lease is vague or silent as to deduction of post-production costs?**

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10

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Minimum Royalty Litigation

- Tawney v. Columbia Natural Resources, LLC
633 S.E.2d 22 (W. Va. 2006)
 - The court found that “at the wellhead” language in leases was silent as to allocation of post-production costs and thus the provision should be construed against the lessee.
 - The court concluded that post-production costs could not be deducted.
 - The jury entered a verdict for \$405 million dollars.

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11

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Minimum Royalty Litigation

- Katzin v. Central Appalachia Petroleum
39 A.3d 307 (Pa. Super. January 2012)
 - Lessor wanted to invalidate the lease based on non-compliance with the Guaranteed Minimum Royalty Act because it does not state what costs may be deducted.
 - The court decided that the lease clearly allows the lessor to deduct costs and that the provision complies with the Act on its face.

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12

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Minimum Royalty Litigation

- **Katzin v. Central Appalachia Petroleum**
39 A.3d 307 (Pa. Super. January 2012)
 - “Vagueness” regarding what costs are deductible is not grounds to invalidate a lease, but perhaps could give rise to a breach of contract claim.
 - **Warning:** Companies may be subject to damages lawsuits if leases are vague or silent as to deduction of post-production costs.

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13

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Minimum Royalty Litigation

- **Pollock v. Energy Corp. of America**
2012 WL 6929174 (W.D. Pa. October 2012); 2013 WL 275327 (W.D. Pa. January 2013)
 - The Court opened the door to allow deduction of certain post-production costs even if the lease is silent.
 - The Court was ruling on motions for summary judgment, and determined that the issues needed to be fleshed out at trial.
 - Federal court decision is not binding on Pennsylvania State Courts.

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14

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“Operations” Litigation

- **Burke v. GAPCO Energy LLC**
2012 WL 1038849 (W.D. Pa. March 2012)
 - 2007 lease with a primary term of 3 years.
 - Provision allowed the lease to remain in effect beyond the primary term if oil or gas was not being produced but the Lessee was “engaged in operations.”
 - Plaintiffs argued that Lessee’s activities did not constitute “operations” as defined in the lease.

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15

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“Operations” Litigation

- **Burke v. GAPCO Energy LLC**
2012 WL 1038849 (W.D. Pa. March 2012)

The court held:

 - “[T]here remains doubt as to whether Plaintiffs’ version of facts, if proven, would constitute ‘operations,’ even under the broad terms of the lease.”
 - The court decided the issues needed to be determined at trial.

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16

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“Operations” Litigation

- **Good Will Hunting Club, Inc. v. Range Resources, Inc.**
2012 WL 722614 (M.D. Pa. March 2012)
 - One section of the lease could be interpreted to require only commencement of a well during the primary term; however, a different section could be interpreted to require both commencement and actual drilling.
 - Operators engaged in some preparatory activities but had not drilled a well at the expiration of the primary term.

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“Operations” Litigation

- **Good Will Hunting Club, Inc. v. Range Resources, Inc.**
2012 WL 722614 (M.D. Pa. March 2012)
 - The court could not dismiss Plaintiff’s claim because of the ambiguity.
 - At trial, the court must reconcile the two different clauses in the lease and decide whether the Operator’s activities were sufficient to hold the lease beyond the primary term.

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18

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Fraudulent Leasing Litigation

- **Harrison v. Cabot Oil & Gas Corporation**
2012 WL 3542382 (M.D. Pa. August 2012)
 - Harrison claimed he was induced to sign the lease by a fraudulent representation.
 - Cabot Oil & Gas Corporation asked the court to extend the lease because this case had prevented it from beginning production during the primary term.
 - The court “split the difference.”

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19

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Future Litigation and Undecided Issues

Implied Covenant to Develop

- **Delmas Ray Burkett, II Revocable Trust v. EXCO Resources (PA), LLC**
2012 WL 1019025 (W.D. Pa. March 2012)
 - The 1916 lease in this case specified that a minimum of two wells were to be drilled during the primary term of the lease.
 - EXCO argued that by drilling two wells within the primary term it had fulfilled the requirements of the lease.

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20

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Future Litigation and Undecided Issues

Implied Covenant to Develop

- **Delmas Ray Burkett, II Revocable Trust v. EXCO Resources (PA), LLC**

2012 WL 1019025 (W.D. Pa. March 2012)

“The Development Clause here does not forever fix the number of wells to be drilled, but only alters the compensation to be paid after the first two wells are drilled and produce paying quantities of oil and/or gas.”

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21

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Future Litigation and Undecided Issues

Butler v. Powers

- Counsel for John and Mary Josephine Butler argued that it is irrelevant whether modern-day experts consider Marcellus shale a “mineral” because it is the intent of the parties to the deed which controls.
- Counsel for Powers Estate argued that general rules of construction require that the words in the conveyance be given their ordinary meaning. Counsel relied on the decision in *U.S. Steel Corp v. Hoge*, 503 Pa. 140 (Pa. 1983).

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22

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Future Litigation and Undecided Issues

Hydraulic Fracturing and Strict Liability

- **Kamuck v. Shell Energy Holdings GP, LLC**
2012 WL 1463594; 2012 WL 1466490 (M.D. Pa. April 2012)
- **Berish v. Southwestern Energy Production Co.**
763 F.Supp.2d 702 (M.D. Pa. 2011); 2011 WL 1569592 (M.D. Pa. May 2012)
“A number of Pennsylvania cases with facts analogous to the instant suit have determined that the activities involved there were not abnormally dangerous.”

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23

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QUESTIONS?
COMMENTS?



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24

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