

## Tawney v. CNR: Flat Rate Leases Challenged

In another decision in the case of *Tawney v. CNR*, the Circuit Court of Roane County held that leases which provide a fixed annual (or otherwise periodic) sum as royalty regardless of the volume of gas actually produced ("flat rate royalty leases") violate public policy. The Circuit Court of Roane County is a trial court whose ruling binds the parties to the action, but producers should be aware of the emphatic view expressed by this judge. Additionally, the ruling voids or reforms 651 leases held by Chesapeake Appalachia, LLC, so the circuit court's decision may be appealed,

and reviewed by the West Virginia Supreme Court.

The court's opinion considers whether flat rate royalty leases are against the public policy of West Virginia in light of the Flat Rate Royalty Statute (West Virginia Code § 22-6-8, effective June 13, 1982). Under this Statute, the legislature required a flat rate royalty lessee to agree to pay a statutory royalty in order to obtain a well work permit from the State. Since drilling, deepening or recompleting a well requires a well work permit, the Statute effectively changed the amount of royalty payable under

flat rate royalty leases with respect to new or reworked wells.

In order to obtain a well work permit on a flat rate royalty lease after June 13, 1982, the lessee must agree to pay "...to the owner of the oil or gas in place not less than one eighth of the total amount paid to or received by or allowed to the owner of the working interest at the wellhead for the oil or gas so extracted, produced



George Patterson

**Tawney Case** Continued on pg 20

## Amendment Approved: Dues Dates Revised

At the Special Membership Meeting held August 1, 2006 during the Summer Meeting, the proposed By-Laws Amendment which authorized changes in the dates for payment of membership dues passed overwhelmingly.

ARTICLE III, Section 2 of IOGA's Bylaw was amended by adding the words "and payment dates" after the word "rates" in the first sentence of Section 2, and as amended the said Section 2 now reads:

### Section 2. Membership Dues.

Each individual, firm or corporation holding membership shall pay dues in accordance with the rates and payment dates established by the Board of Directors. A member qualified during a membership year under more than one category of membership shall only pay

dues under one category of membership, which, except upon approval of the board, shall be the category providing for the highest level of dues for that member that year.

This change establishes the Board of Director's authority to change the date in which membership dues become delinquent. Prior to the passage of this amendment every member had until June 30 of the current membership year to pay their dues and receive full membership services and benefits. The Board of Directors recognized this created a situation where membership services and benefits were provided and dues were sometimes not recovered. This change provides the mechanism to reduce unnecessary expenses, provide better management of cash flow, and

expedite certain membership benefits and services.

The second change in the By-Laws was in ARTICLE III, Section 4, which added the words "in good standing" after the words "are members", and deleted the words "and which have satisfied, or made arrangements with the Board of Directors to satisfy, their dues obligations for the current membership year."

This section now reads:

### Section 4. Voting Eligibility.

Voting members will be those entities that are members in good standing of the Producers/Operators, Allied Industries, Gas/Oil Marketer and Professional membership classifications. Any voting member may be represented and vote at any membership meeting in person

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Denny Harton President, IOGA WV

## Are We Under Attack?

Not long ago when gas and oil prices hovered at or near historical lows for modern times, it seemed that we were all pretty much left alone to wallow in the squalor of diminishing returns. No one seemed concerned that our industry had, for the last decade, lost hundreds of thousands of jobs and that our work force was one of the most under paid among leading industrial sectors.

While we struggled to maintain our very existence, America's appetite for energy continued to grow, but was filled with foreign imports. We complained and predicted what would happen if something was not done to protect and support the producers of domestic oil and gas. Because we could not afford to drill in the United States, we all knew the day would come when energy would once again be in short supply and prices would reach levels that allowed us to drill for more energy here at home.

That time has come. We now can earn a sufficient price for our production that will allow us to begin the rebuilding of the infrastructure that was decimated in the 1990's due to low prices. Now is the time for our companies and our employees to grow as well. After all, we all paid the price and have suffered the consequences of lower prices. Our nation has begun to suffer the consequences of lower prices as well. As the price of energy continues to rise, we simply must drill more wells domestically and nothing should be allowed to impede drilling or circumvent funds allocated for drilling and infrastructure improvements.

Oh, but wait, now that we are beginning to grow a healthier industry because we can afford to increase drilling budgets, it seems there are many out there who think we should take dollars away from our drilling budgets and spend them elsewhere. It started

with an increase in severance tax. And now there is political jargon being bantered around about windfall taxes and the courts have now waded in.

Our industry is under examination on many fronts from being targeted for tax increases of some

**Under Attack** Continued on page 6



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## Quality Control Practices for Improved Cementing Operations

Cementing is perhaps the most important yet least appreciated of all the well services performed during gas well construction. The concept of long term zonal isolation is the focus of much research in cementing today. How do you achieve it? What are best practices for cementing wells in the Appalachian Basin today? Certainly, we should not be so much concerned today with neat, high compressive strength cements but yet the Type I and 15.6 PPG slurry lives on, some still calling it Class A. It may be a technicality but none of the cement being pumped has the API monogram. Sorry, the cement may meet API specs in some cases but it is ASTM Type I.

