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Introduction of Oil and Gas Development

This article provides an update concerning oil and gas law developments in the Commonwealth of Kentucky from August 01, 2019, through July 31, 2020, and focuses on major legislative and regulatory enactments, as well as developments in Kentucky common law.

I. Legislative and Regulatory Developments

The Kentucky General Assembly's regular session began on January 7, 2020, and was scheduled to conclude on April 15, 2020. However, due to the unprecedented COVID-19 pandemic, the regular session was suspended a week early on April 8, 2020. The following is a discussion of the notable legislation relating to oil and gas law passed during the shortened regular session.

*A. House Bill 44**1. "Key Infrastructure Assets."*

House Bill 44 ("HB 44") amends Kentucky Revised Statute Chapter 168, Section 1, by adding to the definition of "key infrastructure assets" any critical system used in the production or generation of energy. Subsection(1)(a) of Section 1 is a list defining certain "key infrastructure assets" in the Commonwealth of Kentucky. HB 44 adds to Section 1, Subsection 1(a)(5) that natural gas or petroleum pipelines are types of pipelines covered under the definition.¹

*B. Senate Bill 55**1. "Blockchain Technology Working Group."*

Senate Bill 55 ("SB 55") adds an entirely new section to Kentucky Revised Statute Chapter 42, Section 747, the creation of Blockchain Technology Working Group ("Working Group"). Blockchain technology allows computer systems to connect over the internet and share or distribute data, transactions, contracts, etc.² Working Group is intended to be attached to the Commonwealth Office of Technology for administrative purposes. Under SB 55, the Working Group evaluates the feasibility and efficacy of using blockchain technology to enhance the security and increase protection for that state's critical infrastructure, including the electric utility grid, natural gas pipelines, drinking water supply and

1. H.B. 44, 2020 Gen. Assemb., 2020 Reg. Sess. (Ky. 2020).

2. S.B. 55, 2020 Gen. Assemb., 2020 Reg. Sess. (Ky. 2020).

delivery, wastewater, telecommunications, and emergency services.³ The Governor of Kentucky signed SB 55 into law on April 24, 2020.

II. Judicial Developments

A. EQT Prod. Co. v. Big Sandy Co.

EQT Prod. Co. v. Big Sandy Co., is a published decision from the Court of Appeals of Kentucky.⁴ Accordingly, it is binding in the Commonwealth of Kentucky unless overruled by the Kentucky Supreme Court. On appeal, EQT Production Company and EQT Gathering, LLC (collectively, "EQT") argued that the circuit court erred as to the following: (1) ruling it must pay to relocate pipelines and (2) that it could not recover payments mistakenly made to Big Sandy Company, L.P. ("Big Sandy"). In a cross-appeal, Big Sandy argued that the circuit court erred in its interpretation of the phrase "coal workings, extend or projected."

This case involved contractual rights outlined in two deeds addressing coal, oil, and gas on property (56,000 acres) located in Pike County, Kentucky. In 1926, predecessors of Big Sandy conveyed oil and gas interests in and to a portion of the lands to R. J. Graf. They retained rights to the coal, all minerals, and surface ownership, with the intent to mine and remove the coal and other minerals within the property. In 1928, Big Sandy conveyed the oil and gas to predecessors of EQT with language similar to the first deed. According to the terms of the two deeds, EQT was obligated to pay Big Sandy a royalty of 1/8 of oil produced from the property and coal left in place around a well.⁵ Moreover, EQT was required to interfere as little as reasonably possible with Big Sandy's right to remove coal and other minerals and obtain approval for "[t]he location of any oil or gas well through coal workings, extended or projected."⁶

With respect to the issue regarding whether EQT must pay to relocate pipelines, the Court of Appeals took a *de novo* review of the following language:

[EQT] agrees to so use said land to so treat same and to so put and use his pipelines, pumps, and buildings upon same as to interfere as little as may be reasonably possible with the mining and removal of said coal and other minerals, and to cause no

3. *Id.*

4. *EQT Prod. Co. v. Big Sandy Co.*, 590 S.W.3d 275 (Ky. Ct. App. 2019).

5. *Id.* at 280.

6. *Id.* at 280.

unnecessary damage and waste to the remaining estate in the lands, the coal, other minerals, surface, fencing, building or timber and that whether said buildings, fencing or timber are now on said land or may hereafter be placed thereon by the first party, its successors or assigns lessees or tenants, and shall pay for any damage done while using said land to crops or fences.⁷

An unambiguous written contract must be strictly enforced according to the plain meaning of its express terms and without resort to extrinsic evidence.⁸ Even if the contracting parties may have intended a different result, a contract cannot be interpreted contrary to the plain meaning of its terms.⁹ The circuit court interpreted the language as "if EQT's pipeline operations interfered more than as little as reasonably possible, EQT must pay to relocate the pipelines."¹⁰ EQT asserted that the interpretation "gives Big Sandy unbridled discretion to decide if and when EQT's pipeline must be moved at their expense."¹¹ However, the Court found that the circuit court's interpretation did not rule that EQT's pipeline needed to be relocated, that relocation would occur "*only if*" pipelines interfered more than a little as reasonably possible with Big Sandy's operation (emphasis added). Moreover, the Court noted, the payment of relocation only occurs if EQT violates the language.

