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Can gas companies and landowners profit?

BY BEN WOLFORD The Dominion Post

Bob Richmond's 505 acres slope away from his back porch, then crest and dive back into each other. They sprawl before the foot of the house that Col. John Fairfax built in 1818.

It's all Richmond's now: the four stately walls of gray stone block, the garden (which the rabbits won't vacate even as you approach) and the green, rolling hills of Preston County, a couple miles east of Kingwood.

"Look at the turkeys out in the field," Richmond says, pointing 700 yards off to a grassy hilltop. Five or six of them strut about, blurred by distance.

Beyond them, a taller, tree-covered ridge conceals the Cheat River Valley. Richmond owns a portion of the bank, but "only a mile and a half," he says with a sarcastic grin, as if to say: "How much beautiful riverbank do you own ?"

It would take a lot to convince Richmond to let an energy company bulldoze part of it and suck the natural gas out of that land. He didn't allow it for $50 an acre. And when they offered him $100 an acre, he still refused.

Of course he refused, he says. They gave him a raw deal because they thought they could get away with it.

"I told them, I said, 'I'm just a simple hillbilly,' " Richmond says with that same sarcastic grin. " 'I don't understand these things.' "

The landmen who came to him in late 2007 couldn't have known that he's anything but a simple hillbilly.

As a diplomat for the State Department, Richmond maneuvered economic development in Vietnam during the war. He helped Mobil (it hadn't yet merged with Exxon) get the rights to a still-producing well off the coast of Southeast Asia.

He worked with Haitians to arrange a lease with a Colorado energy company that "drilled five wells dry as a bone."

For 30 years he did that sort of thing.

Then he started getting letters from landmen, people hired by oil and gas companies to negotiate leases on mineral rights.

Landmen from Mason Dixon Energy Inc., on behalf of Marathon Oil, wanted to lease his mineral rights for a price Richmond didn't think was fair. He says his land is worth more like $3,000 an acre and that he should get at least 20 percent of all the profits for selling the gas underneath it, not the state minimum 12.5 percent royalties they wanted to give him.

"I knew they were trying to screw me," he says.

One woman in Star City, who didn't want her name published to protect her privacy, says she inherited 121 acres of mineral rights in Monongalia County. Soon a landman representing Dominion Energy came to her door and told her not to pass up a $5-an-acre lease and 12.5 percent royalties.

She signed the contract, collected the few hundred dollars for the lease and waited to get rich. That was five years ago, and no one's drilled a single well. The lease didn't say they had to, and with gas prices so low, it hasn't been profitable to drill.

Dominion Energy renewed the five-year lease on her mineral rights once it expired. The language in the lease allows them to continue renewing as many times as they want.

There are stories like that all over the Marcellus Shale target area: north-central West Virginia and southwest Pennsylvania. The friend down the road who got $5. The guy who took a subpar contract because he owed the hospital. The landman who told the neighbors Bob Richmond had signed his lease (Richmond has never signed a lease), and you should, too.

It's all just hearsay. But then there's a lot of hearsay — and misinformation — floating around these hills.

All eyes on Appalachia

Four hundred million years ago, a fish died and sank to the bottom of the ocean.

It decayed and left its carbon in the earth. As Europe and Africa collided with the Eastern Seaboard, creating the Appalachian Mountains, the carbon from that fish was bonding with hydrogen, creating methane and other hydrocarbons, the chief ingredients of natural gas.

Those hydrocarbons stuck in the sediments that were being packed together under tremendous pressure a mile and a half underground. That layer of sedimentary rock became the Marcellus Shale, and the fuel from that fish is still trapped in its pores.

Until the late 1990s, there wasn't any way to extract enough of that trapped gas to make drilling worthwhile. Then, new technology came into use in other shales around the country.

They used hydraulic fracturing, blasting apart hard rock and sucking up large amounts of natural gas. And they dug horizontal wells, drilling down to the shale and then horizontally along it to cover more ground and multiply production. People started looking at the Marcellus Shale.

Energy companies began paying attention to the Appalachian region like they had been paying attention to Fort Worth, Texas, site of the Barnett Shale, and to rural Arkansas, north of Little Rock, where the Fayetteville Shale lies.

Chesapeake Energy snatched up roughly 1.45 million acres of leasehold in the Marcellus Shale including large chunks of Monongalia, Preston and Marion counties. It controls more of the Marcellus Shale than any other company.