What a shame about not looking for cost cutting within the art and science of cement design. Higher yield, lower density slurries maximize well economics. A low yield cement like neat Type I mixed at 15.6 PPG doesn't fit the bill. Something else that no longer fits the bill is using compressive strength as the benchmark comparison of competing cement blends. Instead why not consider cements that at downhole conditions (under confining stress) have the required tensile strength and preferred mechanical properties like a low Young's Modulus. The days of macho cement compressive strength is over. Rest in peace I say – the compressive strength you get from an API crush test or UCA isn't

what is important in cement design these days.

Changing gears, let's turn our attention back to cement QC practices. Would you agree there are cement jobs being pumped in the field today that are done with little thought as to what the standard practices should be, that is, jobs performed in the name of "simply getting the work done?" Should you ever compromise cement job quality control? The standard practice on a cement job must be to measure and document rate, pressure and density.

The quality control process starts at your preferred vendor's cement plant. Let's not forget the local cement plant. **QC Practices** Continued on page 8

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Charlie Burd Executive Director, IOGA WV

## From the Burd's Nest: Making The Right Decision

In a recent conversation with an executive director from another state association, we were discussing the issues confronting each organization and the steps we were taking to achieve a positive conclusion. After the conversation ended, I sat down and made a list of all the issues we talked about. I was astounded to find my list totaled eighteen items!!

With little hesitation I decided to expand the list to categorize, by working committee, who was designated to lead our effort and who was lending their expertise and assistance. Once our new president Denny Harton saw the list, he decided to make it a perpetual

work-in-progress type document.

As such, the Board of Directors now have before them an unsophisticated way of tracking these issues and those yet to be discovered.

As members, you also need to know that your Association works very diligently on a variety of issues throughout the course of each membership year and that some issues get resolved easily and some overlap into succeeding years. The second thing that bears repeating is there is not an issue too big nor too small to get our attention if it unilaterally affects independent producers.

By committee, here is listing of the major issues currently being ad-

dressed by IOGA-WV:

### Commerce Committee

(1) The TCO Refunctionalization of BM-18, (2) capacity through the Kenova interconnect, (3) DTI's rebuild of the Hastings Compressors, (4) the Equitable-Hope Merger, and (5) the verification on the Lost and Unaccounted For Gas provision from the gathering agreement settlement.

### Environmental Committee

Several CBM issues including the (6) Special Field Rules, (7) the Produced Water Permit work, (8) Interim Legislative Studies on CBM

**Burd's Nest** Continued on page 17



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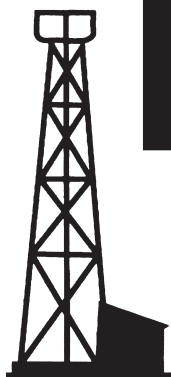
sort to the courts creating legislation from the bench that will do little for growth in production which is what is needed to solve the nation's energy problems.

There are those in Congress, the WV Legislature and the courts who want to influence the future of the domestic energy industry. We who understand our issues must, for the benefit of our nation and our companies and our employees, fight back to prevent or limit any intrusion into our affairs that could serve to limit or curtail future growth of domestic production.

To do this, we must participate in the system at every juncture. We must educate the public and our politicians. We must become more active in the political processes of selecting our congressional, legislative, administrative and judicial representatives. Whether as a group, individually or both, we must be willing to participate in each election process

at a level that far exceeds anything considered before AND WE MUST

EACH DO OUR PART IN OUR AREA.



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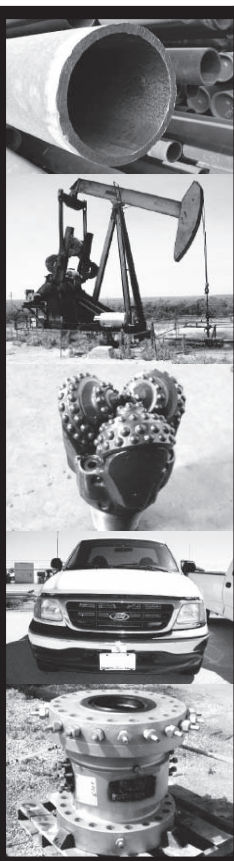
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## QC Practices Continued from page 3

ment plants do NOT manufacture to API specifications, so technically all cement here is more properly classified as Type I, Type II or Type III depending on its physical and chemical characteristics. The cement plant, if requested, will provide your service company lab with a certificate of analysis known as a cement mill run report. That report details the percentages of the four-(4) basic components of portland cement, namely the ingredients responsible for the "strength" of the cement. Not all cements are created equal and some may contain unwanted percentages of certain "bad actors" that cement design engineers would want to know about before the first test is run. Ask your cementing company how often they are testing cement to help protect you from job failures.

Devonian Shale cementing of low frac gradient shales requires low density cement slurries, often in the 12 PPG range. Twenty to thirty years ago service companies provided minimal quality assurance; all the cement jobs were done with jet mixers, a Martin Decker pressure recorder, and a nicely balanced shovel to "weigh" the cement. Buyer beware - that should not cut it with well operators today because there is potential for significant performance issues arising from the apathy toward sticking close to design slurry density. Let's take a closer look at why this is the case.

