Section of Environment, Energy, and Resources
AMERICAN BAR ASSOCIATION

Mining and Mineral Extraction Committee Newsletter

Vol. 9, No. 1 August 2015

MESSAGE FROM THE EDITORS

Jamie Auslander and Gerald George

The latest issue of the ABA Mining and Mineral Extraction Committee Newsletter follows below. We thank the authors for preparing their contributions.

We are now soliciting articles for the next issue of the committee newsletter to be published this Fall/Winter. Articles can range anywhere from a few paragraphs to a few pages on topics covering substantive areas of mining law and practice tips. Examples of articles include updates on new mining legislation or regulation, analysis of recent case law affecting the mining industry, and insight on aspects of existing mining law. If you are interested in contributing an article, please send an e-mail to the Newsletter Co-Vice-Chairs Jamie Auslander (jauslander@bdlaw.com) and Gerald George (geraldgeorge@dwt.com) indicating what you would like to write about.

We hope you enjoy the newsletter and we look forward to receiving your future topic suggestions!

DORMANT NO MORE: FRACKING BOOM CAUSES STATES TO REVISIT DORMANT MINERAL STATUTES

Janna A. Aginsky and Frank Erisman
Schwabe, Williamson & Wyatt, P.C.
Portland, Oregon

As technological advances of the last decade opened up previously inaccessible oil and gas reserves, surface and mineral owners turned to existing state mineral rights abandonment statutes for guidance in determining their respective rights to the newly valuable oil and gas resources. Dormant mineral statutes were enacted in many states to address the problem of fractionalized and unproductive mineral interests interfering with the development of mineral or surface estate. These statutes set forth a procedure for clearing title of such dormant mineral interests and the current fracking boom brought them into the spotlight once again. This article examines the recent interpretation of Ohio and North Dakota dormant mineral statutes to determine emerging legislative and judicial trends regarding the potential of these obscure laws to clarify, or simplify, mineral ownership. We also give a brief overview of the Oregon and Washington dormant mineral statutes to highlight their key elements and some blind spots. Our goal is to assist practitioners in states where dormant mineral statutes have been little used to gain some insight as to how their state legislation might be interpreted.

Continued on page 3.

Mining and Mineral Extraction
Committee Newsletter
Vol. 9, No. 1, August 2015
Jamie Auslander and Jerry George, Editors

In this issue:

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SECTION OF ENVIRONMENT, ENERGY, AND RESOURCES

CALENDAR OF SECTION EVENTS

September 24, 2015
Current Hot Topics in Climate Change Law
CLE Webinar

October 1-2, 2015
36th Public Land Law Conference. Transcending Boundaries: Achieving Success in Cooperative Management of Natural Resources
Primary Sponsor: Public Land & Resources Law Review, University of Montana School of Law

October 28-31, 2015
23rd Fall Conference
Chicago, IL

November 19, 2015
Overview of Intellectual Property Law Affecting Farmers, Agri-Businesses and Food Entrepreneurs
Primary Sponsor: Solo, Small Firm, & General Practice Division

March 29-30, 2016
34th Water Law Conference
Austin, TX

March 30- April 1, 2016
45th Spring Conference
Austin, TX

October 5-8, 2016
24th Fall Conference
Denver

For full details, please visit www.ambar.org/EnvironCalendar

Continued from page 1.

Summary

A severed mineral interest in land is considered "dormant" when it has been inactive for a specified period of time. If the mineral interest is dormant, anyone interested in developing the minerals may find it difficult or impossible to obtain development rights from the missing or unknown owners. Surface owners wishing to develop their property may find the marketability of their estate significantly impaired and the development effectively precluded if the title is not cleared of the dormant mineral rights. The dormant mineral statutes solve this problem by providing for a termination of severed mineral interests after a certain period of non-use and, typically, for the vesting of such mineral rights in the surface owner. The constitutionality of the dormant mineral statutes allowing for extinguishment of abandoned mineral interests was challenged in a few states, but the issue appears to be settled, at least for the time being, by *Texaco Inc. v. Short*, 454 U.S. 516 (1982), which upheld the constitutionality of the Indiana Dormant Mineral Interests Act. Today, roughly half of the states have enacted one or another form of a dormant mineral statute, with significant variations concerning the types of minerals that are covered and the procedure required for extinguishment of the dormant interest. In 1986, the National Conference of Commissioners on Uniform State Laws drafted the Uniform Dormant Mineral Interest Act (the "Model Act") but only one state, Connecticut, followed the Model Act's format in enacting its dormant mineral statute.

