



# Recent Legal Developments Affecting California Royalty Owners

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# Recent California Legal Developments

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- **Judicial Developments**
  - No significant reported California appellate decisions in 2015 or in first half of 2016.

# Recent California Legal Developments

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- **DOGGR Administrative Developments**
  - To implement Senate Bill 4 enacted in 2013 , DOGGR, DOGGR adopted final regulations addressing hydraulic fracturing, acid fracturing and acid matrix stimulation. (CAL. CODE REGS. Tit. 14§§ 1780, et seq.)

# Recent California Legal Developments

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- **DOGGR Administrative Developments- Injection Wells**
- Federal Safe Drinking Water Act requires that an underground source of drinking water or “USDW” be protected from contamination.
  - USDWs are generally aquifers with water quality measured *at less than 10,000 milligrams* per liter of total dissolved solids (mg/L TDS)
  - Upon recommendation by a State, USEPA may exempt individual aquifers in accordance with criteria specified in the federal regulations. (40 C.F.R. 144.3 and 144.7 (2015).)

# Recent California Legal Developments

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- **DOGGR Administrative Developments-**
- DOGGR had not previously considered non-hydrocarbon-bearing aquifers with ***greater than 3,000 mg/L*** TDS to be a drinking water source under California law.
- DOGGR had not previously obtained exemptions for aquifers with TDS between 3,000 mg/L and 10,000 mg/L.
- Has led to a reclassification of aquifers
  - DOGGR has identified over 2,500 wells in California (including both enhanced oil recovery injection wells and disposal injection wells) that may have been improperly approved for injection into non-exempt aquifers containing water with less than 10,000 mg/L TDS.

# Recent California Legal Developments

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- **DOGGR Administrative Developments**
  - **Exempt Aquifers**
    - DOGGR adopted permanent regulations requiring operators injecting or disposing water into identified aquifers to obtain an aquifer exemption issued by the U.S. Environmental Protection Agency under the Safe Drinking Water Act by specified dates or to cease injection activity. (CAL. CODE REGS. Tit. 14, § 1779.1.)
    - Regulations now provide that approval or rescission of an underground injection project are at DOGGR's discretion

# Recent California Legal Developments

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- **Deadlines for Obtaining Aquifer Exemption**
  - Aquifer is *not* a hydrocarbon producing zone
    - Less than 3,000 TDS -injection shall cease by October 15, 2015
    - between 3,000 and 10,000 TDS -injection shall cease by February 15, 2017
  - Aquifer *is* a hydrocarbon producing zone
    - Less than 10,000 TDS -injection must cease by February 15, 2017

# Recent California Legal Developments

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- **DOGGR -Cyclic steam wells**
  - DOGGR identified approximately 3,600 permitted cyclic steam wells that may be injecting near, but outside the boundaries of, exempted zones.
  - Cyclic steam wells will now be included in the inventory of existing injection wells.



# Recent California Legal Developments

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- **DOGGR Re-Abandonment Requirements**
  - Requiring Re-abandonment of Wells to Isolate USDWs
    - Public Resources Code § 3228:

“Before abandoning any well in accordance with methods approved by the supervisor or the district deputy, and under his or her direction, the owner or operator shall isolate all oil-bearing or gas-bearing strata encountered in the well and shall use every effort and endeavor to protect any underground or surface water suitable for irrigation or domestic purposes from the infiltration or addition of any detrimental substances. “ (See, also, Public Resources Code § 3208)

# Recent California Legal Developments

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- **DOGGR Re-Abandonment Requirements**
  - DOGGR informal revision of re-abandonment requirements
  - Recovering “Junk in the Hole”
    - DOGGR’s regulations contemplate and specifically allow wells to be abandoned with fish in the hole.
    - 14 CCR Section 1723(f):
      - Diligent effort shall be made to recover junk when such junk may prevent proper plugging and abandonment either in open hole or inside casing.

# Recent California Legal Developments

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- **DOGGR Re-Abandonment Requirements**
  - 14 CCR Section 1723(f) (continued):
    - In the event that junk cannot be removed from the hole and fresh-saltwater contacts or oil or gas zones penetrated below cannot therefore be properly abandoned, cement shall be downsqueezed through or past the junk and a 100-foot cement plug shall be placed on top of the junk.
    - If it is not possible to downsqueeze through the junk, a 100-foot cement plug shall be placed on top of the junk.
- DOGGR has been not been signing off on reabandonments with junk in the hole, requiring expensive additional well operations

# Recent California Legal Developments

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- **DOGGR Renewal Plan**
  - *Objective 1: Regulatory Overhaul*
    - Review All Approved Injection Projects
      - Mechanical Integrity of UIC Wells will be confirmed
      - New Project Approval Letters (PAL) setting forth requirements may be required.
    - Aquifer exemption review
    - Review and revise existing regulatory standards

# Recent California Legal Developments

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- **DOGGR Renewal Plan**
  - **Objective 2: New Regulations**
    - Adopt new regulations for Cyclic Steaming- expected by December 2016
  - **Objective 3: Modernize Data Management**
  - **Objective 4: Ensure High-Quality Workforce**
    - Reorganization of Division
    - District Offices
      - Closure of Coalinga Office

# Recent California Legal Developments

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- **Other Administrative Developments**
  - State Water Resources Control Board adopted Resolution No. 2015-0047 establishing model criteria for groundwater monitoring in areas of oil and gas well stimulation. (State Water Resources Control Board Resolution No. 2015-0047.)  
[http://www.waterboards.ca.gov/water\\_issues/programs/groundwater/sb4/docs/model\\_criteria\\_final\\_070715.pdf](http://www.waterboards.ca.gov/water_issues/programs/groundwater/sb4/docs/model_criteria_final_070715.pdf)
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# Recent California Legal Developments

