

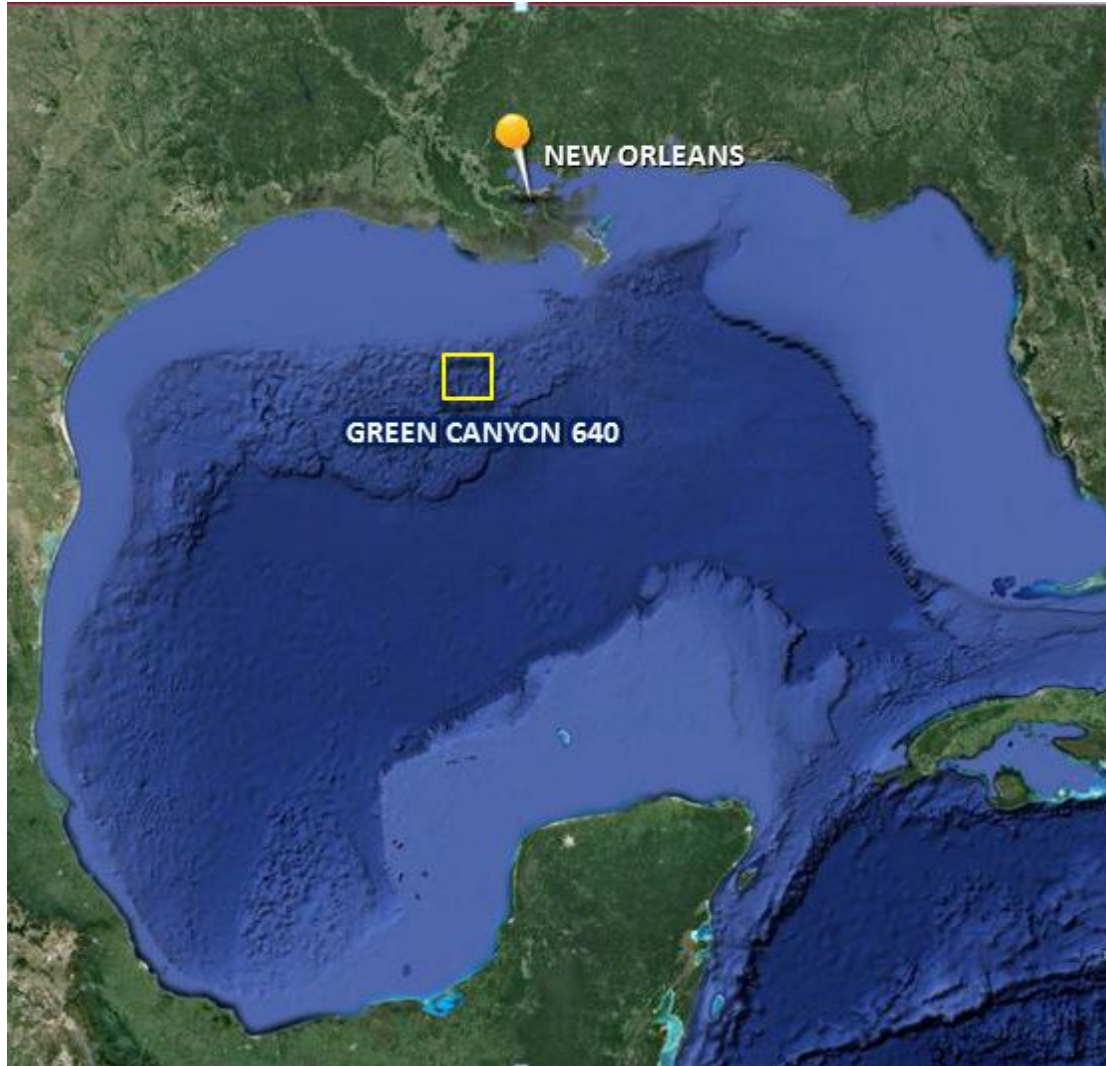
2015 P.L.A.N.O. Seminar

# Legal Updates Affecting the E&P Industry

Presented by:  
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& Patrick “Rick” M. Shelby