Cement design starts with slurries that are mixed in the lab using a known weight of cement to a known weight of water. The accuracy of these measurements can be as fine as two to four decimal points depending on the balance used. In the field the reason two radioactive or mass densimeters (one on low pressure mixing or recirculation side and the other on high pressure downhole side) are used in series for best prac-

tices on recirculating cement pump trucks is to assure that the designed slurry density is achieved, so that the cement slurry performs as expected.

A commonly pumped silicate extended cement slurry at a density of 12 PPG contains about 14.7 gallons of water per 94 pound sack of cement. If you don't monitor its density currently, you are going to see more error (or is that air?) in your cement fill-up and top of cement.

That's because mixing cement by pneumatically transferring it into a mixing bowl with high energy water entrains air in the slurry. That means the density of a non-pressurized mud scale will read less than what it would if it were pressurized. When using any cement, but especially such a lightweight cement, it is very important to pump the slurry within 0.2 PPG of the design density. As

**QC Practices** Continued on page 10

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## Greenhouse Gas Issues Heating Up

From an unusually intense and destructive 2005 Atlantic hurricane season to Al Gore's documentary, "An Inconvenient Truth" to the relatively mild winter, the past year has seen a confluence of events that have spurred a renewed interest in the issues surrounding global climate change. While most of the public is probably more focused on the impact of global warming to their heating and air-conditioning bills, legislatures and courts throughout the country are debating whether the gases most often linked to global warming, including methane and carbon dioxide, should be more aggressively regulated.<sup>1</sup> Oil and gas operators should be aware of these developments because they may have both short and long term impacts not only on the consumption of oil

and gas, but also on possible future emissions controls on wells, gathering lines, and compressor stations. These developments will present both opportunities and risks to operators.

The most obvious potential benefit to oil and gas operators stem from the fact that natural gas is a less intensive source of greenhouse gas than coal. This fact prompted the Pew Center on Climate Change to identify natural gas as an important transition fuel as the country moves away from greenhouse gas intensive fossil fuels and to cleaner burning or renewable energy sources. Such a development would lead to a greater use of natural gas in the short to medium term, but may also result in a long-term move away from natural gas as a source of electrical genera-

tion. It is difficult, if not impossible, to predict when the shift away from fossil fuels may occur, but it is likely to occur, if at all, over decades and not years.

The main risk from additional regulation of greenhouse gas emissions is that the new regulations may increase the cost of producing oil and gas. The process of reporting greenhouse gas emissions may increase costs in additional man-hours worked and software that must be purchased. But the real increase in the cost of production could come if emission limits were placed on oil and gas wells, compressor stations, and gathering and transmission lines, especially if the limits required oil and gas operators to invest in new technologies to control greenhouse

**Heating Up** Continued on page 14



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## QC Practices Continued from page 8

the density increases on these light-weight slurries, the yield goes down and if you pump it at a higher than designed density long enough, the annular fill-up will not be what you want. One possible consequence of poor field QC may be that you won't cover the upper most zone of interest and will have to spend money for a squeeze job.

Have you considered the impact on free water formation and fluid loss control when you don't pump your cement as close to design density as possible? Both can have detrimental effects on the job, the one can allow channeling in the annulus and the other can cause increased viscosity and possible bridging off in the annulus as fluid is literally squeezed out of it into permeable zones. It happens every year, a cement job ends prematurely when a Type I cement mixed like Class A with no fluid loss control has to be drilled out because it "dehydrated" before it was completely placed in the annulus.

Another quality control consideration is how the cement is loaded. How do you know all the cement additives aren't in one bulk tank and not in both on a job that uses more cement than one tear drop tank can carry? What documentation do you have that the vendor really put the right amount of additives in the cement in the first place? Anything more or less than what you ordered isn't right, is it? Rounding up or rounding down to the whole sack can affect job performance. What if your cement didn't set up in the coffee cup on location or it flash set in a couple minutes – have you ever considered poor blending by your pumping service vendor. Too much retarder or calcium chloride in a cement can affect job performance. The root cause analysis for such a problem may find that the cement

loader did not take the time to weigh the additives or did not blend them per standard practice. What you don't know can affect well performance

What about problems related to basic preventative maintenance? There are pads in the pneumatic bulk cement trucks that if not cleaned on a regular basis can lead to erratic delivery of cement to the cement pump truck and likely will result in the inability to unload the full amount of cement ordered. Consider going to visit your service company yard and while you are there ask about their preventative maintenance program related to cleaning their bulk truck air pads.

Every cement job should monitor and record pressure, rate and density. If you don't monitor and document these critical job parameters and there is a job problem, you will never know what happened for sure. After the job it is impossible to recreate what happened without digital

data on all three parameters. Martin Decker pressure charts don't tell you anything about rate and density and are severely lacking in detail. Modern mass density flowmeters are much more expensive and sophisticated and give the best information possible on rate and density. A measured flow from Micro Motion style flowmeters is the preferred best practice industry standard, not calculated flow rates based on pump stroke counters.

