

IN THE SUPREME COURT OF OHIO

CLYDE A. HUPP, et al.	)	
	)	Case No. 2014-1933
Plaintiffs-Appellants	)	
	)	
vs.	)	On Appeal from the Monroe County
	)	Court of Appeals
BECK ENERGY CORPORATION	)	
	)	Seventh Appellate District
Defendant-Appellee	)	
	)	Case Nos. 12 MO 6
and	)	13 MO 2
	)	13 MO 3
XTO ENERGY, INC.	)	13 MO 11
	)	
Proposed Intervenor	)	
	)	
-and-	)	
	)	
STATE OF OHIO EX REL. CLAUGUS	)	Case No. 2014-423
FAMILY FARM, L.P.	)	
	)	Original Action in Prohibition
Relator	)	and Mandamus
	)	
vs.	)	
	)	
SEVENTH DISTRICT COURT OF	)	
APPEALS, et al.	)	
	)	
Respondents	)	

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**REPLY BRIEF OF APPELLANTS CLYDE A. HUPP, ET AL.**

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## **FACTS**

In its brief, Beck makes numerous statements of “fact” without citation either to the record or to its Lease. Beck attempts to bolster the apparent efficacy of its Lease through unsworn and uncited statements that the G&T (83) form was authored in 1983 by a “prominent [Alliance, Ohio] oil and gas firm,” then known as Geiger & Teeple. Beck Merit Brief at 1; Brief of Appellant, Case No. 12 MO 6, at 4. No evidence was ever offered to support Beck’s claim that its form Lease was in fact created by Geiger & Teeple. No evidence was ever offered to show that when Beck had its name, as lessee, printed on the form, Beck did not alter the original form. Indeed, there is no evidence that Beck itself did not create the G&T (83) lease form.

Beck also asserts that delay rental amounts were “negotiated by the landowners,” again with no citation to any evidence indicating arms’ length negotiation between parties on an equal footing. Beck Merit Brief at 4. Beck presented lessors with a form Lease wherein almost all key terms were preprinted in small type with no headings. The number of months within which Beck was to commence a well was filled in by hand, in large numbers, along with the delay rental amount. The provisions that enable Beck to extend the Lease in perpetuity are all buried in boilerplate.

## **REPLY ARGUMENT**

### **Proposition of Law No. I**

An oil and gas lease which can be maintained indefinitely without development is a perpetual lease that is void as against public policy. That a lease purports to establish a fixed term is of no consequence if the duration of that term can be extended without development.

The court of appeals' determination that the Beck Lease is not a no-term, perpetual lease is based on the presumption that (1) the ten-year term in paragraph 2 is a standard primary term during which the lessee must at least commence development to extend the Lease; (2) delay rental payments cannot be used to postpone development beyond the primary term; and (3) to preserve the Lease beyond the ten-year period set forth in paragraph 2, the lessee either (a) must have drilled a well capable of production in paying quantities, or (b) must be conducting operations in a search for oil or gas. However, the Lease contains no express limitation on the lessee's ability to defer development by paying nominal delay rentals.

The true character of the Lease cannot be gleaned from one or two paragraphs: it is the cumulative effect of all its provisions that renders the Lease a no-term, perpetual lease. The Beck Lease is little more than a framework under which the lessee acquires control over a lessor's land that can extend in perpetuity without development. Although most oil and gas leases place some limitation on the amount of time the lessee can hold the lease without any effort to develop the land, the Beck Lease imposes no restrictions on the lessee's ability to extend the Lease. Key terms establishing what the lessee must accomplish to perpetuate the Lease are not defined, while provisions ensuring the lessee's ability to maintain the Lease without undertaking any development are set forth in detail.

Beck itself has offered varying interpretations of what is necessary to extend the Lease, typically taken from case law interpreting other leases rather than from the language in the Lease, suggesting that not even Beck has a clear understanding of the lessee's obligations thereunder. Although the Lease itself does not mention "primary term" even once, both Beck and XTO have generously inserted that term throughout their briefs

as if the Lease explicitly prohibits the lessee from postponing development beyond the purported “primary term.” Had Beck placed some boundaries upon its ability to unilaterally extend the Lease without development by, e.g., specifying in the Lease that such extensions could occur only during the “primary term,” this lawsuit might not have been necessary.