"The Marcellus Shale may ultimately become the largest natural gas field in the U.S.," Chesapeake wrote to investors in an August presentation.

Look at it by the numbers: A gas well in the Marcellus Shale can be expected to produce 4.2 billion cubic feet (bcf) of natural gas in its life, second among the "Big 4" shales, according to Chesapeake figures.

The Haynesville Shale, in east Texas and north Louisiana averages 6.5 bcf per well, the Barnett Shale averages 2.65 bcf and the Fayetteville Shale averages 2.4 bcf.

But Chesapeake doesn't pay the same royalties to mineral rights owners from each region.

In Fort Worth, where the Barnett Shale won't produce as much as the Marcellus, Chesapeake pays, on average, 25 percent royalties on their gas profits. They also pay $12,900 an acre up front.

In Preston County, where the Marcellus Shale may soon be "the largest natural gas field," the average Chesapeake pays in royalties is 15 percent and $610 an acre up front.

And Aubrey Shultz was lucky to get $100 an acre.

'Sitting on a gold mine'

Shultz's house sits on a bald knob two miles outside of Albright. It overlooks his mom's land and the cattle grazing on it. He can even see as far as Coal Lick Road where the spire of a Tenaska drilling rig shoots into the air.

His father died when he was a senior in high school and left his mother and her children with about 220 acres.

He says a landman from Honor Resources Co. came to him in 2007 wanting to lease his land and mineral rights for Chesapeake.

“They were pretty gung-ho, you know, acted like this was going to be the next Texas,” Shultz says.

So he signed — for $30 an acre, “which was the going rate back then.”

The going rate, says Vanessa Richter, human resources manager for Mason Dixon Energy, is determined by their clients, the oil and gas companies.

“Our landmen are given an area — this is the minimum we’ll pay; this is the maximum we’ll pay,” Richter says. “Our landmen will then go out there and negotiate, and if they don’t take it for the minimum, then of course, we have a little bit of bargaining room.”

Lee Warren, a spokeswoman for Marathon Oil, says the bargaining room they allow is often based on how proven a shale is in producing gas.

“In certain land areas, they know how much gas is there and what it’s likely to produce, and it’s very well defined based on hundreds and hundreds of wells that have been drilled in that area,” she says. Hundreds and hundreds of wells have been drilled in the Barnett Shale. There aren’t as many in the Marcellus.

Fortunately for Shultz, there was a mix-up with the deed to the property — Honor Resources wasn’t sure the Shultzes owned the mineral rights. But Shultz was able to prove they did and renegotiated for $100 an acre and 12.5 percent royalties in 2008.

“I think the exploration companies get a bad shake on this,” says Darryl Griwatz, vice president of Honor Resources Co. “They didn’t know any more than the people out there with large tracts of land what prices were going to go to.”

Early on in land acquisition, Marcellus Shale land was plentiful. The market was flooded with cheap acres. As demand increased, so did the price.

“Now I guess $100 an acre is just a drop in a bucket,” Shultz says.

Getting what you want

More importantly, in Shultz’s new lease, Chesapeake decided to add stipulations about how they could use the surface for its drilling.

The first lease didn’t say anything about fencing off the drilling rig to protect his stepfather’s cattle. It didn’t say anything about correcting any disturbances to the groundwater. It didn’t say anything about preventing the company from storing gas in underground formations on the property (essentially keeping the land an active drill site without actually drilling).

“That’s something I didn’t think about,” Shultz says.

The only state legislation on surface owners’ rights was enacted in 1983. It requires oil and gas developers to pay for any damages to a property or its water supply and to cover any decrease in the value of the land as a result of the drilling.

Shultz would have been covered by law if his cattle were affected.

But there’s a lot the state code doesn’t mention.

It doesn’t say how far a well must be from a house or how many wells can be drilled in a given space. It doesn’t stop the wells from being noisy.

And there’s not much oversight from any regulating agency, says Delegate Tim Manchin, D-Marion, about where developers can get the massive amounts of water needed for Marcellus Shale drilling or what to do with it once it's been used.

"People are used to signing consumer contracts, car loans, where almost all the terms are regulated by some law," says David McMahon, cofounder of the West Virginia Surface Owners' Rights Organization. "When it comes to signing a [mineral rights] lease, the only thing regulated by law is that it's got to be notarized."