Try telling your boss that there was inadequate monitoring on a cement job when something goes wrong on that next surface job and you have to skid the rig. Some may say "but we saved a couple hundred dollars on the cement job" but the facts when uncovered could very well be that you really don't have a clue what you pumped down your well which is the case everytime when the benchmark standards for cement quality control are not

**QC Practices** Continued on page 12



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## What Happens To Your IRA When You Die?

Traditional IRA accounts have become a very important tool for accumulating and holding assets for retirement. Many individuals have accumulated large amounts of money in their qualified pension or profit sharing plans. When they terminate their employment, these funds are commonly rolled into a traditional IRA account to provide for greater flexibility in their retirement years. For many retirees, this IRA account will be their largest single asset.

After successfully accumulating these funds, an individual needs to give some attention to the rules that apply to the distribution phase of the retirement accounts. Without proper planning, a traditional IRA can be one of the worst assets to own at the time of death. Estate and income taxes could eat up 60 – 70 percent of an IRA account!

What are the rules for distributing traditional IRA funds at the account

owner's death? Different rules apply, depending on whether death occurs before or after the required beginning date—the date after which you have to begin taking annual distributions. This required beginning date for a traditional IRA is generally April 1 of the year following the year in which the IRA owner attains age 70½.

If an IRA owner dies before the required beginning date, distributions must be made under one of two methods:

- The Five-Year Rule – The entire value of the account must be distributed within five years after the death of the IRA owner.
- The Life Expectancy Rule – Any values payable to a designated beneficiary must be distributed over the life (or life expectancy) of the beneficiary, beginning within one year of the owner's death.

If an IRA owner dies on or after

the required beginning date, the remaining account balance must be distributed over the longer of: (1) the single-life expectancy of the designated beneficiary; or (2) the remaining single-life expectancy of the owner, based on his or her age at death.

In either case, a designated beneficiary may choose to receive a faster distribution of the entire account. Also, a surviving spouse who is the designated beneficiary of the IRA may elect to treat the IRA as his or her own.

A deceased's IRA account may be subject to both estate and income taxes at death. The value of the IRA account will be included in the deceased's estate for estate tax purposes. The amount of any estate tax due on the IRA will depend on the value of the deceased's total estate. In addition to the possible estate tax, distributions to the beneficiary will be considered income in respect of a decedent. The term income in respect of a decedent refers to those amounts to which the deceased was entitled as gross income, but which were not includable in his taxable income for the year of his death. The beneficiary will pay income tax on distributions received in the same manner as the decedent would have.

Proper planning by IRA owners during their lifetime can minimize taxes at the time of death and maximize amounts passed on to their heirs. Coordinating your tax and financial strategies with your life insurance program will allow you to get the greatest benefit from your planning.

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Hugh Byers Membership Chair

## Four New Members Approved

The Membership Committee is pleased to announce the following new members approved by the Board of Directors in August.

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### Katherine H. Abbott ASO

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QC Practices Cont. from pg. 10

practiced. As I said before what you don't know can affect well performance!



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Greg Kozera Halliburton

## Stressed?

You have a full day of meetings, people to call, services to set up, reports that need done. An employee needs to talk to you, an investor is on the phone, a land owner needs you to call him back about a problem and your boss needs that report you haven't started yet. You get home late for dinner, the kids have ball practice, your spouse wants to know when you're going to clean out the

garage and you still have that stack of mail to get through. Is this another "normal" day? Unfortunately for many people it is. Is it any wonder people feel stressed?

Actually stress isn't due directly to a lot of work or things to get done. Stress is what we do to ourselves. It is how we think. Is there anything that we can do to reduce the stress in our lives? Here are some ideas used

successfully by others. You may find them helpful:

- Start the day with gratitude. When we realize how blessed we are it is easier to put daily events in their proper perspective and helps us realize that most things aren't worth worrying about.
- Smile and laugh more. These are instant stress relievers.
- Exercise. Physical activity is a great stress reliever.
- Get proper rest. Sometimes this is easier said than done but still very important.
- Clear your mind. Go get a cup of coffee or just stare out the window for a few minutes.
- Help someone. I don't know exactly why this works but it does. Maybe it helps to put our own problems in perspective.
- Ask yourself, "What is the worst thing that can happen?" or "How big a deal will this be next week." This helps us to put things in perspective.
- Worry causes stress. Realize that over 90% of the things we worry about will never happen and most of what does happen we can't control anyway.
- Take a nap.
- Listen to music.
- Read out of a positive book for at least 15 minutes.

Remember stress, like happiness, is an inside job. It is something we do to ourselves. We can make the decision to deal with our work, the demands put on us and our problems without allowing them to get to us. We can choose not to be stressed. Remember one of our greatest tools to beat stress is humor. So smile.



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## Heating Up Continued from page 9

gas emissions from existing facilities. Even if the regulations only required new emission controls on facilities constructed after the regulation goes into effect, this would still increase the costs of expanding production in the future.

Regulation of greenhouse gases has been reenergized over the last several months due to both legislative and judicial developments.