A. Beck’s own interpretations of its Lease have been inconsistent.

Not even Beck has consistently construed its Lease. Citing the court of appeals’ decision, Beck states that the Lease provides for a ten-year “primary term” within which to *commence* drilling. Beck Merit Brief at 6. Beck next states that a secondary term “commences and continues only so long as there is an established oil or gas well that is actually producing or capable of producing in paying quantities.” *Id.* at 6, 29.

In the trial court, Beck stated that the Leases “will automatically terminate at the end of ten years unless the capacity for production exists”—“a well \* \* \* must exist that is flowing.” Brief in Opposition to Plaintiffs’ Motion for Summary Judgment, Apr. 30, 2012, at 13. Beck further noted that “[i]f actual production has not begun by the end of the primary term, Beck Energy relinquishes its rights under the Lease Agreements.” *Id.* See also *id.* at 15 (“If at the end of ten years there is no producing well, the Lease Agreements terminate”); 21 (the Leases “will automatically terminate at the end of ten years unless production \* \* \* is possible”; “production \* \* \* is possible only if oil and gas can be produced without additional equipment and repairs”). *Accord*, Brief of Amici Curiae Ohio Oil and Gas Assn., et al., at 8 (“there can be no secondary term unless Beck drills a well during the ten-year primary term that is ‘producing or capable of producing’ \* \* \*”).

However, in its first “counter-proposition of law,” Beck states that the indefinite secondary term “continues only so long as the well is producing or is capable of producing in paying quantities or Beck Energy is *operating the premises in search of oil or gas.*” (Emphasis added.) Beck Merit Brief at 7. Hence, according to Beck in this instance, no producing well need be completed to trigger a secondary term: all Beck must accomplish during the purported “primary term” is “commence” operations—i.e., make “preparations for drilling.” *See id.* at 7, 16 (“the case law is clear that the ‘commencement’ of operations is sufficient activity to extend a lease into its secondary term”); Beck’s Brief in Opposition to Plaintiffs’ Motion for Summary Judgment, Apr. 30, 2012, at 5 (under the operations clause, all Beck must do in the “primary term” is commence “operations”).

In its merit brief herein, Beck indicated that “to extend the Leases into their secondary term, [Beck] will have to *commence* a well that produces in paying quantities or is capable of producing in paying quantities.” (Emphasis added.) Beck Merit Brief at 29. It is unclear whether mere commencement of a well that ultimately produces will extend the term, or whether the well must be capable of production to trigger the secondary term. In the next paragraph of its brief, Beck states that the Lease “requires a well to be commenced annually, unless delay rental payments are made \* \* \*.” *Id.*

The court of appeals held that the “capable of production” clause requires an existing well capable of producing without further repairs or equipment. Opinion of the Court of Appeals (App. Op.), ¶¶100-101. Before the appellate court reached its decision, Beck argued that the “capable of production” clause “allows the lease to continue while the

lessee completes the well.” Brief of Appellant, Case No. 12 MO 06, Mar. 15, 2013, at 30.<sup>1</sup> Noting that in some states, the term “produced” does not require actual production, Beck asserted that “[t]he term ‘capable of production’ is designed to avoid a narrow interpretation of the term ‘produced.’” *Id.*, n.13.

The operations clause has been part of the Lease since the Leases were executed, before the inception of this litigation, but was largely ignored during the initial briefing in the trial court. Beck’s and the amici’s statements that the Lease will terminate in the absence of a well capable of production without further modifications were unqualified—neither Beck nor the amici indicated either that without a fully functional well, the Lease could continue under the operations clause, or that the unqualified statements as to termination in the absence of a fully functional well were addressing only the “capable of production” clause. It may be that, as in the case of other language in the Lease, Beck and the amici were relying solely on “traditional oil and gas jurisprudence” rather than the actual language of the Lease at issue. Regardless, that Beck (along with the amici curiae—members of the oil and gas industry) can arrive at differing interpretations of its own Lease, ignoring nearby language in the same Lease (imprecise though it may be) undermines Beck’s construction of the Lease.