As to EQT's second argument, the standard of review on appeal of summary judgment is whether the trial court correctly found that (1) there was no genuine issue to any material fact and (2) that the moving party was entitled to judgment as a matter of law. According to the facts, in 2000, the mistaken royalty payments were paid after a change in the payment system. EQT stated they had no reason to review the payment system without a request from the owner of the royalty, and Big Sandy waited more than four years before notifying EQT of the payment mistake.¹² In its appeal, EQT did not dispute that it had all necessary information to discover the mistaken payments. EQT's corporate representative testified that all information needed to identify the overpayment was at EQT's disposal.¹³ A simple review of payment history, the mistake would have been discovered. There was no disputed issues of material fact to decide.

7. *Id.* at 285.

8. *Id.* (citing *Allen v. Lawyers Mut. Ins. Co.*, 216 S.W.3d 657 (Ky. App. 2007)).

9. *Id.* (citing *Abney v. Nationwide Mut. Ins. Co.*, 215 S.W.3d 699, 703 (Ky. 2006)).

10. *Id.* at 285, 286.

11. *Id.* at 286.

12. *Id.* at 288.

13. *Id.* at 288.

Big Sandy argued that the phrase "extended or projected" applied to all mineable and merchantable coal, contrary to the circuit court's interpretation that such phrase applied only to coal that Big Sandy provided intent to mine.¹⁴ The circuit court found "extended or projected" as an unambiguous phrase. An unambiguous phrase must be interpreted according to the plain meaning of its express term. The "fact that one party may have intended different results" is not enough to construct the words differently.¹⁵ The phrase appears twice in the deeds mentioned above. The first limited EQT's ability to drill through air courses of mines that were already in place or any coal mine "in operation or temporarily shut down."¹⁶ The second use must accord to the same meaning as the first; a different meaning would be inconsistent. Therefore, the second use of the phrase would limit EQT to the existing activity of Big Sandy; if Big Sandy wanted all mineable and merchantable coal, the phrase would not have been included.

Therefore, the Court of Appeals found no error in the circuit court's ruling and affirmed its decision.

B. Crisp v. Blackridge Appalachian Land, LLC.

Crisp v. Blackridge Appalachian Land, LLC, is an unpublished opinion from the Court of Appeals of Kentucky.¹⁷ In this case, Thomas Crisp, James Larger, Magnum Drilling of Ohio, Inc., and Magnum Drilling, Inc. (collectively, "Magnum") appealed a declaratory judgment from the Lawrence County Circuit Court, which held that a natural gas lease Magnum held had expired.

In 1980, Sam and Joyce Caudill executed an oil and gas lease to Burchett Investment Corporation on property known as the Blackburn Property. Magnum purchased the lease in 2000, which property was owned by Anna Rae Blackburn ("Ms. Blackburn"). The property contained one gas well from which Ms. Blackburn and members of the Blackburn family had rights to free gas. Magnum intended to drill new wells on the property due to the one prior well not producing much gas. However, before drilling any new wells, Magnum and Ms. Blackburn had a falling out, and Ms. Blackburn ousted Magnum from the Blackburn Property. Magnum adhered to the request and has not entered the property or removed gas from the original

14. *Id.* at 290.

15. *Id.* at 291 (citing *Abney*, 215 S.W.3d 657).

16. *Id.* at 291.

17. *Crisp v. Blackridge Appalachian Land, LLC*, 2019-CA-000991-MR, 2020 WL 1898371 (Ky. Ct. App. Apr. 17, 2020).

well since 2000. In 2015, Ms. Blackburn executed a new oil and gas lease covering the Blackburn Property to Bigstar Energy, L.P., because she believed the previous lease had terminated according to its terms, as there had been no production from the well since 2000.¹⁸

Magnum argued on appeal that there was a sufficient quantity of gas produced on the property to keep the lease from termination. For an oil or gas well to be deemed as producing, the well must produce oil or gas in paying quantities.¹⁹ Quantities must be substantial enough to pay the lessor a royalty.²⁰ Based on the facts, Ms. Blackburn never received a royalty payment for the well located on the Blackburn Property. For over a decade Magnum never built, permitted, or drilled any new wells on Blackburn Property. Although Ms. Blackburn ousted Magnum from entering the Blackburn Property, Magnum took no action to enter the Blackburn Property after the oust. The Court of Appeals agreed with the trial court that Magnum's well had produced no gas; therefore, under the terms of the lease, the lease had terminated.²¹

Magnum further argued the circuit court erred in determining whether gas was produced in paying quantities. The determination of whether gas is produced in paying quantities is a question of fact.²² The court received no meter readings or measurements of the amount gas used in the houses on the Blackburn Property, just speculative testimony of the possibility of free gas being enough to warrant paying quantities.²³ Magnum failed to show the production of gas on the Blackburn Property in over ten years.

For the aforementioned reasons, the Court of Appeals found no error in the circuit court's ruling and affirmed the circuit court's decision.

18. *Id.* at 1.

19. *Id.* at 2. (citing *Sawyer v. Potter*, 223 Ky. 359, 3 S.W.2d 758, 759 (1928)).

20. *Id.* at 2. (citing *Cumberland Contracting Co. v. Coffey*, 405 S.W.2d 553 (Ky. 1966)).

21. *Id.* at 2.

22. *Id.* at 2. (citing *Warfield Natural Gas Co. v. Allen*, 248 Ky. 646, 59 S.W.2d 534, 537 (1933)).

23. *Id.* at 2.