IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

BLUE EAGLE LAND , LLC, a West Virginia limited liability company, **COALQUEST DEVELOPMENT, LLC.,** a foreign limited liability company, **CONSOLIDATION COAL COMPANY,** a foreign corporation, **HORSE CREEK LAND AND MINING COMPANY,** a West Virginia corporation, **NATIONAL COUNCIL OF COAL LESSORS, INC.,** a West Virginia corporation, **PENN VIRGINIA OPERATING COMPANY, LLC,** a foreign limited liability company, **POCAHONTAS LAND CORPORATION,** a foreign corporation, **WEST VIRGINIA COAL ASSOCIATION** a West Virginia non-profit corporation, **WPP LLC,** a foreign limited liability company, and **WOLF RUN MINING COMPANY,** a West Virginia Corporation,

Petitioners,

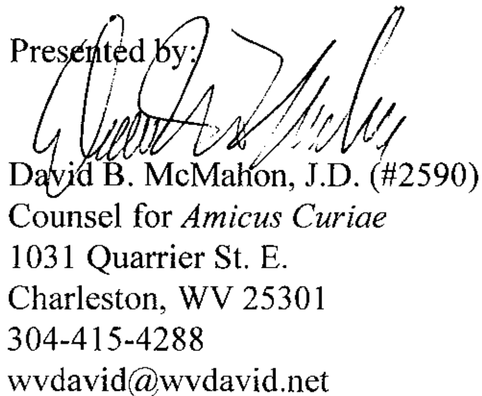
v. No. 072904

WEST VIRGINIA OIL & GAS CONSERVATION COMMISSION, a state agency, CHESAPEAKE APPALACHIA, LLC, a foreign limited liability company, **EASTERN AMERICAN ENERGY CORPORATION,** a West Virginia corporation, and **PETROEDGE RESOURCES (WV), LLC,** a foreign limited liability company,

Respondents.

BRIEF OF THE WEST VIRGINIA SURFACE OWNERS' RIGHTS ORGANIZATION AS AN *AMICUS CURIAE*

Presented by:



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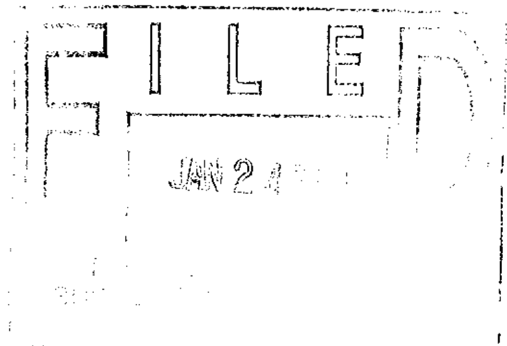

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W.Va. Code 22C-9-7-(b)(4)(1998) – Page 8 (Footnote 10).

W.Va. Code §22-21-15 (1994) – Page 7.

Miscellaneous:

Black's Law Dictionary, "Ferra Naturae" – Page 3.

39 C.S.R. 1- 4.3 and 4.3. – Page 7 (Footnote 8).

Donley, *The Law of Coal, Oil and Gas in West Virginia and Virginia*, 436 (1951) – Page 3 (footnote 3).

Transcript of May 17, 2007, hearing – Pages 5 (footnote 3), 11 and 12.

Willaims, Howard R. & Meyers, Charles J., *Oil and Gas Law*, Matthew Bender, "Pooling and Unitization" – Pages 2 and 4.

BRIEF

The underlying problem leading to this case is the ancient common law "Rule of Capture" that applies in West Virginia to the drilling of gas (and oil) wells. *See, Boggess v. Milam*, 127 W.Va. 654, 34 S.E. 2d 267 (1943).

Under the Rule of Capture a gas well can be drilled on the very edge of a mineral owner's tract. The outside edges of pools of gas pay no respect to the boundary lines between mineral owners. Even though it is known with certainty that this first gas well will drain gas from the gas bearing strata of the neighboring mineral owners' tracts, all the gas that comes out of the initial well belongs to the mineral owner where the well is located (and his lessee/driller/operator).

Not only is this legalized thievery, it results in less total gas being produced. This is true because the neighboring mineral owner, in order to prevent the first mineral owner from legally stealing his gas, will (if the economics are good enough) put down an "off set" well on his side of the boundary to try to get the same gas out first. There are now two wells, when one well would have been enough to get the gas out of the reservoir.

