

NORTH DAKOTA LAW REVIEW
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Litigation Update

North Dakota Law Review Symposium

April 11, 2019

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TOPICS COVERED

- Deduction of Gas Processing Costs – *Newfield Exploration Company v. State of North Dakota*, Case No. 27-2018-CV-00143, Order Dated February 14, 2019
- Use of Pore Space – *Mosser v. Denbury Resources, Inc.*, 2017 ND 169, 898 N.W.2d 406
- Industrial Commission Jurisdiction Over Well Costs – *Continental Resources, Inc. v. Counce Energy BC #1, LLC*, 2018 ND 10, 905 N.W.2d 768
- Extensions and Renewals – *Pitchblack Oil, LLC v. Hess Bakken Investments II, LLC*, 2018 WL 1189879 (D.N.D. Mar. 7, 2018)
- Privity in Quiet Title Actions– *Gerrity Bakken, LLC v. Oasis Petroleum North America, LLC*, 2018 ND 180, 915 N.W.2d 677
- Other recent cases of note

Deduction of Gas Processing Costs – *Newfield Exploration Company v. State of North Dakota*

□ Background

- ▣ Newfield leased State-owned mineral interests on the State's lease form with the following language:
 - C. Lessee agrees to pay lessor the royalty on any gas, produced and marketed, based on gross production or the market value thereof, at the option of the lessor, such value to be based on gross proceeds of sale where such sale constitutes an arm's length transaction. (emphasis added)

Deduction of Gas Processing Costs – *Newfield Exploration Company v. State of North Dakota*

- Newfield entered into arms-length percentage of proceeds contracts with Oneok for sale of gas
 - ▣ Under these contracts, Newfield sold the gas at the wellhead and Oneok paid Newfield a percentage (70%-80%) of the net proceeds Oneok received from the resale of gas after netting post-production costs
- Newfield paid the State's royalties based on amounts it received from Oneok without deductions from Newfield

Deduction of Gas Processing Costs – *Newfield Exploration Company v. State of North Dakota*

- The State asserted the lease required gross proceeds be calculated by multiplying gross production by the sales price Oneok received for the sale of gas
- Newfield asserted the leases required gross proceeds be calculated by multiplying gross production by the sales price Newfield received for the sale of gas to Oneok

Deduction of Gas Processing Costs – *Newfield Exploration Company v. State of North Dakota*

□ Holding

- “The plain language requires payment based on ‘gross proceeds of sale.’ The court does not find the contract terms ambiguous. The lease is between Newfield and the State, not the State and Oneok, or some other third party gas processor. This lease, drafted by the State, requires Newfield to pay based on the gross proceeds it receives from the sale of gas. The State's argument strains the language beyond reason and this court is not persuaded, on the facts of this case, that Newfield is required to pay based on what a third party receives for the processed gas. If that is what the State intended back in 1979 when the lease was revised, it could have easily stated so.”

Pore Space –

Mosser v. Denbury Resources, Inc.

Background

- Mossers owned surface estate burdened by an oil and gas lease executed in favor of Denbury's predecessor
- Denbury converted an old oil well located on the Mossers' property into a saltwater disposal well
- Mossers agreed Denbury had right to dispose of saltwater produced from wells located within the unitized area, leaving only the measure of damages for Denbury's use of the pore space beneath the Mosser's property

Pore Space –

Mosser v. Denbury Resources, Inc.

- Mossers sought damages under North Dakota’s Oil and Gas Production Damage Compensation Act, N.D.C.C. ch. 38-11.1
- N.D.C.C. § 38-11.1-04 entitles landowners to damages equal to “lost land value,” “lost use of and access to the surface owner’s land,” and other factors
- Judge Miller certified seven questions to the North Dakota Supreme Court regarding (1) pore space ownership; (2) compensability of pore space use under N.D.C.C. ch. 38-11.1; and (3) various evidentiary related issues

Pore Space –

Mosser v. Denbury Resources, Inc.

Holding

- Absent some conveyance, surface owner owns pore space
- Surface owner entitled to damages for “lost land value” and “lost use of and access to land” arising from pore space use
- Surface owner is not required to demonstrate that it is currently using or is likely to use the pore space
- Damages are not limited to a diminution in market value
- Price per barrel others are paying for saltwater disposal may provide some probative evidence of damages for “lost use of and access to the surface owner's land”

Pore Space – *Mosser v. Denbury Resources, Inc.*

- Legislative Update – S.B. 2344
 - ▣ Contains provisions regarding use of pore space for natural gas and CO2 storage and EOR purposes
 - ▣ S.B. 2344 adds a new definition to N.D.C.C. § 38-11.1-03 for the term “land”
 - “‘Land’ means the solid material of earth, regardless of ingredients, but excludes pore space.”
 - ▣ Currently in conference committee

Industrial Commission Jurisdiction Over Well Costs – *Continental Res., Inc. v. Counce Energy*

Background

- Continental sued Counce, a participating working interest owner, seeking to foreclose a production lien under N.D.C.C. § 38–08–10 for unpaid JIBS amounting to \$180,000
- After discovering accounting problems, Continental amended its complaint to include claims for breach of contract, unjust enrichment, and account stated, requesting \$160,000
- Counce alleged costs sought weren't reasonable actual costs
- Case went to trial - jury awarded Continental \$154,000

