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## Kentucky

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## KENTUCKY



*Sarah M. Lange*

### *I. Introduction*

In the past twelve months, the U.S. Environmental Protection Agency (“EPA”) granted primacy of the Class II Underground Injection Control program to the Commonwealth of Kentucky; Letcher County’s Fiscal Court proposed an unprecedented local tax, which ultimately failed, that would have applied to each un-reclaimed oil and gas well; the United States District Court, Western District of Kentucky, Owensboro Division, clarified the rights of oil and gas mineral owners in their use of surface property; the Supreme Court of Kentucky addressed a trespass case against a pipeline

operator, and the United States District Court for the Sixth Circuit addressed challenges to oil and gas leases under the False Claims Act.

## *II. Legislative and Regulatory Developments*

### *A. Changes to the Underground Injection Control Program*

The EPA granted primary enforcement authority (primacy) of the Class II Underground Injection Control (“UIC”) program to the Commonwealth of Kentucky on March 21, 2017.<sup>1</sup> As required by regulation, all owners or operators are required to submit to the Kentucky Division of Oil & Gas within 90 days a demonstration of adequate financial responsibility to plug and abandon a well.<sup>2</sup> The EPA Region 4 approved the Cabinet’s longstanding application, effective March 21, 2017 and delegation of the UIC-Class II program from the EPA allows the Kentucky Division of Oil & Gas more comprehensive regulatory enforcement of the oil and natural gas industry.

“This action by the EPA will allow us to give Class II wells increased oversight, which will add another layer of protection to drinking water sources,”<sup>3</sup> said Energy and Environment Cabinet Secretary Charles Snively. “In addition, the public and industry will benefit from a centralized permitting process and regulatory oversight.”<sup>4</sup>

“The Class II program regulates the injection of produced fluids associated with oil and gas operations into wells for enhanced oil recovery and permanent brine disposal.”<sup>5</sup> “[The Kentucky] Division of Oil and Gas will receive a \$143,000 annual EPA grant to help defray the cost of administering the program.”<sup>6</sup> “Under EPA Region 4’s prior oversight, there were two contract EPA inspectors responsible for overseeing Kentucky’s 900 active UIC Class II enhanced recovery wells and 82 Class II disposal wells. The Kentucky Division of Oil & Gas has 14 inspectors for

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1. State of Kentucky Underground Injection Control (UIC) Class II Program; Primacy Approval, 81 FR 95480-01.

2. 805 KY. ADMIN. REGS. 1:110(8).

3. Press Release, Ky. Energy & Env’t Cabinet, EPA Delegates Regulation of Injection Wells to Division of Oil and Gas (Mar. 22, 2017), *available at* <http://dnr.ky.gov/Lists/NewsReleases/EPA%20Delegates%20Regulation%20of%20Injection%20Wells%20to%20Division%20of%20Oil%20and%20Gas.pdf>.

4. *Id.*

5. *Id.*

6. *Id.*

the same coverage and intends to add additional employees through the EPA grant.”<sup>7</sup>

#### *B. The Rejected Letcher County Extraction Tax*

Although it was ultimately voted down, the Letcher County Fiscal Court proposed an ordinance in March 2017 attempting to enact a business tax on all extraction based industries of \$2,500 annually for each well within Letcher County, whether producing or shut-in, that has not been completely reclaimed, including a heavy monthly penalty. This tax—an effort by Letcher County officials to counter a crippling drop in coal severance tax collections—however, was met with an overwhelming amount of negative publicity and created an immense amount of fear and pushback by industry leaders, who stated that the tax, if enacted, would jeopardize the economic future of Kentucky’s oil and gas industry. The Letcher County Fiscal Court subsequently voted down their tax on the industry in a special-called meeting where the final vote count was tied three-to-three, meaning two magistrates changed their votes during the meeting and the ordinance died.

### *III. Judicial Developments*

#### *A. Supreme Court of Kentucky – Trespass*

In *Fleming v. EQT Gathering, LLC*, the Appellants filed a civil action in the circuit court alleging that EQT had trespassed upon their land after EQT constructed a natural gas pipeline along the boundary of Appellants’ property.<sup>8</sup> After a jury trial, the circuit court ruled in favor of Appellants and awarded compensatory and punitive damages.<sup>9</sup> The court of appeals vacated the judgment, concluding that the trial court erred by directing a verdict in Appellants’ favor on the issue of liability and submitting only the issue of damages for the jury’s determination.<sup>10</sup> The court of appeals further concluded, *sua sponte*, that adjoining landowners must be included as parties on remand before the trespass claim could be resolved.<sup>11</sup> The Supreme Court of Kentucky affirmed in part and reversed in part, holding (1) the trial court erred in directing a verdict on the issue of EQT’s liability for the trespass but (2) the court of appeals erred in determining that the adjoining landowners were indispensable or necessary parties to the

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7. *Id.*

8. 509 S.W.3d 18, 20 (Ky. 2017).

9. *Id.* at 21.

10. *Id.*

11. *Id.* at 22-23.

trespass claim and in mandating their involuntary participation in the action.<sup>12</sup> The case was remanded.