Griwatz, for Honor Resources, says his company's job isn't out to cheat anyone out of a profitable agreement. In fact, he'd like to make it profitable for everyone.

"Our people do all they can to be fair and honest with property owners even though they're paid by the exploration companies," he says. "When these leases that aren't drilled upon expire, we want to go back and deal with these people again."

Griwatz says his landmen will ask rights owners what concerns they have about the drilling to see if they can address them in the contract. He says his goal is to bring the companies and the landowners to common ground.

Shultz negotiated for the common ground himself and sat back, ready to collect the royalties on his natural gas.

"We were pretty excited that we were sitting on a gold mine," Shultz says.

He doesn't know if he is or not. With the economy in recession, the market for natural gas is in the dumps. Consequently, companies have been reluctant to drill, and Shultz hasn't seen any revenue from his lease.

But as the economy recovers and gas prices return to normal, Marcellus Shale drilling will resume. Warren, of Marathon Oil, says the company is planning some drilling in the region toward the end of the year.

And when they do, Manchin wants West Virginia to be ready.

West Virginia for sale

Bob Richmond taps his forefinger hard on the table in the dining room of "Fairfax Manor."

"The state should protect its citizens," he says in rhythm with the taps.

Sure, he'd sign over his mineral rights if the price was right, he says. But he won't do it through a landman.

McMahon, from the Surface Owners' Rights Organization, says, "If a lawyer is unethical, he loses his license. If a doctor is incompetent, he loses his license. If a CPA cooks the books, he loses his license. But if a landman is unethical, is incompetent and cooks the books, the next day he's still a landman."

Despite the lack of regulation in the industry and disparity between the going rate in the Marcellus versus other shales, leasing mineral rights can be profitable.

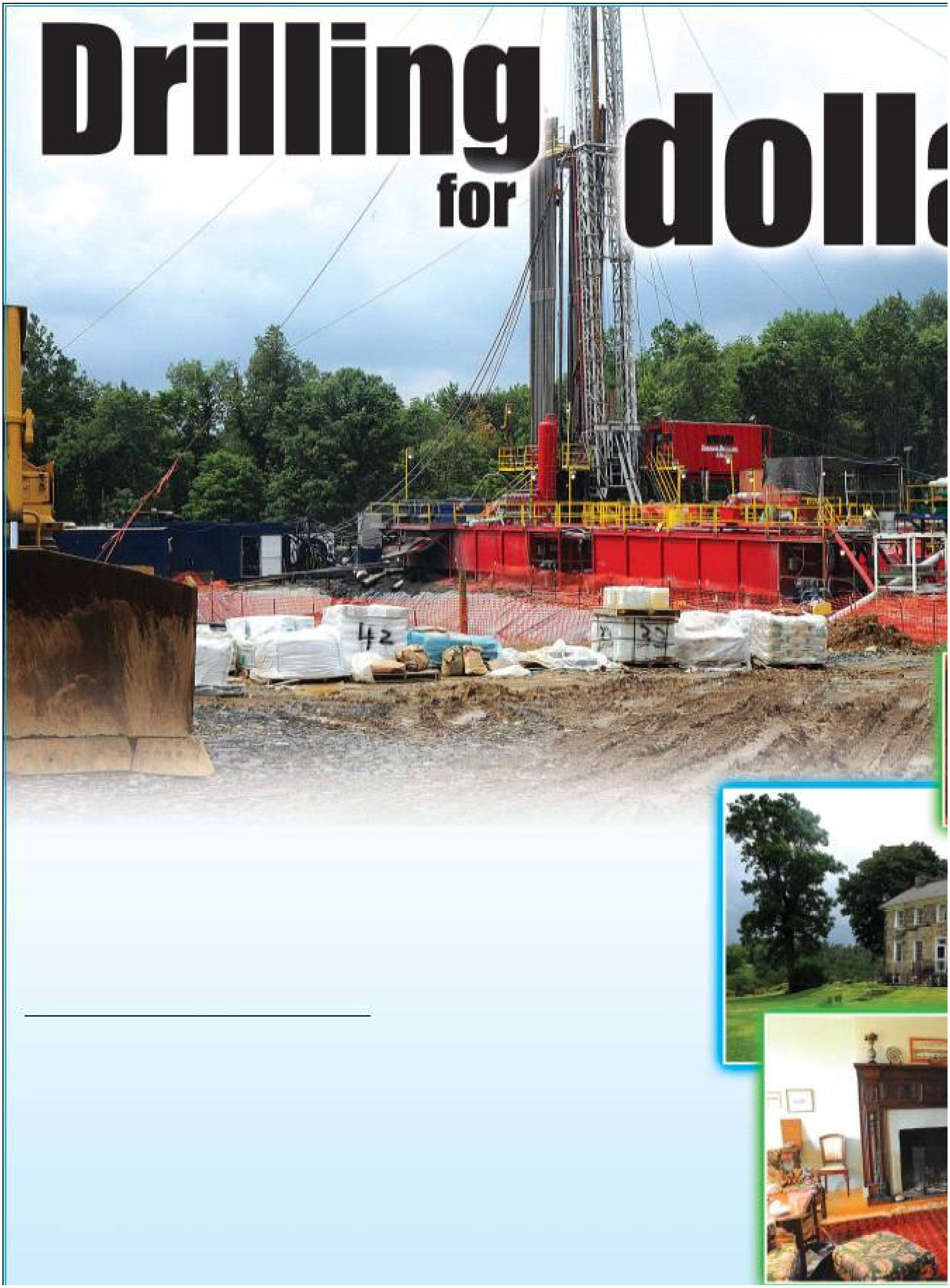
Keith Pitzer did it. He's an environmentalist, executive director of Friends of the Cheat, which for years has fought to keep the Cheat River watershed clean.

