

# Farm Planning

FOR THE FUTURE: MINERAL LEASES



## Mineral Leases

Marcellus Shale gas wells are becoming more and more common. You may be approached by a landman if you own land on the Marcellus formation spanning West Virginia, eastern Ohio, western Pennsylvania and southern New York. A landman is an employee of a gas drilling company. A landman's job is to bargain with landowners so they will lease or sell their mineral rights to the company.

While most people generally think they own everything under the surface of their property to the sky above it, frequently this is not so. When a person buys a piece of land a title search should be done. A title search checks whether the person buying the land is also buying the mineral rights and to make sure no one else, like a bank, owns part of the property. It is common for previous landowners to have sold the mineral rights (permission to use minerals under the property) to drilling companies. This sale should be marked on your county's deed records but sometimes it is not. If the title search finds the mineral rights have been 'severed,' meaning already sold or leased to someone else, then you only own the surface rights. This means you own the actual land on which your home is. Someone else owns the rights to use the coal, oil, gas and other minerals beneath it.

## Who owns the mineral rights?

If the mineral rights are severed from your land, the owner of the mineral rights has the right and power to decide to drill or not to drill for oil or gas under your property. However, if the mineral rights have not been severed, than you still own them. You also own the surface rights. You will know if the mineral rights have been severed from the property because it will be noted in the deed records at your county courthouse. If nothing exists at the courthouse to say the rights have been severed, you own the mineral and surface rights. The ownership of the mineral rights is becoming more and more important because the natural gas industry in West Virginia and the surrounding region is signing more and more leases.

If you own your mineral rights and are interested in selling or leasing them, there are a few basic things you may want to think about. Most people are always welcoming of additional income. However, the decision to enter into a mineral lease is not one that should be taken lightly.

## What do I do if a landman comes to visit?

A landman's job is to go to the county courthouse and find out who owns the mineral rights to a piece of land. The landman then bargains with the owners for an agreement allowing the drilling company to drill the minerals. This agreement can end in either an oil or gas lease or sale. A lease allows the company to drill for gas on your property and take the gas they find.

In exchange, you are paid a signing bonus when the lease is signed and a royalty percentage from the gas that is removed.

A lease of your mineral rights is very different than a sale. If you lease your mineral rights for a fixed term (set amount of time) and no drilling happens, your rights are given back to you when the lease expires (when the set amount of time is over). Many leases offer two terms, the primary term and the secondary term. The primary term is the amount of time the drilling company has to drill and test for minerals. If the company decides to remove your minerals, the lease automatically starts the secondary term.

You may want to bargain for a 'right of first refusal' during your bargaining with the company's landman. A 'right of first refusal' is the right of a person or company to purchase before the offering is made available to others. If the landowner has the right of first refusal, then the drilling company must talk to the landowner before the company starts drilling to check if you (the landowner) still accept the terms for the drilled minerals, e.g., price. This allows the landowner to take advantage of market prices for oil and gas at the time the company decides to drill. Without the right of first refusal, the contract will automatically renew and start the secondary term and you will be paid the price set at the initial negotiation.

Once you sell your mineral rights to a drilling company, the company can do whatever it wants. The company may sell them to a different company. Some companies 'speculate' (guess which land is going to be valuable later) and hold onto land for years with no intention of drilling. Their idea is to sell the rights to a company that does intend to drill, for a profit. In cases like this, the company you sold your rights to will not be the same company that shows up to drill on your land. If you do not receive a notice that this has happened, check the deed records at your county courthouse. Deeds are public records which tell you what has been sold to whom.

It is strongly recommended not to sign a lease the first time it is given to you. On average, 20 changes are made to leases before they are finally signed. If you do not have experience with this, you may want a lawyer to look over the draft lease. This is because companies usually write the first draft. Most likely it is written to favor the company, not the landowner. Many standard lease forms may have terms that are harmful to the interests of the landowner. For example, the standard agreement, when first given to the landowner, may give the oil company the right to remove minerals at any time without the landowner knowing. The standard agreement may not pay for drilling damages to the land. You may also want to talk to several gas companies to compare prices and terms before making a decision.

## What should I be cautious of?

When buying land, it is a good idea to know if the mineral rights have been severed (already sold or leased) or if they are still attached to the surface rights. If the mineral rights have been severed, read the current mineral rights agreement or lease carefully. Although you were not part of making the lease agreement, you still have to follow the mineral contract signed by the previous owner if you buy the land.

If the land you buy still has the mineral rights attached, you will be able to bargain the terms of any lease or sale of your mineral rights. Remember, you do not have to accept the lease as it is handed to you. You have the ability and right to bargain for the terms and conditions you want.