Those two wells will more quickly diminish the reservoir pressure that drives the gas up to the surface. The result is that the two wells together will produce less total gas than the one well alone would have produced! "Excessive drilling is wasteful, both in terms of the cost of drilling unnecessary wells (economic waste) and in terms of unnecessary and undesirable dissipation of native reservoir energy resulting in loss of

otherwise producible hydrocarbons (physical waste)." Howard R. Williams & Charles J. Meyers, *Oil and Gas Law*, Matthew Bender, "Pooling and Unitization" §905.1(1).

The result of extra wells recovering less total gas is that less total gas is produced.[1] Less gas produced means less gas sold. So the mineral owner gets less 1/8 royalty than he or she would have otherwise. The driller/operator's investors who helped pay to drill the well and get profits out of the other 7/8's, so they get less return on their investment. If the driller/operator keeps "an interest in the well" he or she will also get less (though many drillers/operators do not care about total production because they made their profit "on the push" – drilling the wells – for the investors and keep little or no interest in future income from the well). If credence is given to the economic theory that costs are always passed on to the consumer, then consumers will pay more for their gas. There will be twice this risk of environmental harm to the water aquifers as the wells are drilled. And surface owners will have twice as many wells drilled on them as are necessary.

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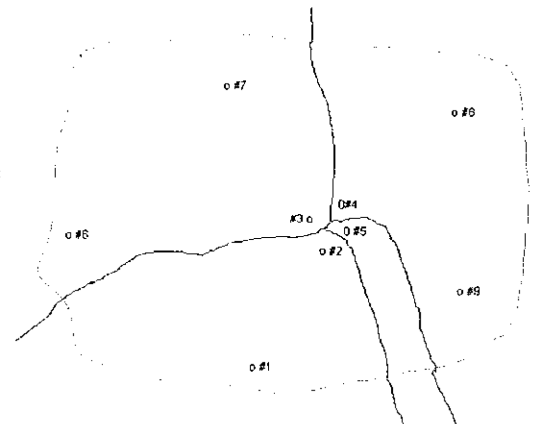
[1]A slide show that includes illustrations of scenarios caused by the Rule of Capture that result in unnecessary wells getting out less gas (but which are scenarios that have more wells than the simplistic two well example in the body of this brief) can be found on the web site of the West Virginia Surface Owner's Rights Organization, www.wvsoro.org, left pane, "Well Spacing and Royalty Sharing . . ."



The Rule of Capture evolved in the Middle Ages in England when the primary natural resource was venison. A deer would be born on one Lord's land, eat grass on a second Lord's land, and be killed on a third Lord's land. Law suits ensued to determine which Lord was entitled to the venison or what share of the venison. English courts opted for a bright line rule. The deer and its meat belonged to the Lord who "captured" the deer. "Ferra Naturae" the courts call it. "**Ferra naturae**...Of a wild nature or disposition. Animals which are by nature wild are so designated, by way of distinction from such as are naturally tame, the latter being called "domitae naturae." *Black's Law Dictionary*. *See*, *Acton v. Blundell*, 12 M&W 324, 152 E. R. 1223 (Ex. 1843).

The Rule of Capture was adopted for gas wells in this country when it was thought that oil and ran in underground rivers[2] and gas was a valueless byproduct[3].

Other states, who came to this problem later in time, solved this problem. They have enacted statutes that force well spacing and royalty sharing (called "pooling and unitization" here and in most statutes. *See* W.Va. Code §22C-9-7 (1998)). At least 31

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[2]"Our first cases seem based upon the theory that oil and gas are both of an inherently migratory or vagrant nature, and our later cases upon the notion that each has a fixed situs until disturbed or released by the act of man." *Boggess* at 127 W.Va. 659.

[3]"At the time this lease was drafted [1893], most drilling operations were primarily for oil. Gas wells were left uncontrolled to discharge into the air because profitable uses for natural gas were only then being discovered. See Donley, *The Law of Coal, Oil and Gas in West Virginia and Virginia*, 436 (1951). It is therefore not surprising that the standard legal form for a mineral lease at that time provided for a small lump-sum payment when natural gas was extracted. It is equally unsurprising to learn: "In modern leases it is frequently provided that gas shall be on a royalty basis, which, of course, is usually more profitable to the lessor." Donley, supra at 219." *McGinnis v. Cayton* 212 S.E.2d 765; 173 W.Va.102 (W.Va. 1984)

states have some form of well spacing and royalty sharing in at lest some circumstances. *Williams,* at §912. In this process oil or gas wells are required to be spaced for maximum production based on the porosity, permeability and other geologic properties of the formation. Each mineral tract owner being drained by a particular well receives a share of the royalty which the particular well produces. Each mineral tract owner's share of the royalty is based on the amount of acreage each mineral owner owns out of the total acreage being drained by the particular well[4]. *See* W.Va. Code §22C-9-7(b)(1). (The lessee/operator/driller and his investors also receive their proportionate share of the profit from drilling and producing the well, subject to increase or decrease depending on whether they "participate" in the drilling or the financing of the drilling. *See* W.Va. Code §22C-9-7(b)(3).

