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# Montana

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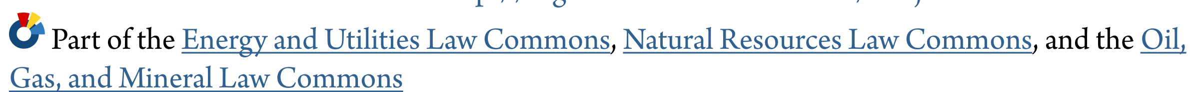
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# ONE J

*Oil and Gas, Natural Resources, and Energy Journal*

VOLUME 2 NUMBER 3

## MONTANA

*Jessica E. McDonald*[*]

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## *I. Introduction*

This Article summarizes important developments in Montana oil and gas law that occurred between August 1, 2015 and July 31, 2016. Part II deals with legislative and regulatory developments, and Part III addresses common law developments in both State and Federal courts.

## *II. Legislative and Regulatory Developments*

### *A. State Legislative Developments*

The 64th Session of the Montana Legislature adjourned, *sine die*, on April 28, 2015.[1] Thus, there were no new statutory developments during the timeframe of this Article. The Legislature will reconvene January 2, 2017.[2]

### *B. State Regulatory Developments*

Effective April 23, 2016, the definitions of "stripper well bonus" and "stripper well exception" pertaining to crude oil were changed to apply to oil prices at $54 per barrel. The prior definitions applied to oil at $38 per barrel.[3]

## *III. Judicial Developments*

### *A. Montana Supreme Court Cases*

#### *1. Interstate Explorations, LLC v. Morgen Farm and Ranch, Inc.*

In *Interstate Explorations, LLC v. Morgen Farm and Ranch, Inc.*,[4] the Montana Supreme Court affirmed the trial court's denial of a motion to dismiss for lack of subject matter jurisdiction. Landowner Morgen Farm and Ranch, Inc. ("Morgen") leased its mineral rights to a predecessor of

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1. *2015 Regular Session,* MONTANA LEGISLATURE (MAR. 22, 2016, 11:28 AM) http://leg.mt.gov/css/Sessions/64th.defualt.asp, (last visited Sept. 20, 2016).

2. *65th Legislature-Tentative 2017 Session Calendar-Adopted May 19, 2016 by Legislative Council*, MONTANA LEGISLATURE (May 24, 2016), http://leg.mt.gov/content/sessions/65th/2017sessioncalendar052416.pdf (last visited Sept. 20, 2016).

3. MONT. ADMIN. R. 42.25.1801.

4. 2016 MT 20, ¶ 1, 382 Mont. 136, 137, 364 P.3d 1267, 1267 (Mont. 2016).

Interstate Explorations, LLC ("Interstate"), which subsequently acquired the leasehold rights and drilled a well on Morgen's property.[5] After Morgen refused to execute an easement needed to install power lines to operate the well, Interstate filed suit in the District Court of the Seventh Judicial District, Wibaux County, seeking a declaration that Morgen had wrongfully denied the easement and affirming Interstate's rights in the property.[6] Morgen asserted counterclaims alleging hydrocarbon spills on the property and requested damages.[7] Interstate responded by filing a motion to dismiss for lack of subject matter jurisdiction, claiming Morgen had failed to exhaust its administrative remedies before seeking damages.[8] The trial court denied Interstate's motion to dismiss.[9]

On appeal, Interstate argued that the District Court lacked subject matter jurisdiction to hear Morgen's counterclaims for damages since Morgen was required to first exhaust administrative remedies under the Surface Owner Damage and Disruption Compensation Act ("Act").[10] In other words, Interstate argued that the Montana Administrative Procedure Act governed Morgen's claims, and that the proper course was to go before the Montana Board of Oil and Gas Conservation ("Board").[11]

The Supreme Court of Montana disagreed, finding that the Board has no direct enforcement authority pursuant to the Act's dispute resolution process.[12] Additionally, the Court pointed out that even if the Board did have such authority, the Act provides that it is not an exclusive remedy.[13] The Court therefore affirmed the District Court's denial of Interstate's motion to dismiss Morgen's counterclaims for damages.[14]

*2. Wicklund v. Sundheim*

In *Wicklund v. Sundheim*, the Montana Supreme Court heard an appeal of a decision by the Richland County District Court in which it interpreted an oil and gas royalty reservation contained in a 1953 deed.[15] The original grantors in the deed were the Teisingers, now represented by Wicklund,