B. The commencement clause does not require any significant development to trigger an indefinite secondary term, and fails to specify what actions constitute commencement.

The Lease requires the lessee to “commence[ ]” a well on the premises within twelve

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<sup>1</sup>On the next page of its brief, Beck stated that “a well capable of production is a well that will produce when turned on line.” Brief of Appellant, Case No. 12 MO 06, at 31.

months or pay delay rentals to avoid termination of the Lease. Lease, ¶2. The dry hole provision requires the lessee to commence another well after plugging a dry hole or resume paying delay rentals. Lease, ¶7. The Lease provides that “[a] well shall be deemed commenced when preparations for drilling have been commenced.” Lease, ¶3. However, the Lease does not specify what “preparations” for drilling constitute commencement. Do “preparations” include drawing up plans to drill? Obtaining permits? Planning an access road to a proposed well site? Placing equipment on the lessor’s property? Regardless of how one interprets “commencement” of a well, “commencement” clearly is not the equivalent of a completed well that is producing or capable of production.

A typical commencement clause permits the extension of a lease into its secondary term so long as the lessee commences operations within the lease’s primary term. Richardson, *Hite v. Falcon Partners: A Model Rule for Marcellus and Utica Shale States Precluding the Use of Delay Rental Payments to Extend the Primary Term in an Oil and Gas Lease*, 46 Akron L.Rev. 1133, 1160 (2013). “Regardless of whether actual drilling is required for commencement, carefully drafted leases can afford lessees more time to complete wells under a lease.” *Id.* at 1160-1161.

Rather than define “commencement” in its own Lease, Beck simply imports definitions from other leases and case law construing those leases. Beck Merit Brief at 16. Commencement “may consist of trivial and comparatively insignificant matters.” *Kaszar v. Meridian Oil & Gas Ent.*, 27 Ohio App.3d 6, 7, 499 N.E.2d 3 (11<sup>th</sup> Dist. 1985). The commencement requirement can be satisfied by staking out a well, contracting to buy timber on the last day of the lease’s term, or the mere driving of a stake; surveying the drill

site, staking out a well, and filing documents; or simply filing a declaration and notice of a pooled unit. Beck Merit Brief at 16, citing *Duffield v. Russell*, 10 Ohio C.D. 472, 19 Ohio C.C. 266, 268 (7<sup>th</sup> Dist. 1899), *aff'd*, 65 Ohio St. 605, 63 N.E. 1127 (1902); *Kaszar*, syllabus; and *Henry v. Chesapeake Appalachia, L.L.C.*, 739 F.3d 909, 914 (6<sup>th</sup> Cir. 2014). See also Merit Brief of Appellants at 17. Is commencement of “operations” equivalent to commencement of a well? The Beck Leases provide no clue.

In contrast, the Premiere lease submitted as an example of reasonable specificity defines “commencement” as the placement of materials on the leased premises or performance of “the first work, other than surveying or staking the location” thereon—not simply making plans, filing paperwork, or purchasing materials that someday may be used in developing a specific lessor’s property. See Appellants’ Merit Brief at 19-20; Premiere lease, ¶4. See also Kramer, *Keeping Leases Alive in the Era of Horizontal Drilling and Hydraulic Fracturing: Are the Old Workhorses (Shut-in, Continuous Operations, and Pooling Provisions) Up to the Task?*, 49 Washburn L.J. 283, 297-298 (2010). In that “commencement” of a well purports to be critical to the lessee’s ability to extend a lease, that term should have been defined sufficiently to permit lessor and lessee alike to understand the criteria for perpetuating a lease.

C. The “operations” clause can extend the Lease indefinitely without any significant development.

Even if, as Beck has asserted and the Court of Appeals held, the “capable of production” clause requires the completion of a well fully capable of production with no additional materials or repairs within the purported “primary term,” the “operations” clause

permits extension into a secondary term, allowing Beck to complete a well, even if no drilling has begun (or is even contemplated), as long as the premises are being “operated by the Lessee in the search for oil or gas.” Lease, ¶2. See App. Op., ¶¶100-101; Beck Merit Brief at 7; Brief of Appellant, Case No. 12 MO 6, Mar. 15, 2013, at 30. In many cases, “operations” are not begun until days or weeks before the end of the primary term. Kramer, 49 Washburn L.J. at 303. See also Beck Merit Brief at 16.