West Virginia only has forced well spacing and royalty sharing in three circumstances, and only then when an interested party "forces" the well spacing and royalty sharing. (In any other circumstance the mineral owners can still agree to well spacing and royalty sharing, but it generally cannot be "forced" upon them by a neighboring mineral tract owner, a royalty owner, etc. unless all the interested parties agree.)

The first circumstance in which West Virginia statutes provide for forced well spacing and royalty sharing is for gas wells which are defined by statute as "deep" wells.

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[4]This total acreage a well is expected to drain is called a "unit" in the statutes. Thus the term "unitization".

W.Va. Code 22C-9-1 *et seq.* Generally speaking these statutory deep wells are gas wells into or below the Onondaga formations. *See* below. There is no geological, engineering or other scientific basis for distinguishing between wells that are shallower or deeper than that formation.[5] The characteristics of that formation make it relatively easy for a driller to know when he has reached that formation based on "cutting" samples during drilling and "well logging" equipment.

The statute for forced well spacing and royalty sharing for statutory "deep wells" in West Virginia, and the demarcation line, was a legislative compromise between major well drillers and the independents. The major well drillers did not want to put a lot of money into exploring for and finding a new good place/formation to drill into, particularly a deeper, more expensive well, only to have an independent come along and "off set" that well and using the Rule of Capture legally steal the gas the major had found. So the major well drillers went to the Legislature to get a well spacing and royalty sharing statute.[6] The independents opposed them favoring the continuation of the Rule of Capture. A political compromise was worked out at the depth of the Onondaga group.

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[5] The enabling statute of the Oil and Gas Conservation Commission makes statements regarding public policy, but refers to no geologic, engineering or other reasons for the divide chosen. And indeed there are no more differences for drilling wells at depths below or above the Onondaga then there are for drilling wells at depths above and below the formations next above or next below the Onondaga, etc. W.Va. Code §22C-9-1 (1994).

[6]Note the "Exxon" deep well mentioned on page 35 of the transcript.

The second circumstance in which West Virginia statutes provide for forced well spacing and royalty sharing is where the gas wells will penetrate a coal seam, and the coal seam owner objects. See W.Va. Code §22C-8-1 *et seq.* Coal seam owners want the fewest possible number of wells through their coal seams. They were able to persuade the Legislature to enact forced well spacing (and the accompanying royalty sharing that had to come with it) in situations where the coal owner wanted it for wells through the coal seam owners' coal seams. The Shallow Gas Well Review Board is the agency that controls this process as laid out in the statutes above. Using the Shallow Well Review Board process for wells like those in question, the coal owner can force a minimum 1500 to 2000 foot well spacing for the wells in question.[7] Generally deep wells must be drilled

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[7]**§ 22C-8-8. Distance limitations**

(a) If the well operator and the objecting coal seam owners present or represented at the time and place fixed by the chair for consideration of the objections to the proposed drilling location are unable to agree upon a drilling location, then the written order of the board shall direct the director to refuse to issue a drilling permit unless the following distance limitations are observed:

(1) For all shallow wells with a depth less than three thousand feet, there shall be a minimum distance of one thousand feet from the drilling location to the nearest existing well as defined in subsection (b) of this section; and

(2) For all shallow wells with a depth of three thousand feet or more, there shall be a minimum distance of one thousand five hundred feet from the drilling location to the nearest existing well as defined in subsection (b) of this section, except that where the distance from the drilling location to such nearest existing well is less than two thousand feet but more than one thousand five hundred feet and a coal seam owner has objected, the gas operator shall have the burden of establishing the need for the drilling location less than two thousand feet from such nearest existing well. Where the distance from the drilling location proposed by the operator or designated by the board to the nearest existing well as defined in subsection (b) of this section is greater than two thousand feet, distance criterion will not be a ground for objection by a coal seam owner.

3000 feet apart[8], unless the Oil and Gas Conservation Commission makes an exception for an individual well or a whole field, which it did in the case at bar, requiring only 1000 foot minimum spacing as a "special field rule".

For deep wells it is the Oil and Gas Conservation Commission that determine and force the pooling and unitization of deep wells if the mineral owners can't agree on how to space the wells and divide the royalty and the cost and profit of drilling the well. (An interested party has to make an application to the Commission for this to occur.)

The third circumstance in which West Virginia statutes provide for forced well spacing and royalty sharing is for coal bed methane wells. W.Va. Code §22-21-15 (1994). These wells are not generally relevant to the present case.