5. *Id.* ¶ 3, 382 Mont. at 137, 364 P.3d at 1267.
6. *Id.* ¶ 4, 382 Mont. at 137-38, 364 P.3d at 1267.
7. *Id.* ¶ 5, 382 Mont. at 137-38, 364 P.3d at 1267.
8. *Id.*
9. *Id.*
10. *Id.* ¶ 9, 382 Mont. at 138, 364 P.3d at 1268.
11. *Id.* ¶ 9, 382 Mont. at 138, 364 P.3d at 1269.
12. *Id.* ¶ 13, 382 Mont. at 140, 364 P.3d at 1269.
13. *Id.* ¶ 14, 382 Mont. at 140, 364 P.3d at 1270.
14. *Id.*
15. 2016 MT 62, ¶ 1, 383 Mont. 1, 2, 367 P.3d 403, 406.

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trustee, and the original grantees were the Sundheims, now represented by their heirs.[16] A dispute between the parties arose when an oil and gas developer began exploration and development on the Sundheims' property around 2012 but refused to issue payment until the successors to the parties to the 1953 deed either signed a stipulation of interest, or filed a quiet title action asking a court to interpret the deed's royalty reservation.[17]

Wicklund then filed suit to quiet title and asked the court to interpret the following reservation:

> First parties reserve unto themselves three-fifths (3/5ths) of Land owners [sic] oil, gas and mineral royalties and three-fifths (3/5ths) of any and all delay rentals on present and existing oil and gas leases now of record against the lands herein described; the conveyance herein is made subject to such oil and gas leases and any and all assignments now of record.[18]

The trial court acknowledged that the reservation language was ambiguous and heard testimony from an English professor who opined that the phrase "on present and existing oil and gas leases" modified both "royalties" and "delay rentals."[19] After a two day trial, the court resolved the ambiguity in favor of the grantees and held that the reservation of 3/5ths of the royalty applied only to the lease in existence at the time of the deed.[20] Wicklund appealed.

While the Supreme Court of Montana agreed that the reservation language was ambiguous, it disagreed with the trial court's failure to consider extrinsic evidence in light of that ambiguity.[21] Specifically, although the lease in place at the time of the 1953 deed was released in 1958, the successors to the original parties shared royalties from subsequent leases in the 3/5ths and 2/5ths proportions set out in the royalty reservation cited above *and* entered into a royalty stipulation as to this split in the 1970s.[22] Finding this evidence highly probative, especially when construed in light of the principle set forth in MCA § 70-1-516 of resolving reservations in favor of grantors, the Court interpreted the reservation in

16. *Id.* ¶ 3, 383 Mont. at 3, 367 P.3d at 406.
17. *Id.* ¶ 5, 383 Mont. at 4, 367 P.3d at 406.
18. *Id.* ¶ 3, 383 Mont. at 3, 367 P.3d at 406.
19. *Id.* ¶ 11, 383 Mont. at 5, 367 P.3d at 407.
20. *Id.* ¶ 12, 383 Mont. at 5, 367 P.3d at 407.
21. *Id.* ¶ 27, 383 Mont. at 9, 367 P.3d at 410.
22. *Id.* ¶¶ 30-31, 383 Mont. at 10-11, 367 P.3d at 410-11.

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favor of the original grantors and remanded with instructions to enter a judgment quieting title to Wicklund.[23]

### *B. Federal Courts*

#### *1. Montana Environmental Information Center v. U.S. Bureau of Land Management*

In *Montana Environmental Information Center v. U.S. Bureau of Land Management*,[24] the United States Court of Appeals for the Ninth Circuit reversed a decision by the Federal District Court for the District of Montana that held environmental groups do not have standing to challenge the Bureau of Land Management's sale of oil and gas leases in Montana.[25] At issue was whether the environmental groups could demonstrate a "concrete and redressable injury."[26] The Ninth Circuit found that "recreational and aesthetic interests . . . may establish actual injury to the extent such interests would be concretely harmed by the challenged governmental action."[27] Thus, the Court explained, the trial court erred by not considering that the development of the leases could cause harm to the surface.[28] The Court remanded to allow the district court to consider which leases the Appellants had standing to challenge, as well as any actual injuries stemming from the surface harms caused by lease development.[29]

