

MISSISSIPPI LEGAL CONSIDERATIONS

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Stan T. Ingram
Biggs, Ingram & Solop, PLLC





MINERAL ESTATE VS. SURFACE ESTATE

- A severed mineral interest is an interest in real estate
- Considered a valuable property right
- No prescription in Mississippi
- Mineral rights include oil, gas and other hydrocarbons (not sand, clay and gravel)



THE TRADITIONAL DOMINANCE OF THE MINERAL ESTATE

The general rule is best described as:

A mineral owner or lessee may use as much of the surface as is reasonably necessary for the exploration, drilling and production of oil and gas. If a mineral owner or lessee's use of the surface is deemed reasonable and necessary he is not liable for injury or damages resulting from his actions.



OPTIONS AVAILABLE TO THE MINERAL OWNER

- Right to explore
- Right to lease, thereby giving such rights to a Lessee



RIGHTS of THE MINERAL OWNER OR HIS/HER LESSEE

- The right to enter, occupy and use as much of the surface as is reasonably necessary to explore, mine and market minerals.
- The right to make all reasonable and necessary use of soil, trees, growing crops, during its operations.
- Not liable for any damages thereto, unless the lease provides otherwise or the damages are the result of negligent, unnecessary or unreasonable use.
- Conduct of the lessee is “to be measured by the broad standard of the prudent operator rule.”



“Reasonable Accommodation” Doctrine

- Many oil and gas operators in Mississippi and elsewhere have already recognized today’s initiative to reach a “reasonable accommodation”
- Mississippi is yet to make this the applicable legal standard.
- *Abram v. Sklar Exploration Co., LLC*, 408 F.Supp.2d 244 (S.D. Miss. 2005); *EOG Resources, Inc. v. Turner*, 908 So.2d 848 (Miss. 2005).



THE RIGHT TO EXPLORE VARIES

- For oil:
 - Shallow oil (Surface – 12,000') – 40 acre unit
 - Deep oil (below 12,000') – 80 up to 160 acre unit
 - Horizontal Wells – 1920 +/- acre unit
- For Gas:
 - Shallow gas (surface – 12,000') – 320 acre unit
 - Deep gas (below 12,000') – 640 acre unit
- For CO²:
 - Units vary in size – 640 to 1280+ acres



FORCE INTEGRATION

- “Non-Consenting” owner defined at §53-3-7(c):
 - “nonconsenting owner” shall mean an owner of drilling rights which the owner has not agreed, in writing, to integrate in the drilling unit.
- Then who is an “owner?”:
 - “Owner” shall mean the person who has the right to drill into and produce from any pool, and to appropriate the production either for himself or for himself and another or others.
- Those who propose a well have the right to force integrate pursuant to Miss. Code Ann. §53-3-7
 - Straight force integration
 - Force integration with alternate risk charges
- Three (3) options
 - Lease
 - Participate
 - farmout



TODAY'S LEASE FORM

If there is one thing certain about today's oil and gas lease, is that it is uncertain.

This presentation will cover the various clauses of the oil and gas lease forms which are commonly used today in Mississippi. These are:

Producers 88(9/70) – With Pooling Provision

Producers 88(9/70) – Paid Up

Producers 88(9/70) – With Pooling Provision (SP 4-75)

All three forms – “Tri-State”

There is no such thing as a “standard” oil and gas lease form



CONSIDERATION

All that is required by law is that some consideration be given.

- The common procedure in Mississippi is to set forth Ten Dollars (\$10.00) in this blank, since most lessees do not want the general public to know what they are paying as bonus.
- Actual consideration varies depending on:
 - Prospect area
 - Existing production
 - competition



LEASE TERM

Paragraph 2 sets out the term of the lease.