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- **Other Administrative Developments- Kern County**
  - Amended its County Zoning Ordinance to set forth new development standards for all future oil and gas exploration, extraction, operations, and production activities in unincorporated areas of the County (Chapter 19.98 (Oil and Gas Production) -Kern County Zoning Ordinance)  
[http://www.co.kern.ca.us/planning/pdfs/eirs/oil\\_gas/oil\\_gas\\_ZO\\_ch19.98\\_final.pdf](http://www.co.kern.ca.us/planning/pdfs/eirs/oil_gas/oil_gas_ZO_ch19.98_final.pdf)

# Recent Judicial Developments in Other States

## Affecting Royalty Owners

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- ***Aycock v. Vantage Fort Worth Energy, LLC***, No. 11-13-00338-CV, 2015 WL 1322003 (Tex. App.—Eastland 2015, no pet. h.).
  - Landowner cotenant who does not sign an oil and gas lease cannot sue lessee of other cotenant for a portion of bonus payment.
    - Only remedy is to seek an accounting from the other cotenant lessor.



# Recent Judicial Developments in Other States Affecting Royalty Owners

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- ***Lightning Oil Co. v. Anadarko E&P Onshore LLC***, No. 04-14-00903-CV, 2015 WL 4933439 (Tex. App.—San Antonio, August 19, 2015)
  - Considered the question of whether the surface owner or the mineral owner must grant permission for a third-party to drill a horizontal borehole through property to access an adjacent parcel of land.
  - The court held, generally, the *surface estate owner* controls the earth and pore space beneath the surface estate.
  - Is this holding consistent with California law?

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- ***Fawcett v. Oil Producers, Inc.***, 352 P.3d 1032 (Kan. 2015).
  - ***Held:*** Costs incurred post-sale and post-production by third party purchasers were to be shared by the royalty interest holder and the lease operator.
  - Kansas follows the “marketable condition rule.”
    - Lessee has the implied duty to produce a marketable product
    - Cost of the marketable product lies exclusively with the lessee.
    - Only after the lessee has achieved a marketable product can any additional costs be deducted.

# Recent Judicial Developments in Other States Affecting Royalty Owners

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- ***Lindauer v. Williams Production RMT Co.***, \_\_\_\_ P.3d \_\_\_\_ (Col. 2016).
  - Colorado follows the “marketable condition rule.”
  - ***Held:***
    - Reasonable post-marketability transportation costs may be deductible.
    - Transportation costs incurred after the first commercial market do not have to enhance the value of the gas or increase royalty revenues in order to be deducted from royalty payments.

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- ***Kittleson v. Grynberg Petroleum Company***, \_\_\_ N.W.2d \_\_\_ (N.D. 2016).
  - Conflict between “market value at the well” and “no deductions from the ... royalty” provisions.
    - “At the well” rule- calculating market value using the work-back method allows a lessee to deduct post-production costs from the royalty.
    - “No deductions” language in the royalty clause, prohibits deductions of post-production costs
  - ***Held:*** more specific “no deductions” language qualifies and prevails over “market value at the well.”

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- ***Anderson v. WPX Energy Production, LLC***, 312 F.R.D. 620 (D.N.M. 2015).
  - “The Court believes that, when the Supreme Court of New Mexico determines the existence of the marketable condition rule is ripe for review, it will find the reasoning of Colorado, Kansas, Oklahoma, and Wyoming more persuasive than that of Texas.”

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- ***Chesapeake Exploration, L.L.C. v. Hyder*, \_\_\_ S.W.3d \_\_\_ (Tex. 2016).**
  - Under terms of oil and gas lease, overriding royalty did *not* bear postproduction costs, where overriding royalty could be paid in cash under lease and lease specified that overriding royalty was “cost-free.”
  - Lease had an express disclaimer of the application of *Heritage Resources, Inc. v. NationsBank*, 939 S.W.2d 118 (Tex.1996)

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- ***Beardslee v. Inflection Energy LLC***, 31 N.E.3d 80 (N.Y. 2015).
  - ***Issues:***
    - Is the habendum clause in an oil and gas lease modified by application of the force majeure clause, thereby extending the primary term of the lease?
    - Was a state moratorium on hydraulic fracturing a force majeure event?
  - ***Held:*** Force majeure clause did *not* modify habendum clause of the lease to extend the primary term.
  - ***Note:*** New York court relied on a decision of California court.

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- ***City of Fort Collins v. Colorado Oil and Gas Association*, \_\_\_ P.3d \_\_\_; 2016 WL 1757630 (Col. –May 2, 2016)**
- ***City of Longmont v. Colorado Oil and Gas Association*, \_\_\_ P.3d \_\_\_; 2016 WL 1757509 (Col. –May 2, 2016)**
  - ***Held***: Because fracking is a matter of mixed state and local concern, Fort Collins’ fracking moratorium is subject to preemption by state law and is invalid and unenforceable.



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- **Compare:**
  - *Youth for Environmental Justice v. City of Los Angeles* - Complaint filed in Los Angeles County Superior Court (LASC Case No. BC600373)- Suit against city to require more scrutinizing review of drilling applications
    - City of Los Angeles has changed its processes and expanded scope of review
  - *SWEPI, LP v. Mora County*, 81 F. Supp.3d 1075 (D.N.M. 2015)- federal court struck down county attempt to ban oil and gas production.

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- ***Pennaco Energy, Inc. v. First Northern Bank Of Wyoming***, 363 P.3d 18 (Wyo. 2015)
  - ***Held:*** Absent an express clause that terminated operator's obligations upon assignment of a surface use agreement, the operator remained liable to the landowners to perform the covenants if its assignee defaulted.

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# Questions

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