#### *2. Energy Investments, Inc. v. Greehey & Co., Ltd.*

In *Energy Investments, Inc. v. Greehey & Co., Ltd.*, the Federal District Court for the District of Montana, Great Falls Division, Magistrate Judge Johnston presiding, granted in part and denied in part a motion for summary judgment regarding the interpretation of an area of mutual interest ("AMI") agreement.[30] In 2012, the parties entered into an AMI agreement in which Greehey agreed to pay Energy Investments ("Energy") $50.00 per net mineral acre for any oil and gas leases Greehey acquired within the AMI and $75.00 per net mineral acre for any leases Energy acquired within the

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23. *Id.* ¶¶ 24-28, 383 Mont. at 8-10, 367 P.3d at 409-410.
24. 615 Fed. Appx. 431 (9th Cir. 2015).
25. *Id.* at 432.
26. *Id.*
27. *Id.*
28. *Id.*
29. *Id.* at 433.
30. No. CV 14-13-GF-JTJ, WL 6034028, *1 (D. Mont. Oct. 15, 2015), *appeal filed,* No. 16-35256, 2015 (9th Cir. April 6, 2016).

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AMI.[31] The parties further agreed that Energy would assign any leases it acquired to Greehey, and Greehey would assign to Energy an overriding royalty interest in the leases Greehey acquired.[32] Greehey intended to sell and assign all leases obtained within the AMI to Apache, but Apache refused to accept the proffered leases because they didn't include certain terms.[33] Since Greehey could not sell the leases, it failed to pay Energy.[34] Energy filed suit and moved for summary judgment as to the unpaid "prospect fees" for the acquired oil and gas leases, as well as an overriding royalty interest on those leases.[35]

Greehey argued that it owed a prospect fee only for those acquired acres with five year lease terms and a two year option to renew, contending that this requirement was evident from the parties' discussions and the language of the AMI Agreement.[36] Initially, Greehey also argued that Energy had never received authorization to purchase leases for more than $200 per acre and that it was not obligated to pay for leases that did not have five-year/two-year term.[37] Greehey later conceded that one of its agents authorized Energy to purchase leases for more than $200 per acre, and Energy thus contended that Greehey had waived any defenses it may have had as to its five-year/two year term claim. [38]

The Court found the contract unambiguous and entered summary judgment for Energy, finding that Greehey owed it approximately three million dollars in unpaid fees, but it denied the motion as to certain remaining leases, finding that a genuine issue of material fact existed as to whether Greehey had waived its defenses as to the five-year/two-year term claim.[39]

*3. Elk Petroleum, Inc. v. Rocky Mountain Regional Director*

In *Elk Petroleum, Inc. v. Rocky Mountain Regional Director*,[40] the Federal District Court for the District of Montana, Billings Division, Judge Watters presiding, granted a motion for summary judgment in favor of the Rocky Mountain Regional Director for the Bureau of Indian Affairs

31. *Id.* at *2.
32. *Id.*
33. *Id.* at *1.
34. *Id.*
35. *Id.*
36. *Id.* at *3.
37. *Id.*
38. *Id.* at *4.
39. *Id.*
40. No. 14-30-BLG-SPW, 2016 WL 676362 (D. Mont. Feb. 18, 2016).

("Director"), upholding an oil and gas lease on lands owned by the Crow Tribe.

In 2008, the Crow Tribe of Indians executed a lease to Elk Petroleum ("Elk").[41] Pursuant to the Indian Mineral Development Act of 1982, the Crow Tribe then submitted the lease to the Bureau of Indian Affairs ("BIA") for its approval.[42] Initially, the Director indicated that he would approve the lease in thirty days and highlighted some concerns.[43] The parties responded to these concerns by submitting a letter of clarification.[44] Shortly thereafter, the Director sent a second letter stating: "This is our approval of the [lease]."[45] This letter also stated that the prior letter of clarification would be made part of the lease.[46] The Director's letter indicated several other times that the lease was approved.[47]

A dispute arose when the BIA sent invoices to Elk to collect its first year rent and bonus.[48] Elk refused payment, claiming that there was no binding lease between Elk and the Crow Tribe.[49] Through the administrative appellate process, the Board of Indian Appeals found that the lease had been unambiguously accepted and affirmed the Director's decision to cancel the lease due to lack of payment.[50]

In the District Court, both parties moved for summary judgment.[51] Applying an arbitrary, capricious, or abuse of discretion standard of review, the District Court affirmed the Board of Indian Appeals' decision, granted the Director's motion for summary judgment, and ordered Elk to pay approximately $870,000 (amount owed plus interest).[52]

*4. Murray v. Billings Garfield Land Co.*

In a most peculiar case, *Murray v. Billings Garfield Land Co*., the Federal District Court for the District of Montana, Billings Division, Judge Watters presiding, was asked to determine whether dinosaur fossils are part

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41. *Id.* at *1.
42. *Id.*
43. *Id.*
44. *Id.*
45. *Passim.*
46. *Passim.*
47. *Id.* at *2.
48. *Id.*
49. *Id.*
50. *Id.* at *3.
51. *Id.*
52. *Id.* at *4-5.