None of the recent cases that came out of Ohio and North Dakota, the two states where dormant mineral statutes have undergone the most scrutiny in the past few years, questioned the constitutionality of these statutes. Rather, these cases have had more to do with the statutory mechanism for extinguishing abandoned mineral interests, i.e., whether notice to the mineral owner has been properly given or the statutory process has been otherwise followed, and with clarifying the meaning of statutory "savings events" that prevent the finding of mineral right abandonment. Some of these issues have now made their way up to the Ohio Supreme Court and stakeholders in that state are waiting for the court's guidance regarding the process they need to follow. In North Dakota, the courts and legislators perfected their dormant mineral statute by adding a very helpful definition of the "reasonable inquiry," required by statute to locate the absentee mineral owner, but left some ambiguity as to when such reasonable inquiry is required. In Oregon and Washington, the courts have yet to interpret their dormant mineral statutes, but it is foreseeable that lack of a definition of "due diligence," a requirement incorporated in both statutes for efforts to locate the mineral owner, may present issues for litigation.

I. Questions from Ohio: Notice and Cure or Notice Only?

Ohio, as a home to the Marcellus and Utica shale plays, has seen the most recent judicial activity on the application of its dormant mineral statute. The Ohio Dormant Mineral Act, Ohio Rev. Code Ann. § 5301.56, *et seq*. (2014) (ODMA), was enacted in 1989 as a self-executing statute, i.e., it provided that noncoal mineral interests automatically vested in the surface owner if no specifically identified savings event had occurred within the preceding twenty years. The original ODMA did not require that the surface owner attempt to locate or identify the mineral owners before the mineral interest was deemed abandoned. In 2006, the legislature changed the law by adding a notice procedure that the surface owners must follow to claim abandonment. The surface owner in Ohio is now required to give the mineral owner notice of the intent to have the mineral interest declared abandoned, by service or publication. To preserve the mineral interest, the mineral owner, within sixty days from the date the notice is served or published, must file with the county recorder either an affidavit describing a savings event that occurred within twenty years preceding the notice or a claim to preserve the mineral interest. This procedure was called into question in *Dodd et al. v. Croskey et al.*, Slip Opinion No. 2015-Ohio-2362, where the Ohio Supreme Court was asked to decide, *inter alia*, whether filing of a claim to preserve a mineral interest under the statute in response to a surface owner's notice of intent to declare the mineral interest abandoned is sufficient to preserve a mineral interest or whether the mineral owner must also prove that a savings event occurred within twenty years preceding such notice. This question was answered last month, when the court ruled that a claim to preserve a mineral interest, if filed within the sixty-day statutory period, is sufficient to preclude the mineral interest from being deemed abandoned, confirming that a postnotice cure is allowed under the ODMA. This decision will no doubt be determinative for the outcome of many quiet title actions currently pending in various Ohio courts. It also shifts the expense of identifying potentially valuable mineral resources and their owners to the surface owners (assuming those surface owners deem it cost effective to engage in the exercise at all), while easing the mineral owners' burden of safeguarding their mineral assets.

In a handful of other cases currently under review by the Ohio Supreme Court, the court is asked to interpret various other provisions of the ODMA and to decide if and when the self-executing 1989 version of the ODMA can be invoked to declare mineral rights automatically abandoned and vested in the surface owner. As of the date of this publication, lower courts and practitioners in Ohio and elsewhere are still awaiting guidance from the court on at least a dozen questions of ODMA law.

