

**MEETING OF THE COMPULSORY POOLING STUDY GROUP
NORTH CAROLINA MINING AND ENERGY COMMISSION
FEBRUARY 8, 2013
CENTRAL CAROLINA COMMUNITY COLLEGE
764 WEST STREET
PITTSBORO, NORTH CAROLINA**

1. PRELIMINARY MATTERS

Chairman Ray Covington called the meeting of the Compulsory Pooling Study Group of the Mining and Energy Commission (MEC) to order at approximately 9:00 am and read the ethics statement into the record.

The following persons were in attendance for all or part of the meeting:

MEC STUDY GROUP MEMBERS

Dr. Ray Covington
Mr. Charles E. Holbrook
Ms. Charlotte Mitchell
Mr. James Womack

STUDY GROUP RESOURCE MEMBERS

Mr. Mark Coburn, Sate Employees Credit Union
Mr. Theodore Feitshans, Dept. of Agriculture and Resource Economics, NCSU
Mr. Ronnie Harrison, State Employees Credit Union
Mr. John G. Humphrey, the Humphrey Law Firm
Mr. Don Kovasckitz, Lee County Strategic Services
Mr. Grady McCallie, North Carolina Conservation Network
Mr. James Robinson, Rural Advancement Foundation International (RAFI)
Ms. Janet Thoren, NC Real Estate Commission
Ms. Lynne Weaver, NC Attorney General's Office, Consumer Protection Division
Ms. Rose Williams, NC Dept. of Insurance

DENR STAFF MEMBERS

Ms. Layla Cummings
Mr. Walter Haven

OTHERS IN ATTENDANCE

See attached sign-in sheets.

2. BACKGROUND AND OBJECTIVES

Dr. Covington welcomed everyone in attendance and explained that the Study Group had been expanded to help guide the group with new perspectives. Dr. Covington clarified the roles of the North Carolina Mining and Energy Commission (MEC) and the Compulsory Pooling Study Group. He explained that the overall goal of commission and study group activities would be to create a new regulatory system for oil and gas exploration and production in North Carolina. Dr. Covington also reviewed the presentations and discussions of the previous two Study Group meetings and reminded the audience that past presentations have been made available on DENR's website.

Panel members made up of the MEC Commissioners and the Resource Group members introduced themselves by stating their backgrounds and explaining their roles in the Study Group. Dr. Covington reviewed the minutes from the last meeting and read aloud the schedule for upcoming Study Group meetings, through the month of May.

3. EXTINGUISHMENT OF ANCIENT MINERAL RIGHTS

Theodore Feitshans, an attorney and professor at North Carolina State University, gave an overview of extinguishment of ancient mineral rights under N.C. Gen. Stat. § 1- 42.1 through § 1- 42.9 (see attached handout). Dr. Feitshans reviewed when it is statutorily permitted to extinguish mineral rights and the exceptions that would allow such mineral rights to continue. Those exceptions occur when the resource is currently in use, the subsurface interest is being held in adverse possession, the mineral rights owner is under a disability or is a minor, the mineral rights are listed for ad valorem taxes, or the exception of mineral rights is noted in the surface holder's chain of title within the past 30 years. Dr. Feitshans also explained that an extinguishment could be challenged if the respective county did not give proper notice of the extinguishment.

4. OWNERSHIP OF OIL AND GAS RIGHTS: THE SURFACE ESTATE AND THE MINERAL ESTATE

Don Kovasckitz, Director of Strategic Services for Lee County, gave a presentation on the current status of mapping and modeling split estates in Lee County (see attached handout). Split estates are estates in which the mineral rights are not owned by the surface owner. That is, there is a mineral estate and a surface estate. Mr. Kovasckitz presented data gathered and modeled by Lee County based on title records. The graphics revealed where natural gas will likely be found in Lee County overlaid with where the surface and mineral rights were owned separately. It was noted that not all title records reveal where there is a split estate. However, since North Carolina is a "race notice" state (first to record title has ownership), there is incentive to record separately held mineral rights with the county Register of Deeds.

5. USDA LOANS AND THE EFFECTS OF NATURAL GAS DRILLING

John Humphrey, a property rights attorney in the DC area, gave a presentation concerning the effect of compulsory pooling on USDA loans, mortgages, and insurance. The NC DOJ Consumer Protection Report to the General Assembly of May 2012

addressed such impacts on landowners, including the impacts of natural gas leases on existing mortgages, ability to refinance, and ability to obtain new credit. The report can be found on DENR's website.

Mr. Humphrey reviewed relevant mortgage clauses requiring that the borrower not create conditions adversely affecting a property value. Violations of such mortgage clauses might involve a borrower allowing hazardous substances or wastes to be generated or stored on the respective property. For new mortgages, lenders are wary of natural gas leases and may refuse mortgages on properties with split estates, due to potential environmental problems or risk of litigation. For existing mortgages, lenders would be necessary parties in any pooling process. Compelling landowners with mortgages into pools may cause them to default on mortgages, but NC DOJ is unaware of any instance of such default.

Landowners who are compelled to join a pool will not be covered by their homeowners or commercial insurance and will not have access to another party to which they can shift risks. If landowners are compelled to join a pool, State action will be required to protect landowners by shifting the risk to the State, gas operators, or other parties.

6. AN OVERVIEW OF COMPULSORY POOLING IN FIVE OIL AND GAS PRODUCING STATES

Layla Cummings of DENR gave a presentation on compulsory pooling laws, rules, and regulations in five oil and gas producing states (see attached handout). Those states were Arkansas, Colorado, Ohio, Texas, and West Virginia. Ms. Cummings listed the mostly commonly used policy rationales in other states which included the following: to prevent waste; to avoid over drilling; to protect correlative rights; and to maximize ultimate recovery of oil and gas.

Ms. Cummings emphasized that certain provisions of the above states' compulsory pooling laws provide a framework to discuss policy options in North Carolina. If North Carolina were to retain compulsory pooling in the state's oil and gas conservation statute, the Study Group should consider whether to require evidence of a fair and reasonable offer to landowners, consent of the surface owner of unleased pooled land for surface operations, statutory Pugh clause, and automatic dissolution of pooling orders.

7. DISCUSSION OF POLICY OPTIONS

One member of the audience asked about House Bill 8 which will limit the State's power of eminent domain. Dr. Covington confirmed that House Bill 8 may substantially affect a compulsory pooling law and it would be a topic to be addressed further. Additionally, a few members of the panel discussed the necessity of compulsory unitization and whether or not it is appropriate with North Carolina's geography.

DEMLR Staff Contact for this Study Group: Walt Haven, Energy Program Supervisor, Land Quality Section.