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of the surface or the mineral estate.[53] Beginning in 2005, multiple dinosaur fossils were discovered on the ranch owned and operated by the Murrays.[54] The estimated value of the fossils was in the millions and included two dinosaurs that were apparently locked in battle when they died (a rarity), a T. Rex, and a Triceratops skull.[55] The Murrays, who own the surface of the ranch but share fractional interests in the minerals underlying the ranch with the defendants, filed suit seeking a declaratory judgment that the fossils were part of the surface estate.[56] The Seversons counterclaimed, arguing that the fossils should be classified as minerals.[57] Both parties offered expert testimony regarding the composition of these specific fossils.[58]

Noting that the question is not whether the item falls within the scientific definition of a mineral or is "rare and exceptional in character," the Court applied the "Heinatz" test taken from a Texas case, which asks whether the substance at issue falls within the "ordinary and natural" meaning of "mineral."[59] In addition, the Court looked to both dictionary and statutory definitions and concluded that dinosaur fossils do not fall within the ordinary and natural definition of "mineral" for purposes of a mineral deed and therefore belong to the owners of the surface estate.[60]

*5. Northern Oil and Gas, Inc. v. Continental Resources, Inc.*

In *Northern Oil and Gas, Inc. v. Continental Resources, Inc.,*[61] the Federal District Court for the District of Montana, Billings Division, Magistrate Judge Ostby presiding, considered whether operations on adjoining land were sufficient to perpetuate a lease into its secondary term. Continental Resources ("Continental") and Northwest Farm Credit Services ("NWFCS") entered into an oil and gas lease whose primary term expired September 29, 2013, covering the west half of Section 10 in Richland County, Montana.[62] Prior to the execution of the lease, the Montana Board of Oil and Gas Conservation ("Board") made Section 10, along with

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53. No. 14-106-BLG-SPW, 2016 WL 3030929, *appeal filed*, No. 16-35505 (9th Cir. June 20, 2016).
54. *Id.* at *2.
55. *Id.*
56. *Id.* at *1-2.
57. *Id.*
58. *Id.*
59. *Id.* at *8.
60. *Id.*
61. No. 14-90-BLG-CSO, 2016 WL 3079692 (D. Mont. May 31, 2016).
62. *Id.* at *1.

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Section 3—which was not part of the NWFCS lease but is adjacent to Section 10—part of a temporary spacing unit for Bakken production.[63] Continental completed a well on Section 3 on September 29, 2013, the last day of the primary term of the lease covering Section 10, but no well was drilled on Section 10.[64] On May 1, 2014, the Board issued an order declaring both Sections 3 and 10 part of a permanent spacing unit for pooled production from the Bakken/Three Forks Formation.[65]

NWFCS filed suit, claiming that the lease on Section 10 had expired because Continental failed to commence operations on the leased premises prior to the expiration of the primary term.[66] Continental argued that because Sections 3 and 10 were part of a temporary spacing unit, operations on Section 3 amounted to operations on lands pooled with the leased premises, and therefore prolonged the lease covering Section 10 into its secondary term.[67]

MCA § 82-11-202(1)(b) provides that "[o]perations incident to the drilling of a well upon any portion of a permanent spacing unit covered by a pooling order are considered, for all purposes, the conduct of the operations upon each separately owned tract in the spacing unit by the several owners of the tracts."[68] Continental cited no similar authority for its position that inclusion in a temporary spacing unit had the same effect.[69] Since the unit covering Section 10 was not made permanent until after the expiration of the lease's primary term, the Court held that the lease had expired on its terms.[70]

63. *Id.*
64. *Id.* at *2.
65. *Id.*
66. *Id.* at *3.
67. *Id.*
68. *Id.* at *8.
69. *Id.*
70. *Id.*

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