The current suit is over wells that produce gas from the "Marcellus" formation. The Marcellus formation is the formation that sits right on top of the Ononada formation group. Drillers say that using modern technology, in order to drill a well to produce gas from the Marcellus formation, some additional well bore, called a "rat hole", has to be drilled into the Onondaga about 75 feet. See the Petition in this case. The statute only allows "shallow" wells to penetrate the Ononada by 20 feet for the rathole. *See* below.

So, where does this leave everyone?

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[8]See 39 C.S.R. 1- 4.3 and 4.3.

The coal owners want the Marcellus wells to be statutory "shallow wells" in order that the coal owners can use the Shallow Gas Well Review Board to impose a minimum 1500 to 2000 foot well spacing whenever the coal owners want it.[9]

Some oil and gas drillers prefer to fall under the jurisdiction of the Oil and Gas Conservation Commission which will has given them closer spacing. They also want certainty that forced well spacing and royalty sharing does apply or does not. Some oil and gas drillers do not want forced well spacing and royalty sharing to apply.

The Oil and Gas Conservation Commission believes that well spacing and royalty sharing is by far the best public policy. It is absolutely right in that belief. So it exercises its jurisdiction whenever it can to impose forced well spacing and royalty sharing.

Surface owners also like forced well spacing and royalty sharing, since the result is fewer wells sites and access roads getting bulldozed on their lands! Also there is a requirement that the driller of a deep well must get new surface owner consent.[10] However, the State has followed legal authority that allows it to interpret this provision

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[9]The coal owners also complain that they only get publication notice when the Oil and Gas Conservation Commission deals with "deep" wells, but direct written notice for shallow wells through coal seams under the Shallow Gas Well Review Board. The problem would be ameliorated if the Oil and Gas Conservation Commission would distribute/publish its notices using the web site/services of the Department of Environmental Protection. Upon information and belief, it refuses to do this in order to bolster its view of itself as a separate agency. Also there are well known associations of the named parties. Written notice to the coal owners of a half a million acres would certainly be unworkable. And new legislation could certainly deal with the problem by allowing direct written notice and opt out requests for individual wells during the permit applications.

[10]W.Va. Code 22C-9-7(b)(4).

very narrowly and so does not often require it. *See, State ex rel Lovejoy v. Callahan,*576 S.E.2d. 246, 213 W.Va. 1 (W. Va., 2002) Albright concurring at W.Va. p. 7; *Ashland Exploration Inc. v Miller*, Kanawha County Circuit Court No. Misc. 82-17 (1985) Judge Smith.

Much of the problem is caused by the poor drafting technique used in the relevant definitions.[11] The statutory definition language includes wording that is also permissive language. This permissive language should not drafted into a statutory definition. The question then arises how this permissive language limits or expands the definition language, particularly when the definition is cross referenced by a complimentary definition. And here we are.

The most literal reading of the statute is that the wells that the drillers want to drill are not legal to drill. They are not literally deep wells. They are literally shallow wells,

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[11]The apparently identical definitions are contained in three places. W.Va. Code § 22-6-1 (g) and (r) (1994); W. Va. Code § 22C-8-2(8)and (21) (1994); and

§ 22C-9-2. Definitions

(a) Unless the context in which used clearly requires a different meaning, as used in this article:

. . .

(11) "Shallow well" means any well drilled and completed in a formation above the top of the uppermost member of the "Onondaga Group": Provided, That in drilling a shallow well the operator may penetrate into the "Onondaga Group" to a reasonable depth, not in excess of twenty feet, in order to allow for logging and completion operations, but in no event may the "Onondaga Group" formation be otherwise produced, perforated or stimulated in any manner;

(12) "Deep well" means any well, other than a shallow well, drilled and completed in a formation at or below the top of the uppermost member of the "Onondaga Group"; . . . [1994]

and shallow wells cannot have a rat hole deeper than twenty feet into the Onondaga.[12] That is a real mess for the petitioners.