The ODMA and recent litigation surrounding it highlight several important features of the dormant mineral statutes that come into play during the statute's application, among them: (1) preabandonment notice requirements (what actions need to be taken, if any, to identify and notify the mineral owner?); (2) opportunity to cure (can mineral owner preserve its rights after the surface owner expends time and resources to file the notice of intent to declare abandonment?); (3) trigger of the statutory look-back period during which the savings event must have occurred (passage of the statutory period in a self-executing statute, or filing of the notice of intent to declare abandonment?); and (4) definition of a savings event that precludes a finding of abandonment. Some of these features are specific to the Ohio statute, but a few (e.g., notice requirements and savings event definition) are shared by many other dormant mineral statutes and the examination of these features by the Ohio Supreme Court in 2015 should provide guidance to practitioners in other states as well as to Ohio practitioners.

II. Lessons from North Dakota: Due Diligence Defined

The oil boom in North Dakota similarly has caused renewed judicial and legislative scrutiny of the state's dormant mineral statute, N.D. Cent. Code § 38-18.1, *et seq*. (2013).This statute provides that a mineral interest, if unused within a twenty-year period, is deemed abandoned and may be acquired by the surface owner. The notice requirement of the North Dakota statute provides that notice to the mineral owner must be given by publication, but if the address of the mineral owner is shown of record, or can be determined upon "reasonable inquiry," notice must also be given by mailing a copy of the notice to the mineral owner within ten days after the last publication is made.

Three North Dakota Supreme Court cases examined the notice requirement and held that the surface owner is required to conduct a "reasonable inquiry" under N.D. Cent. Code § 38-1831-06(2) only if the mineral owner's address does not appear of record, even if the surface owner had actual knowledge that the address of record was incorrect. *See Sorensen v. Felton*, 793 N.W.2d 799 (N.D. 2011), *Sorenson v. Alinder*, 793 N.W. 2d 797 (N.D. 2011), and *Johnson v. Taliaferro*, 793 N.W.2d 804 (N.D. 2011).This year, in *Capps v. Weflen*, 855 N.W.2d 637 (N.D. 2014), the Supreme Court went even further to hold that notice to the address of record was correctly made even though the surface owners had knowledge that the mineral owner had died. These three cases, however, interpreted the version of the North Dakota dormant mineral statute in effect prior to the statute's 2009 amendment. The 2009 amendment muddied the waters somewhat by adding a provision allowing a surface owner to maintain an action to quiet title to minerals and requiring such owner to "submit evidence to the district court establishing that all procedures required by this chapter were properly completed *and* that a reasonable inquiry […] was conducted." N.D. CENT. CODE § 38-18.1-06.1.2 (emphasis added). Now, if the surface owner initiates the statutory process under the 2009 version of the statute, it seems that the surface owner could be required to conduct reasonable inquiry even if the mineral owner's address appears of record.

The North Dakota law, unlike many other dormant mineral statutes, defines "reasonable inquiry."N.D. CENT. CODE § 38-1831-06(6) requires the surface owners to conduct a search of (1) the county recorder's records for the existence of any uses defined in the statute by the mineral owner; (2) the clerk of court's records for the existence of any judgments, liens, or probate records which identify the mineral owner; (3) the social security death index for the last-known residence of the mineral owner, if deceased; and (4) one or more public internet databases to locate or identify the mineral owner or any known heirs of the owner. By adding a definition of "reasonable inquiry" to the dormant mineral statute, the North Dakota legislators provided much needed clarity to what could otherwise be an ill-defined, time-consuming, and expensive process of identifying and notifying absentee mineral owners.

This clarity is helpful since, in the current internet age, the concept of proper notice is evolving the ease with which absent owners can be found via online resources. If the mineral owner has truly abandoned the interest as the result of death, movement from the area or state, or failure to pay real estate taxes (if assessed), then the actual intent of the dormant mineral statute can be achieved. It would seem to us that if the mineral owner is merely out of touch but can be found with "due diligence" or "reasonable inquiry" then the intent of these statutes is also achieved; that is, the dormant interest becomes active and the mineral owner can exercise its ownership rights.