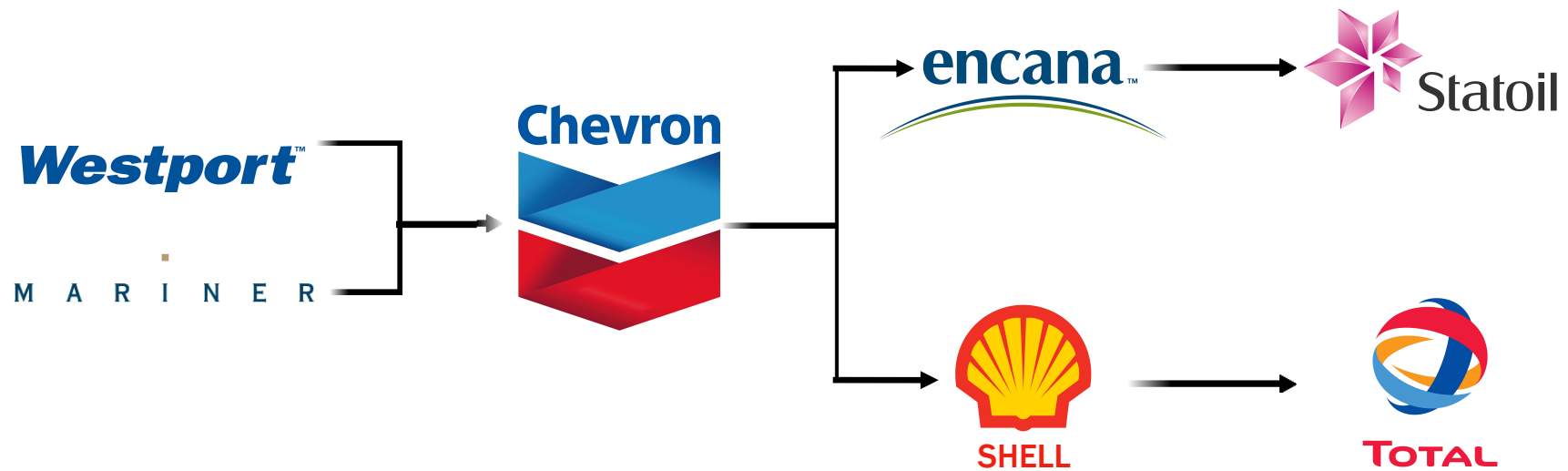


# Total E&P USA, Inc. v. Kerr-McGee Oil and Gas Corp.



- Declaratory action filed in Eastern District of Louisiana in 2009
- Issue: Whether overrides are due when the federal government's royalty is suspended for royalty relief
- Statoil joined lawsuit as a co-lessee. Chevron did not.

# Chain of Title



The overriding royalties described herein shall be calculated and paid **in the same manner and subject to the same terms and conditions** as the landowner's royalty under the lease.

# The GC 640 Lease – Includes Royalty Relief

Form MMS-2005 (March 1986) (Supersedes MMS-2005 August 1982)	Office New Orleans, LA	Serial number OCS-G 20082
UNITED STATES DEPARTMENT OF THE INTERIOR MINERALS MANAGEMENT SERVICE	Cash bonus  \$610,560.00	Rental rate per acre, hectare or fraction thereof \$7.50 per acre
OIL AND GAS LEASE OF SUBMERGED LANDS UNDER THE OUTER CONTINENTAL SHELF LANDS ACT	Minimum royalty rate per acre, hectare or fraction thereof \$7.50 per acre	Royalty rate  12 1/2 percent <sup>1</sup>
This form does not constitute an information collection as defined by 44 U.S.C. 3502 and therefore does not require approval by the Office of Management and Budget.		Profit share rate
This lease is effective as of JUN 1 1998 (hereinafter called the "Effective Date") and shall continue for an initial period of ten years (hereinafter called the "Initial Period") based between the United		

In consideration of any cash payment heretofore made by the Lessee to the Lessor and in consideration of the promises, terms, conditions, and covenants contained herein, including the Stipulation(s) numbered 3 attached hereto, the Lessee and Lessor agree as follows:

(hereinafter called the "Lessee"). In consideration of any cash payment heretofore made by the Lessee to the Lessor and in consideration of the promises, terms, conditions, and covenants contained herein, including the Stipulation(s)

**'This lease may be eligible for royalty suspension pursuant to PL 104-58. If eligible, Sections 5 and 6 of this lease instrument will be superseded by 30 CFR Part 26, published in the Federal Register on January 16, 1998 (63 FR 2626).**

All of Block 640, Green Canyon, OCS Official Production Diagram, NOG 13-5.