What the Oil and Gas Conservation Commission has done with this mess is to try to get everyone out of this thicket of poorly drafted statutory enactments that incompletely solve the terrible public policy of the Rule of Capture. The Commission has said that these Marcellus wells are "deep" wells that can be drilled, but they are subject to well spacing and royalty sharing.[13]

The coal owners would probably have been able to live with this if the Oil and Gas Conservation Commission had declared the well spacing to be the 1500 or 2000 feet that the coal owners can impose on statutory "shallow wells". Surface owners would agree with them. The geology and science presented at the hearings before the Commission below did not justify the 1000 foot spacing granted. And that could be up to 9 gas wells per 100 acres of surface owner's land! Indeed, the evidence presented to the

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[12]The Petitioners lean strongly on the term "completed". Petition page 23. They state, "[A] well completed in only the Marcellus formation will produce gas from no other formation other than the Marcellus formation." This may well be the intention of someone "treating" the Marcellus formation by fracturing the rock in order to get the gas to flow to the well bore more quickly along the fractures in the intended formation. "Fracing" however may not always be so tamed, and the fractures may go above and, importantly here, below the target formation. The fractures may produce gas from the locations of those fractures outside the target formation too, should gas be there. So there is no guarantee that a well "fraced" in the Marcellus will not produce from the Onondaga.

[13]The Petitioners suggest that the Office of Oil and Gas has the power to grant a variance to the 20 foot limitation in the definition. Since the limitation is in a definition, a question arises whether the limitation is a "requirement" for which a variance can be granted. Also the definition is found in three statutes, and technically the Office of Oil and Gas may not have authority regarding definitions in the authorizing statues of independent boards.

Commission below by the parties seeking the spacing was that the 1000 spacing was "arbitrary". Transcript of May 17, 2007, hearing, page 48.

The witnesses for the parties seeking the spacing order testified that they had 1,700 well sites planned based on 1500 foot spacing (Tr. 47) which is their current practice (*ibid.*). They only want 1000 foot spacing to, "allow us flexibility for topography issues, coal owner/surface owner issues, and also we have a lot of existing wells in the area that we would be drilling deeper . . . to Marcellus." Tr. p. 46. Proceeding based upon this rationale perverts the purpose of well spacing and royalty sharing.

Spacing of 1500 feet is not what they requested and not what the order granted. The order provided 1000 foot spacing. It grants 1000 foot spacing for every well, not just if there is a surface owner, coal operators or redrilling issue! They can state that their plans are for 1500 foot spacing. But if the order stands, they cannot be held to it. They can space all wells at 1000 feet.

Indeed, the geologic basis for the 1500 foot spacing was thin. There have been no reservoir studies done. Tr. 49.

It was arbitrary for The Commission to grant spacing any less than 1500 feet. If there is a need for closer spacing for a particular well, they can ask for the variance.

So what should The Supreme Court do with this mess?

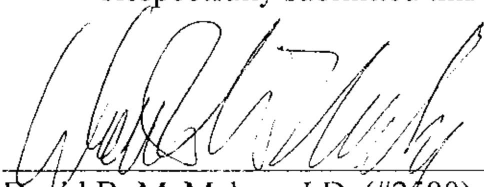
The Court should dismiss the appeal as improvidently granted. This quarrel over The Marcellus wells should be put in perspective. The coal owners live with the statutory

regime for "deep" wells for all of the many wells drilled to all of the many deeper formations. The oil and gas owners live with the statutory regime for "shallow" wells for all the many wells to all of the many shallower formations. It is only about this one formation. Let the agency do its job.

In the alternative, when interpreting the statutory definitions in question, the Supreme Court should give deference to the agency charged with enforcing this law, the Oil and Gas Conservation Commission. *See, Appalachian Power Company vs. State Tax Department of West Virginia* 466 S.E.2d. 424 (W.Va. 1995). It should honor the Commission's interpretation of its law and find that Marcellus wells with ratholes deeper than 20 feet are "deep wells". And if the result makes no one happy, that may be the best result. It will force them to go to The Legislature where the law of West Virginia can be dragged, literally, out of The Dark Ages. It will hopefully force the interested parties to move toward well spacing and royalty sharing for all gas and oil wells.

In the alternative, The Supreme Court should reverse the order of 1000 feet and either send it back for further consideration, or order the spacing be 1500 feet, The only spacing for which there was any scientific basis. The 1000 foot spacing is arbitrary. For this case's particular of the issues, that is the true crux for coal owners, and for surface owners, as well as for investors, consumers and even operators as a class.

Respectfully submitted this 24th day of January, 2008.



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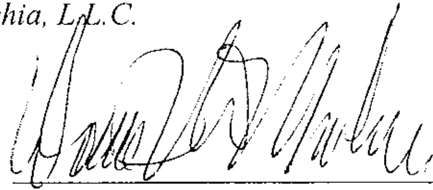

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CERTIFICATE OF SERVICE

I, David B. McMahon, counsel for the West Virginia Surface Owner's Rights Organization, do hereby certify that a true and exact copy of the foregoing Brief of the West Virginia Surface Owners' Rights Organization As an *Amicus Curiae* has this 24th day of January, 2008, been served upon the following parties, via U.S. Mail, addressed as follows:

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