III. All Is Quiet on the Western Front

Meanwhile, in the Pacific Northwest, the dormant mineral statutes remain dormant. The Oregon Dormant Mineral Interest Act, OR. REV. STAT. § 517.180 (2013), was enacted in 1983 and, aside from minor amendments, has been unaltered since 1999. The State of Washington statute, WASH. REV. CODE § 78.22 020 *et seq*. (2014), was enacted in 1984 and has not been revisited by the legislature or examined by the courts since. The restrictive nature of both the Oregon and Washington statutes (requiring notice to be given to the mineral owner by publication and imposing the due diligence burden upon the surface owner to locate the mineral owner to give such notice) effectively may preclude these statutes from being of much use in extinguishing what the surface owner originally perceived to be dormant mineral rights.

In Oregon, a mineral interest that is more than thirty years old can be extinguished by the surface owner unless the mineral owner, within the last thirty years, has recorded a statement of claim in the manner prescribed by the statute. To extinguish the mineral interest that is presumed to be dormant, the surface owner in Oregon must (1) notify the current mineral owner by publishing a notice of lapse of the mineral interest and, if the address of the mineral owner is known or can be determined by "due diligence," by mailing this notice to such owner; and (2) record an affidavit of publication with a copy of the notice and a statement of claim with the county clerk. The notice of lapse of the mineral interest must be published at least once each week for three consecutive weeks in a newspaper of general circulation in the county in which the land affected by the mineral interest is located. If the surface owner gives notice as required by the statute and submits a copy of the notice and the affidavit of publication for recording, the mineral interest of the mineral owner will be extinguished and become the property of the surface owner, unless the mineral owner submits a statement of claim to the county clerk within sixty days after the date of the last publication of the notice.

In Washington, a mineral interest, if unused for a period of twenty years, may be extinguished by the surface owner by following the procedure set forth in WASH. REV. CODE §§ 78.22.050 and 78.22.060. If the mineral interest in question is dormant (that is, if none of the savings events identified in the statute have occurred), the procedure for extinguishing the mineral interest in Washington follows the same general two-step process as in Oregon: notice and recording of the statement of claim. To begin the process, the surface owner must provide sixty days' notice of intention to file a claim of abandonment and extinguishment of the mineral interest to the current mineral owner. Such notice must occur by personal service or registered mail to the last known address of the current mineral owner. The county treasurer is required to supply the name and address of the current mineral owner as they appear on the county property tax records to the surface owner without charge. If the current mineral owner is unknown to the county treasurer and the current mineral owner cannot be determined after "due diligence", the surface owner must serve the notice upon the current mineral owner by general publication. It is unclear whether the surface owner that mailed the notice to the mineral owner's last known address provided by the county treasurer still has to conduct "reasonable inquiry" under the Washington statute or, similarly to the North Dakota pre-2009 statute, the surface owner's obligation to locate the owner ends there and Washington courts may have to grapple with this issue in the future.

As in Oregon, the notice of lapse of mineral interest in Washington must be published at least once a week for three consecutive weeks in a newspaper of general circulation published in the county in which the property interest is located.

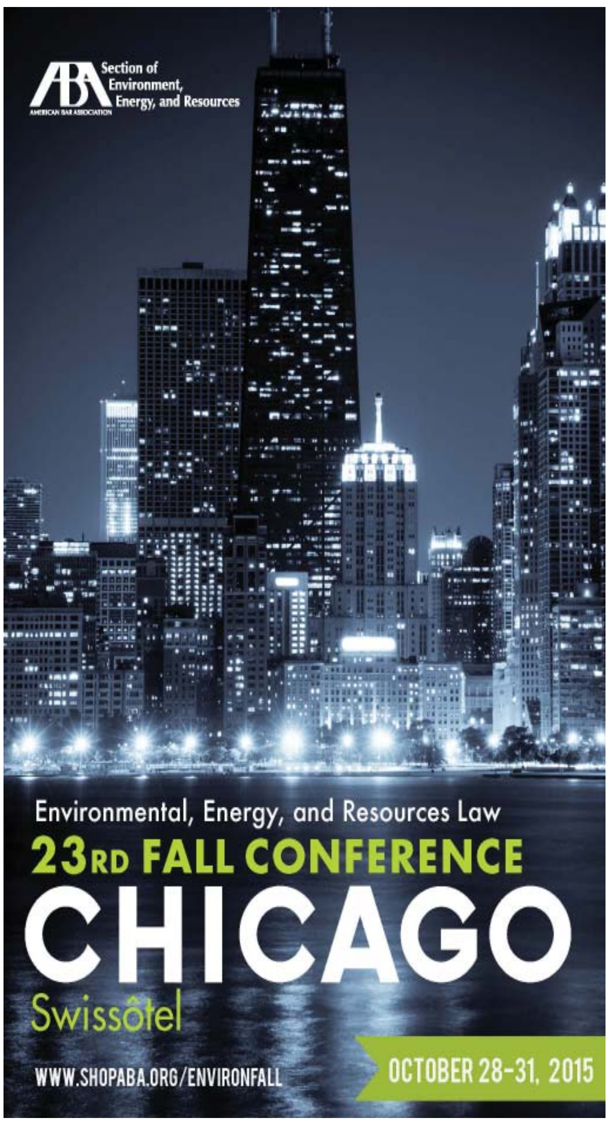
The Washington statute provides more guidance on what should be done if there is no newspaper of general circulation in the county where the interest is located; in such circumstances the notice must be published in a newspaper of general circulation published in an adjoining county, and if no such newspaper exists in an adjoining county then in a newspaper of general circulation published at the capital of the state.