'This lease may be eligible for royalty suspension pursuant to PL 104-58. If eligible, Sections 5 and 6 of this lease instrument will be superseded by 30 CFR Part 26, published in the Federal Register on January 16, 1998 (63 FR 2626).


May 7 2001 11:20

Fax: 7135482030

WESTPORT

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# Example of Other Overrides

<p> (An indirect wholly owned subsidiary of Anadarko Petroleum Corporation)</p> <p>February 23, 2009</p> <p>Ms. Colette Worcester Minerals Management Ser 1201 Elmwood Park Blvd. New Orleans, LA. 70123-</p> <p>RE: Green Canyon Block Assignment of Over</p> <p>Dear Ms. Colette:</p> <p>Enclosed for filing with the (2) fully executed original McGee Oil &amp; Gas Corpora USA, Eni Petroleum US</p>	<p><b>OVERNIGHT</b></p> <p>Kerr-McGee Oil &amp; Gas Corporation 1201 Lake Robbins Drive The Woodlands, TX 77380</p>
<p>The con</p> <p>One the cop</p> <p>If y 300</p> <p>Since</p> <p>Ver Off</p> <p>Enc</p> <p>c: I</p> <p>N</p> <p>S</p>	<p>Except as set forth in the succeeding sentence relating to the calculation and payment of the overriding royalty interest, this Assignment of Overriding Royalty Interest (this "Assignment") is subject to the terms and conditions of the Lease.</p> <p>Assignees' overriding royalty interest shall be calculated and paid at the same time, in the same manner, and subject to the same terms and conditions as Lessor's royalty interest under the Lease would be calculated and paid were the Lease not governed by 43 U.S.C. Section 1337(a) (3) or any successor statute providing for royalty relief respecting the Lease.</p> <p>This Assignment is made without warranty of any kind, express or implied on the part of Assignor, except for claims arising by, through, or under Assignor.</p>
	<p>Name: <u>FRANK WILLIAMS</u> Its: <u>Attorney-in-Fact</u> <i>FW</i></p> <p><u>Vera Wells</u></p> <p>Name: <u>Vera Wells</u></p>

# The Granting Clause

Green Canyon 640

## ASSIGNMENT OF OVERRIDING ROYALTY INTEREST

### KNOW ALL MEN BY THESE PRESENTS:

That the undersigned WESTPORT OIL AND GAS COMPANY, INC. whose address is 410 17<sup>th</sup> Street, Suite 2300, Denver, Colorado 80202-4436 ("Assignor"), for and in consideration of the sum of Ten Dollars (\$10.00) and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged by Assignor, does hereby CONVEY, TRANSFER, ASSIGN AND SET OVER unto the following parties ("Assignee") the interest set out opposite their names, as an overriding royalty interest payable out of all oil, gas, casinghead gas and associated substances produced, saved and marketed from the lease (the "Lease") and described on Exhibit "A" attached hereto, subject to any applicable pooling, unitization or similar agreement, statute or order:

**That the undersigned WESTPORT OIL AND GAS COMPANY, INC. whose address is 410 17<sup>th</sup> Street, Suite 2300, Denver, Colorado 80202-4436 ("Assignor"), for and in consideration of the sum of Ten Dollars (\$10.00) and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged by Assignor, does hereby CONVEY, TRANSFER, ASSIGN AND SET OVER unto the following parties ("Assignee") the interest set out opposite their names, as an overriding royalty interest payable out of all oil, gas, casinghead gas and associated substances produced, saved and marketed from the lease (the "Lease") and described on Exhibit "A" attached hereto, subject to any applicable pooling, unitization or similar agreement, statute or order:**

3. The overriding royalty interest herein conveyed is payable out of and only out of oil and gas produced, saved and marketed, pursuant to the terms and provisions of the Lease, and is expressly subject thereto.

