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I. Introduction

Amid the downturn, the Fayetteville Shale of Arkansas has provided some notable state and federal cases during the survey period of August 1, 2015 to July 31, 2016. Below are some of the highlights.

II. Legislative and Regulatory Developments

The Arkansas General Assembly met during the survey period; however, all matters concerning oil and gas dealt with funding the Arkansas Oil and Gas Commission and were not substantive. A few Arkansas Oil and Gas Commission rules took effect in July and March of 2016.[1] Of note, the Commission updated its hearing procedures after the enactment of Senate Bill 778 or Act 906 of the Arkansas General Assembly.[2] The purpose of Act 906 was to give the Commission some flexibility in scheduling hearings without depriving citizens of the opportunity to be heard on issues.[3]

III. Judicial Developments

A. Drilling Not Adverse to Co-Tenant of Minerals

In the quiet title action of *SEECO, Inc. v. Holden*, the Arkansas Court of Appeals determined whether a lessor's possession of minerals was adverse to his co-tenant.[4]

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1. *Commission News and Alerts*, Arkansas Oil and Gas Commission, http://www.aogc.state.ar.us/.

2. ARK. OIL & GAS COMM'N, GEN. RULES AND REGULATIONS A-2, A-3 (2016), http://www.aogc2.state.ar.us/OnlineData/Forms/Rules%20and%20Regulations.pdf. Act 906 was approved by the Arkansas General Assembly on April 1, 2015, one month before the survey period for this paper.

3. *See* Act 906, S.B. 778, 90th Gen Assemb., Reg. Ses. (Ark. 2015).

4. 473 S.W.3d 36 (Ark. App. 2015).

In 1912, Joyce Walls' grandfather, W. M. Howell, acquired fee interest in ninety-five acres in White County; and subsequently in 1948, he sold the land to Raymond and Clotene Cox, reserving an undivided one-half mineral interest.[5] Then in 1952, Raymond and Clotene Cox conveyed to Carver Ray and Ola Holden, Carver L. Holden's parents, the tract of land, save and except the undivided one-half interest in the minerals.[6]

Howell died in 1953, leaving his one-half interest in the minerals to his daughter, Grace Marshall. Due to nonpayment of taxes, Carver Ray Holden bought Grace Marshall's interest in a tax sale in 1958, appearing to unify the surface with all the minerals.[7] Then, Marshall died in 1983, and her interest eventually passed to Joyce Walls.[8] In 2005, Walls executed an oil and gas lease that SEECO later acquired via assignment.[9] There was no drilling conducted on the property.[10]

In 2006, Carver Ray Holden conveyed to Carver L. Holden, his son and the appellee, the ninety-five acres complete with all the minerals.[11] The appellee, then, executed a lease in May 2007 with drilling and production occurring in January 2008.[12] Walls became aware of the producing wells in September of 2009 and filed a quiet-title action, alleging that the 1958 tax sale was void and that she had retained an undivided one-half interest in the minerals.[13] A representative from the White County Tax Collector testified that the one-half interest was improperly recorded in the assessment book, as required by law at the time.[14] This fact made the tax sale void, according to the Court of Appeals.[15]

Holden argued that Walls' claim was time-barred by the two-year statute of limitations.[16] The circuit court agreed with Holden, stating that Walls did not have possession of the mineral rights within two years before filing her lawsuit and that Holden took possession of the minerals in May 2007

5. *Id*. at 37.
6. *Id*.
7. *Id*.
8. *Id*.
9. *Id*.
10. *Id*.
11. *Id*.
12. *Id*.
13. *Id*. at 38.
14. *Id.*
15. *Id.*
16. *Id*.

when he signed the lease.[17] Joyce Walls and her lessee, SEECO, Inc., appealed.[18]

The two-year adverse possession requirement comes from the statute of limitations found in Arkansas Code Annotated section 18–61–106(a) (Repl. 2003), which "has been interpreted to mean that a person holding land (or a mineral estate) by virtue of an invalid tax deed may nevertheless dispossess the legal owner and gain good title if he possesses the property adversely and continuously for two years before the legal owner files suit."[19]

The Court of Appeals said that the adverse possession required by this section "must be of such character as to put the legal owner on notice that his rights are being challenged."[20] Because Walls and Holden are co-owners of the mineral interests, they each had a right to go on the land and drill subject to the duty to account to their co-owner.[21] Holden's drilling was not enough to put Walls on notice that her rights to the land were being challenged.[22] The court held that the statute of limitations did not bar the quiet-title action and remanded the case for further proceedings.[23]