## Things to think about when bargaining

- You may want to add a clause to the lease about subsidence (when your land and/or home sink because the minerals supporting the land were removed). Subsidence can go unnoticed for years.
- You may want the drilling company to pay for reclamation when drilling ends. This means the company must return the land to the state it was in before drilling started.
- Decide if the lease is only for gas or if it is also for oil, coal-based methane or other minerals.
- Find out if infrastructure on your land, like a pipeline or a pond, will benefit others. The drilling company may want to put a storage tank on your land that will hold not only the gas produced on your land but the gas produced on your neighbors' land as well. If this is the case, you will be suffering an inconvenience (having their gas stored on your land). You can receive compensation (pay) for this. You may want to bargain an additional payment for the inconvenience in your lease.
- Determine the pooling and unitization rights of the gas company. The gas company has the right to combine your gas with the gas drilled from other land properties. If this happens, your payments are based on your percentage contribution to the whole. You will want to know this to make sure you are getting the proper price for your portion.
- You may want to know if a horizontal well

(a well that runs across under ground, rather than straight down vertically) will be drilled. Horizontal wells pose a different threat for subsidence (land sinking due to removal of the minerals below it).

- Consider including a clause in the lease that releases you from liability. This means you are not responsible if something goes wrong in connection to the drilling. This includes company employees getting hurt or a neighbor's road being damaged from the heavy drilling equipment being driven across it.
- You may also want to include a 'duty to defend' clause. This means the drilling company will have to pay for your lawyer and fees if someone personally sues you for drilling damages.
- You may want to include how you will receive signing and royalty payments. For example, do you want to be paid monthly or quarterly, or by cash or check?
- You may also want to bargain

for free home-use gas. Be aware that you will probably be paying the cost of running a pipeline from the well to your house.

- Are you part of any conservation programs? Program rules may not allow drilling on your land until the program ends.
- Trees may be removed from your land to make room for the drilling operation. Consider writing compensation for the value of the timber taken from your land into the lease.

**The most important thing you can do to protect yourself is to make sure that everything you and the drilling company agree to is in writing.**



## What can I do if my neighbor drills?

It also helps to know if any wells are drilled near your property. West Virginia follows the Doctrine of the Rule of Capture. This means that if your neighbor drills a well on his/her property that is near your property line, and the gas from your property exits through a well on your neighbor's property, your neighbor gets to keep the earnings from your gas. One way to stop this is to drill a well on your property. You can also enter into a 'voluntary unitization and pooling agreement.' This means each neighbor gets a share of the royalties based on how much of their gas is flowing out of which well. This type of agreement is not required by law in West Virginia.

## What should I consider before signing a lease?

Landowners are often approached by a landman with little idea of what their rights are when it comes to a mineral lease or sell. There are many things to consider if you are interested in leasing or selling your mineral rights.

- Think about the impact that drilling and having a well will have on your farming operation.
- Where will roads to the wells be located?
- Where will the wells be drilled? Drilling usually disrupts several acres of land. A few acres are usually needed for a drill pad and a few more acres may be needed for runoff capture or water treatment.
- Think about the taxes you will have to pay on the additional income (signing bonus and royalties) you will be paid. This additional income must be reported to the IRS. There are ways to lessen the

amount of taxes you

owe. A mineral rights lawyer can help you with this.



Keep in mind payments from leasing your mineral rights may not stay the same over time. Wells often produce more gas at first and give less gas over time. Your first few royalty checks may be much higher than ones you receive the next year. Royalty checks also depend on current market prices. They can differ greatly even month to month.

## Resources

The Independent Oil and Gas Association of West Virginia, Inc. is West Virginia's largest oil and gas association with approximately 500 company members. The purpose of the organization is to promote and protect the West Virginia oil and natural gas industry. For more information on Marcellus Shale, including a history of oil and gas in WV and an up-to-date newsletter, visit the Independent Oil and Gas Association of West Virginia at [www.iogawv.com](http://www.iogawv.com) or call **304-344-9867**.

The West Virginia Surface Owners Rights Organization was formed in 2007 by landowners, WV Citizen Action Group and public interest lawyer Dave McMahan. The group focuses on public policy and regulatory changes needed to expand surface owner's rights and help West Virginia protect her land and resources. You can contact the West Virginia Surface Owner's Rights Organization by visiting [www.wvsoro.org](http://www.wvsoro.org), or call **304-346-5891**. The website features photos of the drilling process and other general information on drilling for oil and natural gas.



West Virginia University Extension has a wide variety of programs and resources available regarding Marcellus Shale at [http://anr.ext.wvu.edu/oil\\_gas](http://anr.ext.wvu.edu/oil_gas). WVU Extension hosts various educational programs across the state as well. For more information call **304-234-3673**.



 West Virginia University

West Virginia AgrAbility is supported by the USDA Cooperative State Research,  
Education and Extension Service Special Project #2009-41590-05437.  
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