The term "due diligence" is not defined in either Oregon and Washington statutes and there are no cases in either jurisdiction interpreting this term in the context of dormant mineral interest extinguishment. In the absence of the developed case law interpreting dormant mineral statutes in these states, the courts in Oregon and Washington might consider the North Dakota "reasonable inquiry" requirements informative in determining whether the due diligence requirement was satisfied. Similarly, in determining whether any of the savings events identified in WASH. REV. CODE § 78.22.030 occurred, the Washington courts might also look to the Ohio and North Dakota case law to see how those courts interpreted similar questions.

Conclusion

In Ohio and North Dakota, in reaction to increased mineral exploration and development, legislators and courts have reexamined the dormant mineral statutes and attempted, with varying degrees of success, to clarify the process used to extinguish abandoned mineral rights. While the dormant mineral statute will be different in each state and some states still have no laws on the books dealing with abandoned minerals, the latest litigation and legislative activity in states such as North Dakota and Ohio is informative in understanding the application of these laws. The internal tension between protecting individual property rights while encouraging economic activity that is at the heart of the dormant mineral statutes is still evident in every court decision interpreting these statutes, and providing procedural clarity and consistency in the application of these statutes may be the only way to ease it.

We believe some surface owners may view these statutes as a possible quick (and sly) means to obtain rights to mineral interests in instances where the mineral owner's whereabouts are perhaps not too conveniently known; that is, the owner may have moved but his whereabouts could possibly be discovered with some searching. The better approach is to instruct clients that these statutes should be used not as a means to trick an absent, or perhaps unwary, mineral owner, but rather as a means of eliminating truly abandoned mineral interests that may burden an otherwise clean title. It should be expected that courts will interpret dormant mineral statutes in a way that would avoid making the court a party to trickery if in fact a reasonable inquiry would lead to the absent owner.



"IT'S GOOD TO BE THE KING!": OFFICE OF NATURAL RESOURCES REVENUE PROPOSES SIGNIFICANT CHANGES TO FEDERAL AND INDIAN MINERAL LEASE ROYALTY VALUATION STANDARDS

Peter J. Schaumberg
Beveridge & Diamond, P.C.
Washington, D.C.

The concept of a royalty payment dates back to medieval times when the king would grant use of his land in exchange for a share of the crops or livestock produced from the land—hence the term "royalty."The Department of the Interior's Office of Natural Resources Revenue (ONRR) is responsible for collecting royalty payments owed to the United States on oil, gas, coal, and other minerals produced from leases on federally managed lands on the Outer Continental Shelf, from public lands onshore, and from Indian lands. The royalty payment due each month on production from a federal mineral lease is based on the royalty percentage specified in the lease, the volume of production, and the value of that production (royalty due = royalty rate x volume x value).