B. No Reformation of Correction Deed to Include Mineral Reservation

In *Elsleger v. Runsick*, the Arkansas Court of Appeals held that a court cannot reform a correction deed to include a mineral reservation.[24]

In December 2007, Jeff Van Runsick and Tonya Runsick conveyed to Kenneth and Gloria Elsleger their home and five acres.[25] That deed contained the following reservation language: "RESERVING AND RETAINING, HOWEVER, unto the GRANTORS all oil, gas and minerals and all oil, gas and mineral rights and interest . . . . This conveyance conveys unto the GRANTEES no oil, gas or minerals and no oil, gas or mineral rights or interests."[26]

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17. *Id*. at 38.
18. *Id*. at 37.
19. *Id*. at 39 (citing Hurst v. Rice, 643 S.W.2d 563 (Ark. 1982); Adams v. Bruder, 627 S.W.2d 12 (Ark. 1982); Sage Land & Lumber Co. v. Hickey, 257 S.W.2d 941 (Ark. 1953); Honeycutt v. Sherrill, 179 S.W.2d 693 (Ark. 1944)).
20. *Id*. at 40; *see Taylor v. Scott*, 685 S.W.2d 160, 161 (Ark. 1985); *Adams*, 627 S.W.2d 12.
21. *Id*.
22. *Id*.
23. *Id*.
24. 479 S.W.3d 43 (Ark. Ct. App. 2015).
25. *Id*. at 45.
26. *Id*.

At the request of the title company, the parties executed two more deeds.[27] Only the Runsicks signed the second deed, entitled "Warranty Deed."[28] This second deed included similar mineral reservation language as the first deed.[29] In March 2008, both the Runsicks and the Elslegers executed a third deed, the "Correction Deed," which its stated purpose was to correct the spelling of Tonya Runsick's name.[30] The correction deed did not include words of grant nor did it include any mineral reservation language.[31]

Finally, in December 2008, an employee of the title company filed an affidavit stating that the third deed failing to mention the mineral reservation was the result of a scrivener's error.[32] Shortly thereafter, the Elslegers requested royalty payments from Chesapeake Operating, Inc.[33] However, before making payments, Chesapeake requested that the Runsicks file a quitclaim deed ensuring all their interest in the minerals went to the Elslegers.[34] The Runsicks filed suit claiming they owned the minerals under the land and asked for reformation of the correction deed to correct the mutual mistake.[35]

The circuit court found that the Runsicks owned the minerals under the land, reforming the correction deed and reasoning that the lack of a mention of the reservation therein was a scrivener's error.[36] The Elslegers appealed.[37] The Court of Appeals decision was narrow, only answering the question of whether reformation was proper and not answering the question as to who owned the minerals.[38] The Court of Appeals said that the district court's reformation of the correction deed was legal error, and the addition of a mineral reservation to such a deed goes beyond the limited scope of what a correction deed can do.[39]

A correction deed that adds reservation or exception language not stated in the original deed burdens the recording system. The same can be said for

27. *Id*.
28. *Id*.
29. *Id*.
30. *Id*. at 47.
31. *Id*. at 45.
32. *Id*. at 46.
33. *Id.*
34. *Id.*
35. *Id.*
36. *Id.* at 47.
37. *Id.* at 48.
38. *See Id*.
39. *Id*.

calling the forgotten mineral reservation or exception a scrivener's error. Adding a reservation or adding a property interest goes beyond the scope of what a correction deed can do. The proper use of a correction deed is narrow in scope and can only be used to correct some facial imperfection in the title, like to correct a defective description of a single property when a deed recites inaccurate metes and bounds or to correct a grantor's name. [citation omitted] Our recording system is designed to allow a person to rely on it without using any outside research.[40]

Like *SEECO*, the court remanded this case back to the district court for additional proceedings.[41]

C. Damages in Breach of Warranty Claim Calculated at Time of Conveyance

In 1987, Bruce Smith and Jan Smith, husband and wife, purchased from Mountain Pine Timber, Inc. what they thought to be all the rights in two tracts of land totaling 250.22 acres in Cleburne County.[42] However, two years prior, Mountain Pine Timber, Inc. sold all the oil and gas under the land to CenArk Oil and Gas Company for $1.00 an acre.[43] The 1987 deed to the Smiths did not mention a reservation or an exception to the minerals.[44] The Smiths did not realize that their ownership of the minerals was in question until they unsuccessfully attempted to sell the minerals in 2008 for $1,500.00 an acre.[45]