1. Primary term - as long a period as the lessor and the lessee agree
2. Secondary term for so long as “operations” are conducted with no cessation of more than ___ days, etc.
 - Tri-State Form defines “Operations”



ROYALTY CLAUSE

- Paragraph 3
- Usually 1/8 of the oil and gas produced under the lease, but many times the lease forms are revised to provide for larger royalties.
- Many sophisticated lessors (especially timber companies) incorporate special terms and provisions into the royalty clause:
 1. Grant lessor the right and option to purchase all or any part of lessee's share of oil or gas produced.
 2. Requires lessee to pay all of the costs of any treatment processing plant, including construction, transmission and operation.
 3. Grants lessor the right and option, but not the obligation to take any of the lessor's royalty share of oil in kind.
- Shut-in gas royalty clauses solve the problem of a lessee's inability to produce gas pending construction of the necessary pipelines.



POOLING PROVISION

- Paragraph 4
- Many leases provide for the maximum number of acres which a particular unit may contain, i.e. 80 acres for oil and 640 acres for gas, plus 10% acreage tolerance; or larger unit as required per governmental rule or order.
- Most pooling provisions require that some affirmative steps be taken in order to pool or designate a unit:
 1. Prior written notice to the lessor of the proposed unit and well location.
 2. Filing a pooling declaration for record
 3. Providing lessor with a copy

EFFECT OF POOLING:

- Once pooled, production from one tract is considered as production from all of the lands within the unit.
- Proportionately reduces the royalty
 - The Tri-State form grants a lessee the right to exercise a pooling option at any time, “whether before or after production has been established either on said land or on the portion of said land included in the unit.”
 - However, we recommend that the pooling declaration be filed on or before the expiration of the primary term.



Example – Landowner owns

- $\frac{1}{4}$ mineral interest in NW/4 of NW/4 of Section 1-T1N-R1W
- Landowner gives a Lease to company with a $\frac{3}{16}$ royalty
- Oil Company forms a 640 acre gas unit comprised of Section 1 – production is found

What is the Landowner's unit interest?

$$\frac{1}{4} \times \frac{3}{16} \times \frac{40}{640} = 0.00292969$$



Pugh Clause:

- Not in most printed forms; added as an addendum
- Provides that upon expiration of the primary term, the lease terminates as to all lands outside established and/or producing units.

Two Types:

1. Horizontal Pugh Clause
1. Vertical Pugh Clause



Continuous Drilling Obligation:

- Commonly associated with the Pugh Clause
- Maintains all acreage outside existing units, provided Lessee conducts a continuous drilling program
- Purpose – To insure that all of the acreage is ultimately tested
- No more than 90 - 180 days lapsing between cessation of operations for one well and commencement of operations for another.



SURFACE USE AND DAMAGES PROVISIONS

- Paragraph 7 of Tri-State lease forms.
- In Mississippi the holder of a valid oil and gas lease has the right to go on the land described in the lease and do all things necessary and incidental to the drilling of a well, including the right to use the surface as long as it is not unnecessarily damaged or injured.
- The surface/damage clause serves to:
 1. Permit lessee to use water free from royalty (other than from lessor's water wells);
 2. To use oil and gas produced from said land in relation to lessee's operations.
 3. Authorizes the lessee to remove certain equipment upon completion of operations; and
 4. Provides that no well shall be drilled nearer than 200 feet from a house or barn on the lessor's property.



EXTENSION OPTION CLAUSE

- Producers 88 (9/70) – Paid-Up (SP 4-75) form.
- Extends the primary term for an additional period of five (5) years, provided the following steps are taken:
 1. Lessee provides lessor with written notification of exercise of option.
 2. Written notification must be received prior to 30 days before expiration of primary term.
 3. Tendering the designated bonus for each net acre as to which lease is so extended.
 - “within 30 days prior to expiration of the primary term of this lease”
 - A payment must be made prior to the last 30 days of the primary term.



OTHER NOTORIOUS CLAUSES

- Vertical “Pugh” Clause w/ Continuous Drilling
- Favored Nations
- Offset Well Obligation
- Surface Restoration/Compensation
- Access to Drilling/Geological Data
- Special Royalty Payment Provisions
- Retained Access Clause