The royalty rate for a federal mineral lease is set in the lease agreement and generally ranges from 12 ½ percent to 18 ¾ percent. The volume of production generally is measured at the lease. In contrast, value is a subjective determination, and federal mineral leases reserve the value determination standards to ONRR. On January 6, 2015, ONRR issued a proposed regulation (80 Fed. Reg. 608) that would substantially modify existing regulations in 30 C.F.R. Part 1206 for the valuation for royalty purposes of oil, gas, and coal produced from federal leases onshore and on the Outer Continental Shelf. The proposal also would amend ONRR's royalty valuation regulations for coal production from Indian leases. While this proposed rule may have certain benefits for industry, ONRR is proposing to eliminate several existing provisions to the disadvantage of existing and future lessees. ONRR also is amending the rules to reserve considerable new "default" authority to unilaterally determine the appropriate royalty value.

On the positive side for lessees, ONRR is proposing to amend the valuation procedures for gas produced from federal leases, adopted in 1988, to make them consistent with current ONRR oil valuation regulations adopted in 2000. Valuation of nonarm's-length dispositions of gas production would be based on a methodology that relies primarily on published index prices. For valuation of arm's-length sales of gas production, lessees could elect either to pay royalties based on their or their affiliates' "gross proceeds" (less applicable transportation adjustments) even if that sale occurs in a distant market or to instead pay based on the new index-based methodology proposed for nonarm's-length dispositions. Lessees would not be required to "chase" gross proceeds to distant sales points.

The ONRR proposal includes many changes to other valuation procedures for both oil and gas. ONRR is proposing to eliminate a number of existing allowances for transportation and processing, with resulting higher royalty values. The most costly change for industry is that ONRR is proposing to reverse its current practice and disallow any transportation deduction to move oil or gas production from deep water completions on the Outer Continental Shelf to the first platform. Notably, ONRR discarded some of these same proposed reforms for federal oil and gas in recently finalizing its regulations for Indian oil valuation on May 1, 2015.

The proposed rule would also revamp valuation procedures for coal production from both federal and Indian leases. Under the existing regulations, if a coal lessee transfers production to an affiliate in a nonarm's-length transaction, then the production would be valued by application of benchmarks that look first to prices in comparable arm's-length sales in the same area where the mine is located. ONRR is proposing instead that if a lessee sells or transfers coal to an affiliate under a nonarm's-length transaction and the affiliate ultimately resells at arm's-length, then the affiliate resale price establishes the royalty value. Unlike for oil and gas, ONRR is not providing coal lessees an option to use the valuation procedure for nonarm's-length dispositions (that currently looks to values in the area where the mine is located) instead of "chasing" gross proceeds to a distant sales point. Because any disparity in pricing would inevitably favor a lower price in the local market, this proposal would significantly increase royalty obligations and valuation complexities related to transportation allowances, particularly for coal producers whose marketing affiliates are selling coal under arm's-length contracts in distant markets. With respect to nonarm's-length dispositions of coal production, ONRR is proposing to replace its benchmark process that relies on comparable sales in the area with a provision that would require the lessee to value coal production based on the price of the electricity generated by the coal. This proposal is highly questionable because the royalty rate set in the lease is for coal, not electricity. It is also unclear that coal producers would be able to obtain information on sales prices for electricity and associated generation and transmission costs.

The most controversial new provision applicable to oil, gas, and coal is what the agency denominates as its "default provision." Under this provision, there are multiple opportunities for ONRR to elect not to apply the regulatory valuation standards and to instead unilaterally establish a "reasonable" royalty value on a case-by-case basis using a variety of discretionary factors. This proposal is problematic for industry because it diminishes the certainty in the valuation process provided in the existing oil, gas, and coal valuation standards, the single most critical underlying principle in those rules. This provision establishes a very low bar for the agency to second-guess a lessee's valuation.

The public comment period for the proposed rule closed on May 8, 2015. Several leading industry trade associations and companies weighed in on the proposal. ONRR must consider and respond to those comments in adopting any final rule, and its final rule is subject to judicial review. While it is indeed good to be the king, fortunately under our jurisprudence federal agencies are bounded by well-established standards of administrative procedure when making changes to existing regulatory regimes.