Green Canyon 640 OFRI.doc

CONFIDENTIAL

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# TOTAL Case – 2010 Summary Judgment & Fifth Circuit Appeal

- Total and Statoil filed motions for summary judgment on grounds that the two assignments creating the Overrides are clear and unambiguous.
- Judge McNamara granted summary judgment. He ruled that the assignments were unambiguous and thus “Total’s and Statoil’s payments of the overriding royalty interest payments are suspended until production reaches the 87.5 million barrel of oil equivalent.”
- On appeal, a divided panel of the United States Court of Appeals for the Fifth Circuit reversed the district court decision and remanded the action.
- The panel concluded that “a court may not find that the parties intended to suspend the overriding royalty obligation based exclusively on the words of the calculate and pay clauses but must interpret the overriding royalty contracts further in search of **the parties’ common intent.**”



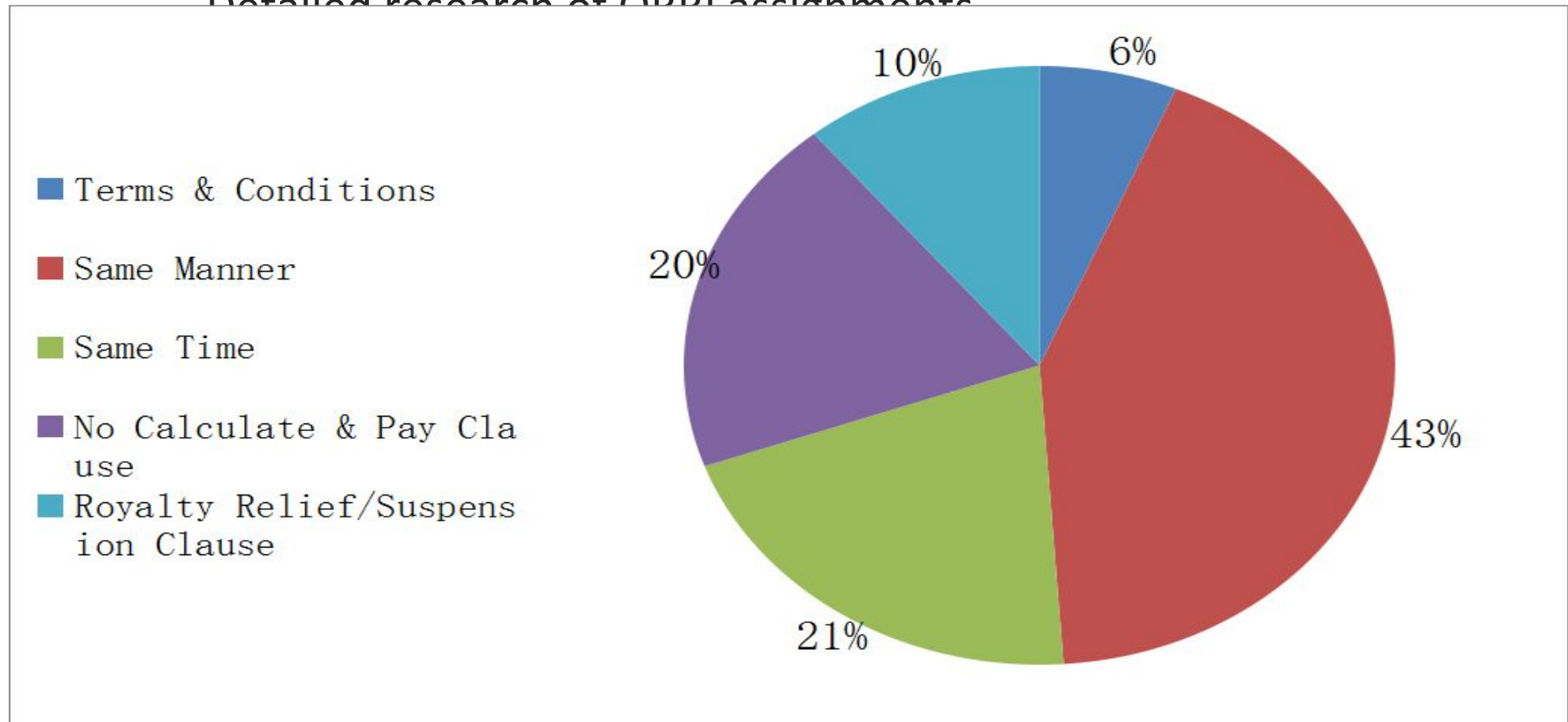
# TOTAL Case – Custom & Usage

- An industry custom or usage is a practice that has been performed regularly for a sufficient period of time that it enjoys a general and widespread acceptance in the industry.
- ONE ISSUE – when is custom & usage significant; at time of production or at time of assignment?
  - Research = 3,528 DWRRA Leases issued between 1995 and 2000
  - Leases producing at time of assignment (1999 = 5; 2001 = 10)

# TOTAL Case – Custom & Usage

- SECOND ISSUE – what is custom & usage in connection with payment of ORRI during royalty relief period?

Detailed research of ORRI assignments



# TOTAL Case – Double Damages

- Kerr-McGee and the individual plaintiffs also sought damages for statutory penalties under Mineral Code Articles 137/212.21 *et seq.* They argued the suspension was unreasonable because the companies expected to pay the ORRI's and because all other companies paid during royalty relief.
  - If the obligor fails to pay and fails to state a reasonable cause for failure to pay in response to the notice, the court *may award as damages double the amount due*, legal interest on that sum from the date due, and a reasonable attorney's fee regardless of the cause for the original failure to pay.
- Total and Statoil filed summary judgment on this issue, arguing that they stated a reasonable cause for nonpayment of ORRI's – basically citing the language of the ORRI contracts in their reports.