He says he got the price for the land and the percentage of royalties he wanted.

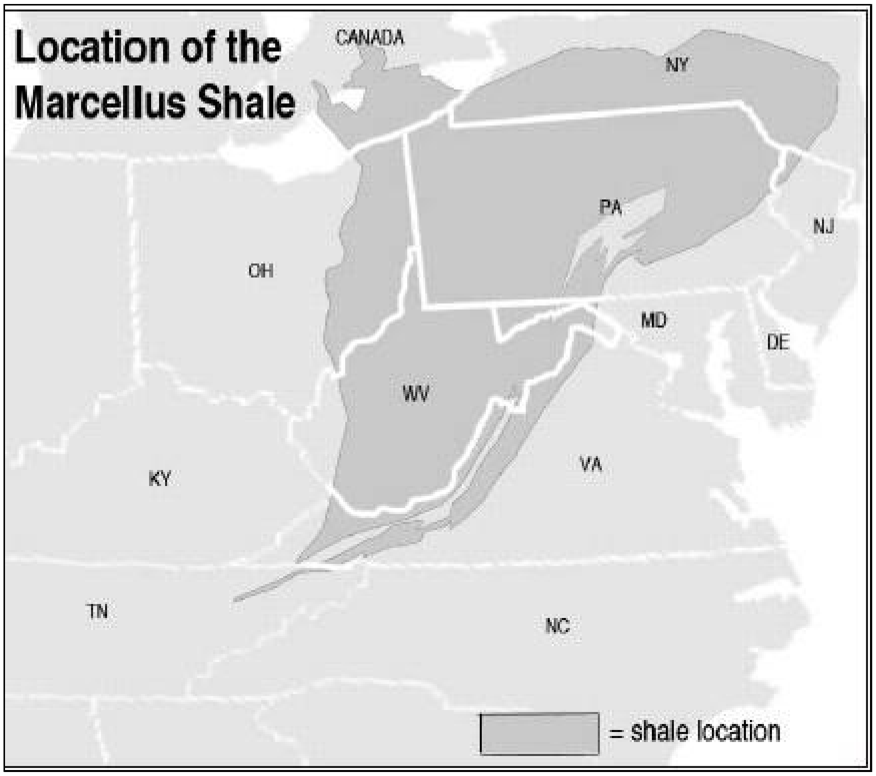
Though he wouldn't say what that price was, he did say it was "enough to help me make a decision."

He says it can be financially rewarding for him. He says his well won't destroy the environment any more than the dozens of others they'll drill around him.

Besides, he says, most people say it's safe. Then, with resignation, "Who do we believe ?"


Drilling
for
dolla

Ron Rittenhouse/The Dominion Post photos A large drilling rig taps into property along Coal Lick Road in Preston County. Bob Richmond and his wife, Caroline, (inset photos) have refused to lease the mineral rights of their 505 acres to energy companies. Eric J. Tomlinson/The Dominion Post photo illustration



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