On the judicial side, the United States Supreme Court's decision to hear arguments in a suit brought by twelve states and various environmental groups seeking to force the United States Environmental Protection Agency ("EPA") to regulate carbon dioxide and other greenhouse gases as air pollutants has raised the possibility of a sweeping change in the way both the federal government and the states regulate greenhouse gases. In 2003 EPA took the position that it does not have the authority to regulate greenhouse gases under the Clean Air Act because they are not hazardous to human health like other air pollutants. The states and environmental groups claim that the threat to human health from greenhouse gases is clear and that EPA must regulate these gases. If the states and environmental groups prevail, then EPA would have to establish air quality standards for greenhouse gases which would in turn lead to emission limits on individual sources of greenhouse gas emissions. If, however, EPA prevails, this will likely settle the question of whether EPA will regulate greenhouse gases and may halt, or at least slow, attempts to regulate greenhouse gas emissions at the state level. Oral argument is expected in this case in December with a decision to be rendered by the end of June 2007.

In West Virginia, the most significant legislative development that oil and gas operators should note is

the Greenhouse Gas Inventory bill that has been introduced in two of the last three Regular Sessions of the Legislature. Greenhouse gas inventories are repositories of emissions data from various sources. The previous versions of the bill aimed to establish an inventory of "significant emissions, reductions, capture and sequestration of greenhouse gases from stationary sources" including, "natural gas/oil systems." The DEP would establish a program for reporting, but every "significant" emitter of greenhouse gases would have to report their emissions.

This type of greenhouse gas inventory can be found throughout the country. California established a greenhouse gas registry in 2001 and has recently considered imposing a cap on greenhouse gas emissions. A

group of Northeastern states has taken steps to develop a regional greenhouse gas registry along with a "cap-and-trade" system for these gases during the last year. In June, a group of five Midwestern states announced a plan to create a new greenhouse gas registry that they hope will standardize greenhouse gas emissions reporting in that region. It is clear that states are taking the lead in creating these registries and placing caps on the greenhouse gas emissions.

The EPA has attempted to estimate statewide greenhouse gas emissions for the past several years and, in 2002, provided DEP with a grant to conduct baseline greenhouse gas emissions inventories for State's industrial, agricultural, transporta-

**Heating Up** Continued on page 16

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## Well Control and Drilling Practices – Part 2

I'll assume that you have already had an organizational meeting with your drilling contractor as we discussed in the last newsletter and now want some specifics! A good place to start is a review of your wellhead setup. Although every drilling contractor has his own idea of the "optimum" configuration, I'll take the liberty to cover a style which works well and is recommended by local drilling contractors. Remember, many of these setups might be different than the way things have been done in the past, which, as you might expect, often causes some resistance to change.

### 1) Nippling Up Casing Head

One method of setting up the wellhead requires that you nipple up on a casing head. The reason for this is that you have the protection of the blow-out-preventor throughout drilling, logging, and running pipe. Many contractors nipple down (remove the BOP and diverter air-bowl) before open hole logging or running pipe. This can result in total loss of control should well fluids ignite or the well kicks. Think about it. If you are logging with the BOP off and the well begins to kick out your kill fluid,

what can you do? What can you do if the well that was only making a few thousand begins to come to life and a spark ignites it? With the BOP in the center tub, you can only watch. Thankfully, I do realize, it is an infrequent occurrence that a well ignites during logging or kicks off while running pipe. However, it has happened, with a melted rig too often the consequence. Even if the situation is brought under control without injury or equipment damage, there would be fewer gray hairs if contractors routinely rigged up on a casing head.

Nippling up on a casing head might require you to dig a shallow cellar if the rig has a short substructure or if you are drilling with a top drive without a substructure. Make sure that it is a full opening casing head with clearance to run an open hole packer if the need arises. Running pipe is no more difficult with the BOP on than it is with it off as most slips will clip on the casing, allowing you to land the pipe with the BOP connected.

### 2) Steel BOP Lines

Should you need to close the BOP during a well fire, you will be glad you insisted that the contractor run

steel lines from the accumulator to the BOP. I have many photos that I would be glad to send you of burning rigs with USELESS BOP's in place. It always seems that the area directly around the substructure has enough oil or burnables nearby that rubber hoses rarely survive a fire. I have been surprised to see, that even after a hot well fire, the rubber inside the closing element was in good shape, even closeable if it could have been energized. Again, I know that rubber hoses are considerable easier to rig up than steel lines, but it takes time to pack a good parachute, too!

### 3) Flanged Choke/Bloody Line

Should you have that once in a life time well, that one that you can use in an evening gas patch, "can-you-top-this" B.S. session, you will want to tell the story without any need to cover injuries, especially your own! Since the choke manifold is usually under or in close proximity to the flow-line, it is prudent to make sure that the flow line is flanged to the air-bowl and not attached with a dresser-sleeve connection. Dresser sleeve's hold well in a static condition, but should the flow line jump or move, before or during killing, it might wiggle off, giving you or whoever happens to be manning the choke manifold a better look at the flow than they might care to have.

These set-up suggestions might seem very basic, and could be a source of friction with your contractor. However, once you incorporate them in your plan the extra margin of safety will pay you back when you get that excited call on the radio, "Quick, get out here, you gotta see this well!"

Next month I'll cover some of the mechanics of well control theory.