- A few weeks before trial, the court found Total & Statoil timely stated reasonable cause for nonpayment – namely, that their interpretation of the contracts was at a minimum, reasonable.
  - “Thus, although perhaps maverick, the Court cannot say the query raised by Defendant was legally unreasonable.”
  - “That being said, statutory penalties may be imposed, pursuant to §212.23 of the Louisiana Mineral Code, only if the clause for nonpayment of royalties is unreasonable; **mere error does not suffice.**”

## *Samson Contour Energy E&P v. Smith*

- After receiving a copy of a judgment annulling the donation, Samson suspended royalty payments for the existing wells subject to the donation.
- Using an outdated paydeck, Samson then paid the heirs the inaccurate royalty percentages for six new wells over a 2 year period.
- Samson received written notice under R.S. 31:137. The notice also indicated the wells at issue and potential errors made.
- Samson responded but did not specifically address the issue of incorrect royalties or pay additional royalties.
- The Succession filed suit seeking double damages under the Mineral Code.

## *Samson Contour Energy E&P v. Smith cont.*

### Samson argued:

1. The notice was insufficient because it did not specifically demand payment;
2. Samson timely responded to the notice;
3. Samson paid the heirs, just not the “Succession”;
4. Samson did not receive a certified copy of the judgment annulling the donation and the judgment was never recorded in the public record; and
5. The same heir who received excess royalties initiated the claim as co-administrator of the Succession so he had “unclean hands”.

## *Samson Contour Energy E&P v. Smith cont.*

- The court concluded that Samson failed to follow industry practice in using an old paydeck and not adjusting the payments when it discovered the error (even though it partially paid the Succession).
- Samson did not have reasonable cause for nonpayment because it failed to respond with reasonable cause for nonpayment and failed to investigate its records and pay the proper owner after it received notice.
- The court awarded the Succession \$3.1 million, which was double the amount of royalties owed (\$2.6 million) and \$505,000 in attorney fees. This was in addition to \$1.3 million paid to heir/son.
- The dissent agreed that Samson received adequate notice; however, it questioned whether Samson owed the heir/son a second time for his interest that Samson had already timely paid and a third time for penalties.