In 2010, the Smiths filed a breach of warranty lawsuit against Mountain Pine Timber, Inc., a now-defunct partnership, and eventually added its partners to their complaint.[46] A Cleburne County Circuit Court jury found in the Smiths' favor, awarding them $250.22.[47] The Smiths appealed.[48] The Smiths argued that the circuit court should have calculated their damages based on the value of the minerals at the time of constructive eviction, being 2008, and that the circuit court erred in not allowing them to bring in such evidence.[49]

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40. *Id*. at 50; *see also* Mason v. Jarrett, 234 S.W.2d 771, 774 (Ark. 1950).
41. *Elsleger*, 479 S.W.3d at 50.
42. Smith v. Mountain Pine Timber, Inc., 487 S.W.3d 409, 411 (Ark. Ct. App. 2016).
43. *Id*. at 411, 414.
44. *Id*. at 411.
45. *Id*.
46. *Id*.
47. *Id*.
48. *Id.*
49. *Id.* at 412.

The Court of Appeals disagreed and upheld the circuit court decision, calculating damages for a breach of warranty claim based on the value of the minerals rights at the time of the conveyance and declining to adopt an exception to this general rule.[50]

D. Lessors Did Not Prove Allegedly Fraudulent Notarized Leases Caused Damages

In *Lipsey v. Giles*, the Arkansas Supreme Court affirmed a grant of summary judgment, throwing out a case in which a class of people alleged the Cleburne County Circuit Court Clerk fraudulently notarized oil and gas leases.[51]

Landmen were delivering leases signed by Cleburne County property owners to the clerk's office.[52] The property owners filed suit after they found out the clerk was notarizing the leases without witnessing the property owners' signatures and then recording the instruments.[53] The landowners were not arguing that the landmen illegally procured the leases but that the clerk fraudulently notarized the instruments.[54] They sought an injunction requiring the clerk to inspect all leases received for recording for accuracy and to "purge any and all oil and gas leases which contain false notarial acknowledgments."[55]

During a circuit court hearing, the court dismissed the case sua sponte when it determined that the property owners could not assert any damages.[56] The property owners appealed.[57] The Supreme Court reversed and remanded to the circuit court to determine the damages.[58] Shortly after remand, the clerk filed a motion for summary judgment arguing that the property owners could not prove damages.[59] In determining the damages, the property owners offered evidence from Tom Ferstl, an attorney and certified appraiser.[60] In his affidavit, he swore that leases notarized by the clerk without witnessing the property owners' signatures have had a "chilling effect" on property values "because buyers will be less likely to

50. *Id*.
51. 487 S.W.3d 366 (Ark. 2016).
52. *Id.* at 368.
53. *Id*.
54. *Id*.
55. *Id*.
56. *Id*.
57. *Id*.
58. *Id*.
59. *Id*.
60. *Id*.

purchase property there knowing the uncertainty in the official county-property records."[61] The circuit court determined that the property owners had not proven damages and granted the motion for summary judgment.[62] The property owners appealed.[63]

The Supreme Court agreed with the circuit court, stating "conclusory allegations are insufficient to create a factual issue in a summary-judgment situation."[64] The evidence proffered did not rely on facts to support the claim of a "chilling effect."[65]

E. Assignee Not Liable for Predecessors Actions

The only federal case included in this summary is *Walls v. Petrohawk Properties, LP*, from the Eighth Circuit Court of Appeals.[66] Zelda Walls, individually and as surviving spouse of Arlie Walls, filed suit against Petrohawk alleging that the company materially breached a certain oil and gas lease due to acts committed by previous working interest owners.[67]

The Walls entered into a lease with Griffith Land Services in 2005, which called for a three-sixteenth royalty and contained an assignment provision that stated, "Lessee shall obtain written consent from Lessor before assigning lease to a third party which consent shall not be unreasonably withheld."[68]

Griffith Land Services assigned the lease to Alta Resources, LLC, who then assigned the lease to Petrohawk.[69] This was all done without acquiring consent from the Walls.[70] Additionally, Petrohawk did not pay the Walls the full royalty owed under the terms of the lease.[71]

In May of 2010, the Walls' attorney notified the Petrohawk by letter of the underpayment of royalties.[72] The letter also noted that Walls signed the lease with Griffith Land Services, and it was their understanding that