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## Heating Up Continued from page 14

tion, coal mining landfills and other associated sectors. Although some of the inventories have been completed, this information has not yet been included on EPA's web-page for West Virginia's estimated greenhouse gas emissions. This means that EPA's current greenhouse gas estimates for West Virginia are based on assumptions and limited data, therefore, the EPA's estimated inventory may or may not accurately represent the State's greenhouse gas emissions.

The DEP has pointed to the lack of hard data on West Virginia's greenhouse gas emissions as one reason the inventory bill should be passed. The DEP is concerned that EPA may soon regulate greenhouse gases and this may well happen if the Supreme Court rules against EPA, a future Congress mandates greenhouse gas regulation, or a future Presidential administration reverses EPA's position on this issue.<sup>2</sup> In the past, states with emission inventories for other pollutants have been better equipped to argue for more budget trading credits from EPA when those credits are assigned. Currently, the EPA statewide estimate, which does not even include the DEP's baseline inventories, would be the only basis for assigning emissions credits. The DEP believes that creating the greenhouse gas inventory bill now will have long term benefits to West Virginia emitters by establishing a more accurate and defensible inventory of greenhouse gas emissions.

Despite the DEP's support for this bill, it has failed to advance out of committee due to significant opposition from industry groups. The bill raises two areas of concern for oil and gas operators. First, the term "natural gas/oil systems" is not defined. Will operators have to report emissions from every well,

gathering line, compression station, and transmission pipeline? It is also unclear exactly how oil and gas operators are supposed to measure greenhouse gas emissions from some of these sources. Presumably, these issues would be addressed in the rules promulgated to implement this inventory, but the uncertainty surrounding these issues is problematic. Another issue of particular concern to oil and gas operators is that the bill does not define what level of emissions should be reported as "significant." While the latest version of the bill would have required the DEP to establish a de minimis standard below which an emitter would not have to report. Again, these levels, presumably, would be addressed in subsequent

rulemaking, but without guidance from the Legislature about the level of emissions that should be reported it is impossible to predict where that level will be set and that creates an uncertainty about the full impact of the inventory bill.

The Environmental Committee will continue to monitor the judicial developments and will work with members to formulate IOGA's position on any Greenhouse Gas Inventory bill proposed during the next Legislative Session.

(Footnotes)

<sup>1</sup> From November 2002 to April 2003, IOGA News ran a five-part series on greenhouse gases. These articles provide further background on the issues discussed in this article.

<sup>2</sup> EPA's current position on its authority to regulate greenhouse gas emissions is contradictory to its position on the same issue during the Clinton Administration.

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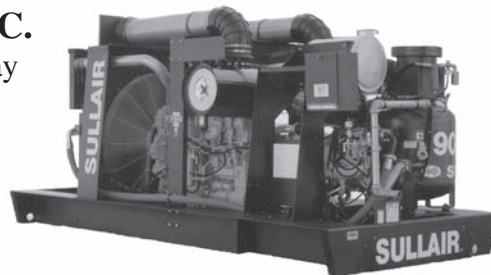
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Burd's Nest Continued from page 4

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IOGA accepts advertising for the IOGA News, as well as other publications. Contact IOGA for advertising rates.

IOGA's purpose is to promote and protect the West Virginia oil and natural gas industry through:

- Identifying and educating our members as to the challenges and opportunities confronting our industry.
- Encouraging and projecting a unity of purpose among our membership.
- Educating the general public and our elected and appointed representatives as to the importance of the industry.
- Protecting and improving the business and natural environment of our state.

The IOGA News is provided to Association members and friends of the industry as a part of our activities to inform and update our members on industry issues and events.

The contents of IOGA News are intended for general information purposes only and should not be read as specific legal, financial, or business advice regarding specific issues or factual events.

We urge you to always consult your legal, financial, and professional advisors with any specific questions you may have.

Readers are encouraged to pass copies of the IOGA News to their friends.

For additional copies of this newsletter or for reprint rights, please contact the IOGA office.

permitting and (9) water replacement regulations; (10) the SERC Tier II filing fees; water issues that include (11) Trout Stream listing, (12) Tier 2.5 stream listing, and the upcoming (13) Triennial Review on water quality; (14) proposed revisions to the STRONGER guidelines.

### Finance and Tax Committee

(15) Guarding against proposed and rumored tax Increases as part of the Governors tax reform package. Implementation of an energy reserve tax, a tax on water withdrawal and a proposed constitutional amendment on property tax minimum valuations is being reviewed.

### Governmental Affairs

Several coal related issues including the (16) sterilization of coal seams, plugging, well location, dominant estate, and general safety concerns; (17) recent negative rulings on royalty payments and flat rate royalty contracts, and a (18) PSC issue defining when a producer comes under utility jurisdiction.

These 18 issues, and those of the unknown variety that lie ahead of us, will demand our fullest attention

in the upcoming months. If one or more of these issues hit home and you want to be involved, you simply need to contact the IOGA office and let us know.

What continues to make IOGA-WV such a strong voice is the Board of Directors' willingness to tackle the tough issues. Their approach is pretty straight forward: they are inclusive of all members in the decision making process; they are unwilling to play politics; they seek the best legal advice; and then in the end, they base their decisions on what is best for all producers over individual interests. And while some might contest these individuals do not always make the most popular decision, you can trust that they have made the right decision.