# ATP Bankruptcy Case Background

- Case No. 12-36187 (Isgur) – S.D. Texas
- ATP sought Chapter 11 bankruptcy protection in August 2012, citing dramatically reduced cash flows from the deepwater drilling moratorium.
- ATP listed assets of \$3.6 billion and liabilities of \$3.5 billion in its Chapter 11 petition.
- Much of ATP's development and production was funded by debt and issuance of term ORRIs/NPIs.
- In these proceedings, ATP's lawyers creatively questioned the nature of ATP's interest in the OCS leases and their derivative interests.



# ATP Lessons Learned – ORRI

- ORRI holders made claims to recognize ORRIs as property rights not subject to rejection in bankruptcy
- Pre-bankruptcy = ATP assigns/conveys Term ORRI / NPI to raise capital (lenders, drilling contractors, charterers)
- Post-bankruptcy = ATP labels conveyances of non-cost bearing interests as financing transactions and not sales of a property interest
- ISSUE: “disguised financing” or transfers of ownership
- WHY? Property of the Estate or not?





# ATP and DOI Position on Nature of an OCS Estate

- In these cases, ATP argued that under the OCSLA, the title it acquired from the DOI in the OCS leases was that of a lessee, and did not constitute absolute title.
- Making the OCS leases unexpired leases.
- Accordingly, any ORRI or NPI conveyance that is derivative of ATP's OCS leases, did not constitute real property interests.
- Therefore, the ORRIs are not property of the burden holder and may be rejected in bankruptcy.
- The DOI supports ATP's position because it agrees that OCS leases are merely contractual leasehold rights.

# ATP Implications

- Does state law still apply as surrogate federal law?
- Does the U.S. Government recognize ORRI's as property interests? Are these property rights at risk?
- Does this mean anything for us outside of the bankruptcy context? For recordation or mortgage purposes?
- Probably not now, but this is an issue that will come up again.

## Lesson:

Protect your interest in offshore ORRI's as property and interest rights where possible. Realize that at least in the bankruptcy context, there may be some question as to whether the ORRI's are property rights.



# Donna Dixon – 2014 OCS Workshop



## Determination of Financial Strength and Reliability in Existing NTL

BOEM may but is not required to consider:

### EITHER

future net revenues associated with the value of proved producing reserves for all leases where a lessee owns record title interest equaling the percentage of their interest. (Up to 25% of reserve value can be used to calculate net worth)

### OR

future net revenue associated with the value of proved producing reserves in calculating net worth by obtaining an independent 3rd party estimate of total proved producing reserves. (If value includes record title and operating rights interests, then up to 50% of the reserve value can be included in net worth calculation)

- Following recent bankruptcy matters, these considerations will likely be revised to reflect difficulty in tracking offshore interests not currently in BOEM's system.
- The NTL also contemplates BOEM's request for additional insured status and insurance for residual liabilities for both catastrophic events and non-payment.

## *Century Exploration New Orleans, LLC v. United States*

- BOEM/BSEE issued new regulations increasing the bond amount requirements that oil and gas lessees must post with the federal government for oil spill financial responsibility (OSFR) to address “worst case discharges” of oil from the lease – calculated in connection with submittal of an exploration plan.
- Under these new regulations, Century’s bond requirements rose from \$35 million to \$150 million—1500 to 143,000 bbls.
- Century filed suit in the federal Claims Court and argued that the federal government improperly imposed these new regulatory requirements under OPA and thus breached the lease.
- The government maintained that these new regulations were issued instead under OCSLA and thus that the new regulations could properly be applied Century’s existing lease.

## *Century Exploration New Orleans, LLC v. United States*

- NTL about the new regulations identified an OCSLA provision as its source of authority—limited to OCS leases.
- NTL “did not change the text of the relevant OPA regulation ... [but instead] merely changed the way an OCSLA regulation incorporates an OPA calculation”; further, “for three out of the four alleged alterations to the worst case scenario requirement, it is not even clear that the original requirement was an OPA requirement.”
- Concluding that the government acted pursuant to OCSLA, the Federal Circuit held that there was no breach of the lease.

## ANY QUESTIONS?



\*

**GORDON**  
**ARATA** MCCOLLAM DUPLANTIS  
& EAGAN LLC