Industrial Commission Jurisdiction Over Well Costs – *Continental Res., Inc. v. Counce Energy*

Holding

- District court lacked subject matter jurisdiction over all claims for want of administrative exhaustion
 - While an operator may place and foreclose a lien on a non-operator's share of production, that statutory scheme doesn't allow an action for breach of contract to collect "reasonable actual cost" of drilling or any claim inextricably intertwined
- Where "reasonable actual costs" are in dispute, the Industrial Commission must determine that issue before a district court has jurisdiction

Extensions and Renewals – *Pitchblack Oil, LLC v. Hess Bakken Investments II, LLC*

Background

- Pitchblack owned ORRI burdening Bottom Leases “or any extensions or renewals thereof entered into within 180 days of expiration of the applicable [Bottom] Lease.” (emphasis added)
- Majority WI interest owner in the Bottom Leases acquires Top Leases covering same interests, which would expand WI if vested
 - ▣ Different terms, including royalty amounts and primary term lengths
 - ▣ Also contained new bonus consideration
- Production ceased on certain tracts, vesting some of the Top Leases
- Hess acquires nearly all of the WI in both Bottom Leases and Top Leases. Pitchblack asserts that its ORRI burdens the Top Leases

Extensions and Renewals –

Pitchblack Oil, LLC v. Hess Bakken Investments II, LLC

Holding

- Because an ORRI derives from a lease, the ORRI generally doesn't survive expiration of that lease absent a special relationship, bad faith, or by contract
- Without any allegation of any special relationship or bad faith between Hess and Plaintiffs, the ORRI survived the Bottom Leases only if the Top Leases were “extensions” and/or “renewals” of the Bottom Leases
 - Renewal and extension involve continuation of the relationship on essentially the same terms and conditions as the original contract

Extensions and Renewals – *Pitchblack Oil, LLC v. Hess Bakken Inv. II, LLC*

- None of the Top Leases were extensions or renewals of the Bottom Leases, so the ORRI did not burden them
 - ▣ Top Leases lack significant similarity to the Bottom Leases so as to be considered extensions or renewals because of the differing royalty amounts, primary terms, and additional bonus consideration
- Appeal pending before the Eighth Circuit, Case No. 18-1737
- Disclaimer: Crowley Fleck PLLP represents Hess in this case

Privity in Quiet Title Action – *Gerrity Bakken, LLC v. Oasis Petroleum N. Am., LLC*

□ Background

- ▣ Competing mineral interest owners brought quiet title action and the district court ruled against Gerrity Bakken’s lessors, who didn’t appeal
- ▣ Gerrity Bakken initiated a second quiet title action seeking to quiet title to its leasehold interest derived from the quieted mineral interests

Privity in Quiet Title Action – *Gerrity Bakken, LLC v. Oasis Petroleum N. Am., LLC*

□ Holding

- Unless one is a party to a proceeding or in privity with those who are parties to an action, he cannot be bound by the judgment in that action, but privity is inapplicable if the rights to property were acquired before the adjudication
- Because Gerrity Bakken acquired its interest prior to the first action and was not named as a party in that action, Gerrity Bakken was not bound by the judgment

But see N. Oil & Gas, Inc. v. EOG Res. Inc., Case No. 1:16-cv-388 (D.N.D.) Order Dated January 15, 2019

□ **Background**

- ▣ Northern and EOG's lessors brought quiet title action against one another regarding disputed mineral interest; district court ruled in favor of EOG's lessors
 - Northern's lessor appealed; North Dakota Supreme Court affirmed in *Johnson v. Finkle*, 837 N.W.2d 132 (N.D. 2013)
- ▣ Northern brought quiet title action against EOG to quiet title to their leasehold interests derived from the quieted mineral interests

But see N. Oil & Gas, Inc. v. EOG Res. Inc., Case No. 1:16-cv-388 (D.N.D.) Order Dated January 15, 2019

□ **Holding**

- *Gerrity Bakken* did not alter traditional notions of privity focusing on “fundamental fairness” and not “defeat[ing] the ends of justice”
- Because Northern’s interests were aligned with its lessors, and because Northern’s lessors extensively litigated title ownership, Northern’s interests were adequately protected, rendering Northern in privity with its lessors and binding Northern
- Appeal pending before the Eighth Circuit, Case No. 19-1326

Additional Cases of Note

- *Dale Exploration, LLC v. Hiepler*, 2018 ND 271, 920 N.W.2d 750
 - ▣ Specific performance is the presumptive remedy for breach of a contract to convey real property, including mineral interests
 - Disclaimer: Crowley Fleck PLLP represented certain defendants in this case

Additional Cases of Note

- *Johnson v. Statoil Oil & Gas LP*, 2018 ND 227, 918 N.W.2d 58
 - ▣ Specific language in a lease addendum will prevail over form language if the two cannot be reconciled
 - Disclaimer: Crowley Fleck PLLP represented certain defendants in this case

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