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Michael J. Zentz, President

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## CALENDAR

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September 14, 2006

**IOGA Sports Weekend**  
**Tailgate Party/WVU Game**  
Morgantown, WV

September 14-17, 2006

**WV Oil & Gas Festival**  
Sistersville, WV

September 19-20, 2006

**North American Coalbed**  
**Methane Forum Fall Session**  
Morgantown, WV

October 11-13, 2006

**Society of Petroleum Engineers**  
**Ohio Petroleum Section**  
**Eastern Regional Meeting**  
The Marriott, Canton, OH

October 15-17, 2006

**IOGCC 2006 Annual Meeting**  
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October 18 - 19, 2006

**OOGA Fall Conference**  
Salt Fork Resort & Conference  
Center, Cambridge, OH

October 23 - 25, 2006

**2006 IPAA Annual Meeting**  
Gaylord Grapevine Hotel  
Grapevine, TX

March 21 - 23, 2007

**Ohio Oil & Gas Association**  
**2007 Annual Winter Meeting**  
Easton Hilton  
Easton Town Center  
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or by properly authorized proxy or ballot mailed to the Executive Director. Such proxy or ballot shall be directly associated with an eligible firm or corporation.

The change to ARTICLE III. Section 4 was necessary to establish the "member in good standing" terminology.

The third and final change to the By Laws was the addition of the new Section 6 in ARTICLE III. That new Section 6 reads:

**Section 6. Member in Good Standing.** The Board of Directors may establish and amend from time to time a due date schedule for payment of membership dues in one or more installments. Each member shall pay all installments on or before the due date set forth in the schedule, or the member shall be delinquent. In the event a delinquent member fails to pay in full any one or more past due installment(s) of membership dues within thirty (30) days of

mailing the Association's notice that one or more installment(s) are past due, then the member shall not be a member in good standing, and all privileges of membership shall automatically be revoked at 5 pm the thirtieth day after the notice is mailed. Notice that the member is past due shall be mailed via certified United States mail to the address shown on the membership application of the delinquent member, or if the member has in writing notified the association of a change of address, then to the changed address. Each member has a duty to notify the association of their current and correct address, and to pay each installment of dues on or before the due date.

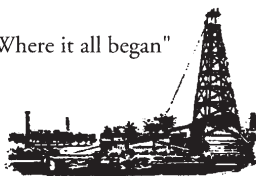
Changes to ARTICLE III, Section 6 were necessary to identify and define "member in good standing", to establish payment and delinquency dates, creates the mechanism in which a company or individual is no longer considered "in good standing", and sets up the procedure to terminate membership.

The due date schedule for payment of membership dues adopted by your Board of Directors, is as follows for the

**Dues Dates** Continued on page 23

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## Tawney Case Continued from page 1

or marketed ...." (W. Va. Code 22-6-8(e)) or sue to challenge the law. Perhaps to lower the possibility of a challenge to the Statute on constitutional grounds, the legislature did not attempt to change the amount payable with respect to wells drilled prior to June 13, 1982, unless those wells were deepened or reworked.

The circuit court's opinion reviews commentaries by well known Professors Robert Donley and Eugene Kuntz, who essentially reported that flat rate royalty leases were negotiated in the early days, when the primary objective of drilling was oil. According to Professor Kuntz, drillers regarded it a misfortune to find gas alone, and while gas had some value, it was difficult to market. Professor Kuntz noted that producing gas held a lease, so a flat rate royalty was included and when pipelines were constructed, gas became valuable, but the parties to a flat rate lease did not foresee that value.

The court also relied heavily on the Flat Rate Royalty Statute. Concerned about a challenge to the statute on constitutional grounds, the Statute made several findings:

That a great portion, if not all, of such leases or other continuing contracts based upon or calling for an annual flat well royalty, have been in existence for a great many years and were entered into at a time when the techniques by which oil and gas are currently extracted, produced or marketed, were not known or contemplated by the parties, nor was it contemplated by the parties that oil and gas would be recovered or extracted or produced or marketed from the depths and horizons currently being developed by the well operators;

That continued exploitation of the natural resources of this state

in exchange for such wholly inadequate compensation is unfair, oppressive, works an unjust hardship on the owners of the oil and gas in place, and unreasonably deprives the economy of the state of West Virginia of the just benefit of the natural wealth of this state;

Before the Roane county judge, CNR (now Chesapeake) ably advanced several reasons longstanding flat rate leases should be enforced as to wells drilled prior to enactment of the Statute, but the court did not agree. Relying on the Statute, the circuit court found that:

"[T]he West Virginia Legislature's declaration of public policy in this case is free from doubt. Its statutory declaration

leaves no question for oil and gas lessees in West Virginia. This continued "exploitation" of natural resources leases in exchange for "wholly inadequate compensation" is "unfair," "oppressive" and works an "undue hardship" on the oil and gas lessors, and "unreasonable deprives" West Virginia economy of the just benefit of the natural wealth of the states. The legislature expressly declared that it is the policy of this state to the extent possible "to prevent the extraction, production or marketing of oil or gas under a ...flat well royalty [lease]."