61. *Id*.
62. *Id*. at 369.
63. *Id*.
64. *Id*. (citing Sundeen v. Kroger, 133 S.W.3d 393 (Ark. 2003)).
65. *Id*.
66. 812 F.3d 621 (8th Cir. 2015).
67. *Id.* at 623.
68. *Id*.
69. *Id.*
70. *Id.*
71. *Id.*
72. *Id.*

Petrohawk currently held the lease.[73] After an internal audit, in October 2010, Petrohawk cut a check for $200,000.00, which the Walls cashed.[74]

Subsequently in December 2010, Petrohawk sent a letter to the Walls requesting their consent to assign the lease to Exxon Mobil Corporation.[75] Walls' attorney responded by sending Petrohawk a letter stating previous assignments of the lease without consent constituted a breach and requesting more information regarding why assigning the lease to Exxon would be in the best interest of Walls.[76] Walls filed suit the next day.[77] Petrohawk did not respond to Walls' letter and assigned the interest in the lease to Exxon later that month.[78]

In the suit, Walls claimed that Petrohawk materially breached the lease by not obtaining consent to assign the lease and for not paying the total royalty amount due.[79] Walls claimed Petrohawk was liable for the additional royalties owed by Alta, the predecessor in interest, and for a statutory fourteen percent per annum penalty for fraudulently withholding royalty payments.[80]

On summary judgment motion, the district court found that Petrohawk did not materially breach the lease.[81] In regards to the royalty payments, the court held that Petrohawk's 2010 payment cured any breach, and the Walls subsequently waived any breach by accepting the payment.[82] Additionally, the Walls also waived the ability to protest the assignments before Exxon and unreasonably withheld consent to assign to Exxon.[83] Walls appealed.[84] The Eighth Circuit Court of Appeals upheld the lower court rulings.[85]

The appellate court first addressed the issue of royalties, stating that "Arkansas courts have generally not considered nonpayment of royalties a material breach."[86] Citing *Schaffer v. Tenneco Oil Co.*, the appellate court said, "[w]here there is no cessation of marketing of oil and gas for a

73. *Id.*
74. *Id*.
75. *Id*. at 624.
76. *Id*.
77. *Id.*
78. *Id.*
79. *Id.*
80. *Id.* (citing ARK. CODE ANN. § 15-74-602).
81. *Id*.
82. *Id.*
83. *Id.*
84. *Id.*
85. *Id.* at 628.
86. *Id*. at 625.

substantial period but only the nonpayment of royalties, the lessors generally have a plain, speedy, and adequate remedy at law for damages."[87] The appellate court said that the payment of royalties was secondary to extracting, developing and marketing the minerals under the land, which Petrohawk continued to do.[88] To be made whole, Petrohawk just needed to pay the Walls what was owed. Termination of the lease was not the right remedy. The appellate court held that the nonpayment of royalties in the case was not a material breach.[89] The appellate court also mentioned that if it were to consider the nonpayment of royalties a breach, the Walls waived the breach by accepting the 2010 payment.[90]

The second claim the appellate court addressed was the failure to obtain consent from the Walls to assign the lease.[91] The Court found that the Walls waived all the breaches prior to the Petrohawk-Exxon assignment by the May 2010 attorney letter, wherein the attorney noted that Petrohawk was the working interest holder, and the subsequent acceptance of the payment.[92] The appellate court found that the Walls unreasonably withheld consent to the Petrohawk-Exxon assignment because Walls did not allow Petrohawk to respond to her question regarding the reason for the assignment before filing suit.[93]

Next, the appellate court addressed the issue of whether Petrohawk was liable for the shortfall of royalty payments Alta owed Walls.[94] The appellate court said that the language of the lease does not support the argument that Petrohawk is liable, stating it is only "liable for obligations arising subsequent to the date of assignment."[95]

Lastly, the appellate court found that Walls did not provide any factual allegations of Petrohawk willfully or in bad faith withholding royalty payments; therefore, Petrohawk was not subject to the statutory penalty.[96]

87. *Id*. (citing *Schaffer*, 647 S.W.2d 446, 447 (Ark. 1983)).
88. *Id*.
89. *Id*.
90. *Id*. at fn. 2.
91. *Id*.
92. *Id*. at 626.
93. *Id*.
94. *Id*.
95. *Id*.
96. *Id*. at 627.