*B. United States Court of Appeals, 6th Circuit – Challenging Leases Under the False Claims Act*

*USA ex rel. Harper v. Muskingum Watershed Conservancy District* is an appeal in which the relators challenged the Muskingum Watershed Conservancy District's ("MWCD") oil and gas leases under the False Claims Act.<sup>13</sup>

"In 1949, the federal government deeded a large parcel to the MWCD, [which controls] flooding in eastern Ohio. The deed provided that the land would revert to the United States if MWCD alienated or attempted to alienate it, or . . . stopped using the land for recreation, conservation, or reservoir-development purposes."<sup>14</sup> MWCD sold rights to conduct hydraulic fracturing ("fracking") operations on the land.<sup>15</sup> Fracking opponents discovered the deed restrictions and, arguing that MWCD's sale of fracking rights triggered the reversion, filed a "qui tam" suit under the False Claims Act, 31 U.S.C. 3729 ("FCA"), alleging that MWCD was knowingly withholding United States property from the government.<sup>16</sup>

The Sixth Circuit affirmed dismissal of the claim.<sup>17</sup> The court noted, "recent legislative amendments that replace a fraudulent-intent requirement in two FCA provisions with a requirement that the defendant acted 'knowingly,'" but concluded that the plaintiffs failed to state a claim, "even under the more lenient scienter requirement."<sup>18</sup> Plaintiffs did not specify whether or how MWCD knew or should have known that it was in violation of the deed restrictions, such that it knew or should have known that title to the property reverted to the United States.

*C. United States District Court, Western District of Kentucky – Rights of Mineral Owner to the Surface Estate*

In *Bickett v. Countrymark Energy Resources, LLC*, the owner of surface area filed suit against the owner of mineral rights, seeking compensation for

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12. *Id.* at 25.

13. 842 F.3d 430, 438 (6th Cir. 2016).

14. *Id.* at 432.

15. *Id.*

16. *Id.* at 432-33.

17. *Id.* at 440.

18. *Id.*

damages allegedly arising from the drilling operations.<sup>19</sup> Between 1966 and 1991, Ashland Oil and Refining Company drilled seventeen oil and gas wells on the property, built access roads, installed electric lines and poles and gates at certain access points.<sup>20</sup> In 1991, Ashland transferred the mineral rights to Geigo Company LLP, who drilled one additional well. And in 2010, Geigo transferred the mineral rights to the Defendant, who engaged in seismic testing on the property, resulting in crop damage.<sup>21</sup>

The language in the deed that reserved the minerals stated that the owner has the right to “*such use of the surface areas of the property conveyed hereby which is reasonably necessary* to prospect, explore, mine, operate, produce, store and remove minerals, provided however, that the owner or owners of the mineral rights shall be liable to the owner of the surface area for actual damages caused thereby to the surface, improvements, livestock and growing crops.”<sup>22</sup> “The rights granted to the mineral owner in the deed clearly gave the mineral owner a dominant easement.”<sup>23</sup>

“Under well-established Kentucky law, ‘an oil and gas lease, or owner of minerals, unless expressly limited by the terms of the lease or conveyance, has the right to use and occupy so much of the surface as may be necessary and reasonably convenient in the exercise of his rights in operating his facilities and marketing the oil and gas, even to the preclusion of any other surface possession.’”<sup>24</sup> “The mineral and surface owner “have correlative rights and duties which neither may unreasonably exercise to the injury of the other.”<sup>25</sup> “Thus, the owner of minerals may become liable to the surface owner if the surface owner suffers injury from the mineral owner’s negligence in its use of the land, and vice versa. III.”<sup>26</sup> “Additionally, [the mineral owner] ‘shall not utilize any more of the surface estate than is reasonably necessary for exploration, production and development of the mineral estate.’”<sup>27</sup>

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19. No. 4:15-CV-00093-GNS-HBB, 2017 WL 1228418, at \*2 (Mar. 31, 2017).

20. *Id.*

21. *Id.* at \*3.

22. *Id.* at \*1 (emphasis in original).

23. *Id.* at \*4; see *Wells v. N.E. Coal Co.*, 274 Ky. 268, 118 S.W.2d 555, 556 (1938).

24. *Bickett*, 2017 WL 1228418, at \*4 (quoting *Lindsey v. Wilson*, 332 S.W.2d 641, 642 (Ky. 1960)).

25. *Id.* (quoting *Higdon v. Ky. Gas Transmission Corp.*, 448 S.W.2d 655, 657 (Ky. 1969)).

26. *Id.* (quoting *Basin Oil Ass’n v. Lynn*, 425 S.W.2d 555, 558 (Ky. 1968)).

27. *Id.* (quoting *Chesapeake Appalachia, LLC v. Williams*, No. 7:10-87-KKC, 2012 WL 2178859, at \*3 (E.D. Ky. June 13, 2012)).

“Plaintiffs allege[d] that the access roads and wells on the property utilized more surface area than was reasonably necessary to conduct its drilling operations,”<sup>28</sup> however, the Court reiterated that the Defendant has a right, as the mineral owner, to use as much of the surface estate as reasonably necessary to conduct their drilling operations and dismissed said claims.<sup>29</sup> The Plaintiffs further claimed that the electric lines and poles utilized more of the surface area than was reasonably necessary and were an unreasonable use of the land because of the danger that the structures pose;<sup>30</sup> that the access gates were being maintained by the Defendant in an unsafe condition;<sup>31</sup> and that maintenance of the access roads and well sites interfered with their use of the surface estate because grasses around the wellheads were not sprayed or mowed.<sup>32</sup>

The court held that (i) Kentucky’s five-year statute of limitations for injuries to rights not arising on contract applied to the claim that access roads and wells utilized more surface area than reasonably necessary; (ii) the doctrine of laches barred claims related to access roads and wells; (iii) Kentucky’s five-year limitations period for noncontract claims began to run on the date the lines and poles were completed; (iv) the surface area owner did not own access gates or pipe bridges on the property; and (v) the surface area owner had the duty to mow and spray areas around the wellheads.<sup>33</sup>

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28. *Id.*

29. *Id.* at \*7.

30. *Id.* at \*8.

31. *Id.* at \*9.

32. *Id.* at \*11.

33. *Id.* at \*12.