In the court's view, CNR could not pay "wholly inadequate com-  
**Tawney Case** Continued on page 22



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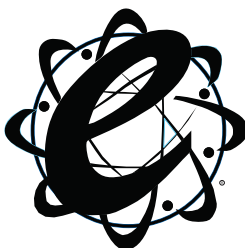
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## Summer Meeting

## Record Crowd Attends Summer Meeting

Over 260 people attended the recently concluded 2006 Summer Meeting at The Greenbrier Resort in White Sulphur Springs, WV.

In addition to the Annual Business Meeting and a Special Membership Meeting to address a proposed By-Laws amendment, those attending also enjoyed a wide variety of IOGA-sponsored activities and a full complement of resort amenities.

Sunday evening's Welcome Reception event held atop Kate's Mountain featured a buffet with grilled lobster and filet that was, in the words of many, "to die for"!!

The Trap and Skeet Tournament held on Monday and Tuesday keeps

growing in popularity with the highest number of participants ever.

The annual Tennis Tournament featured outstanding play in the men's and women's singles, doubles and mixed doubles competitions.

Monday evening's after dinner reception, held in Chesapeake Hall, included a Texas Hold 'em poker tournament for players of all skill levels, a door prize give away, and a fantastic "DJ" spinning tunes.

Tuesday's golf tournament on the Old White Course went off without a hitch. While some of the players might have wished for lower scores, the course was in perfect shape.

Tuesday night's closing recep-

tion and dinner featured nationally known comedian Chris Bliss who kept the IOGA crowd in stitches with his humor and in total amazement with his ability to juggle to Beatles music.

"This was an excellent opportunity for our members and guests to make new friendships, discuss business, and cement existing working relationships through participation in the business sessions and the recreational activities," said IOGA President Denny Harton. "We would especially like to thank our corporate sponsors for their continued support of IOGA and the industry."

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## Tawney Case Continued from page 20

pensation for CNR's operations that represent the continued exploitation of their State's natural resources, where such contract right has been found by the Legislature of this State – some 24 years ago and substantially before the period of gas production involved in this class action case - - to be unfair, oppressive and unjust to Plaintiffs, as royalty owners, and to the people of this State...It simply was never the reasonable expectation or intention of lessees to obtain such windfall profits....[from the]...antiquated, 100 year old flat-rate royalty leases at issue here....—enforcement of these clauses results simply in a monetary windfall to CNR, a windfall beyond the reasonable contemplation of the parties at the time of the execution of these leases, a windfall found and declared by the Legislature of this state to be unjust, oppressive and unfair....”.

Firmly convinced that the flat rate royalty clause could not be enforced, the court then proceeded to decide whether the invalid royalty clauses meant that CNR should lose the leases in issue. The court noted that the royalty was the essence of the lease for the lessor, and if the royalty was void, then the lease might be rescinded. According to the court, rescinding the lease would result in forfeiture by CNR of its windfall profit, but would also forfeit rights to wells drilled or reworked on the same leases where CNR admittedly had since 1982, paid the 1/8<sup>th</sup> royalty provided in the Flat Rate Royalty Statute. Since the Statute only operated prospectively through permit issuance or denial, CNR had by paying the flat rate on old wells and the statutory 1/8<sup>th</sup> on new wells, complied with what CNR believed to be the law. The court believed that rescission could be appropriate, but stopped slightly short of that

result:

...CNR has continued to operate these leases with full knowledge and appreciation of the fact that since 1982, it has been the public policy of this state to discourage to the extent possible extraction of minerals pursuant to these leases, and that these leases are oppressive, unfair and work an unjust hardship on owners of the oil and gas and the people of this state. Having stated the argument, the court has nevertheless concluded that the effects of a forfeiture can and should be mitigated....

While the court emphasized its view that CNR could not reasonably expect to pay the flat rate since 1982, the court recognized that some expectations under the leases

were justifiable, and the leases were unquestionably valid and reasonable when signed. Relying on the court's right to reform or equitably adjust the leases, and the plaintiffs' representation that they would agree to reformation if CNR paid the statutory royalty for the entire period of the class action claims, the court declared that within twenty days CNR could agree that CNR would pay the statutory royalty, or forfeit the leases.

The court's order left CNR to consider how it might proceed, and also left another issue open, that is, how does one calculate "... one eighth of the total amount paid to or received by or allowed to the owner of the working interest at the wellhead for the oil or gas so extracted, produced or marketed ...”.



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## Dues Dates Continued from page 19

## 2006-07 Membership Year:

<u>Total Dues</u>	<u>Payments</u>	<u>Invoice Date</u>	<u>Becomes Delinquent</u>
\$1,500 or less	1	7-1	8-31
\$1,501-\$4,000	2	7-1 1-1	8-31 1-31
\$4,001 - \$10,000	4	7-1 10-1 1-1 4-1	8-31 10-31 1-31 4-30
\$10,001 - \$25,000	12	First working day	Last working day

The IOGA Board of Directors and staff wish to thank the membership for approving the Bylaw changes, and ask that any member who has not paid their current

2006-07 membership dues please do so as soon as possible. Should you have any questions, need additional clarification or if you qualify for and wish to take advantage of

one of the installment options, please contact Charlie Burd at the IOGA Office (304-344-9867) at your earliest convenience.



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