The Beck Lease does not specify which “operations” are sufficient to trigger an extension of the Lease. The term “operation” is “not a term of art with a clearly understood definition.” Kramer, 49 Washburn L.J. at 302. That term should be defined in an oil and gas lease. *Id.* While some courts have found that backdragging a backhoe to delineate the location of an access road to a well site is not an operation sufficient to trigger a lease extension, other cases have concluded that road clearing activities may constitute operations. *Id.* at 302-303.

An operations clause is very similar to a commencement clause, but it can be an even broader way for a lessee to preserve its interest in an oil and gas lease. \* \* \* [T]he “immature” oil and gas jurisprudence of the Midwest states that make up the shale gas plays makes it unclear how these states will interpret operations clauses. However, as long as the clauses are specific about what “operations” are required to keep a lease in effect and the lessee moves forward with the operations in good faith, the lease should be extended as long as the operations continue. *In this way, a lease may be kept alive even if development of a property is only in the planning or preparation phases.*

(Emphasis added.) Richardson, 46 Akron L.Rev. at 1162.

The savings provisions in a lease interpreted by a Texas court were much more specific with respect to operations than those in the Beck Lease:

If prior to discovery and production of oil, gas or other mineral on said land

or on acreage pooled therewith, Lessee should drill a dry hole or holes thereon, or after the discovery and production of oil, gas or other mineral, the production thereof should cease from any cause, this lease shall not terminate if Lessee commences operations for drilling or reworking within sixty (60) days thereafter. \* \* \* If at the expiration of the primary term, oil, gas or other mineral is not being produced on said land, or on acreage pooled therewith, but Lessee is then engaged in drilling or reworking operations thereon \* \* \* the lease shall remain in force so long as operations on said well or for drilling or reworking any additional well are prosecuted with no cessation for more than sixty (60) consecutive days, and if they result in the production of oil, gas, or other mineral \* \* \*.

(Ellipsis sic.) Kramer, 49 Washburn L.J. at 303.

The Beck Lease contains no guidance as to what activities constitute “operations”; how much time can elapse between these operations without terminating the Lease; and whether protracted delays during said operations can result in the termination of the Lease.

D. The Lease places no limitation on the time during which development may be postponed by the payment of delay rentals.

Beck repeatedly states that delay rentals are payable “during the primary term,”<sup>2</sup> even though that language appears nowhere in the Lease, and asserts that the Lease provides for both a primary term and a secondary term. Beck Merit Brief at 2-3. Beck cites no provisions in the Lease establishing either that the ten-year period referenced in paragraph 2 is a true “primary term” during which development must be commenced, or that that term has the attributes of a traditional primary term, after which development can

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<sup>2</sup>Beck argues that the absence of the words “primary term” in the Lease is irrelevant because the habendum clause of an oil and gas lease always includes a primary term and a secondary term. Beck Merit Brief at 17-18. However, the Beck Lease contains no language limiting the indefinite extension of the lease through the payment of delay rentals, either in ¶2 or in the provisions for extending the Lease following the drilling of a dry hole or the plugging of a producing well, ¶7 and ¶8. Even without using the words “primary term,” Beck easily could have limited delay rentals to, e.g., “the term set forth in paragraph 2” to eliminate any possibility of indefinite extensions with no development.

no longer be postponed by the continued payment of delay rentals. Beck relies on case law construing other leases—not the language in its own Lease.

XTO also asserts that the “language of the lease” requires the lessee to develop the land during “the first year of the primary term” or pay delay rentals “during the primary term.” Merit/Amicus Brief of XTO<sup>3</sup> at 5. The language of the Lease makes no reference to a “primary term,” and contains no other time limitation on the lessee’s right to perpetuate the lease without development by paying delay rentals. See Lease, ¶¶2-3.

Beck asserts that the Lessors “contend case law does not support the court of appeals’ decision that the delay rental clause only applies during the Lease’s primary term.” Beck Merit Brief at 8. The Lessors acknowledge that in many, if not the majority, of cases, delay rentals were typically paid during the primary term. In their merit brief, Appellant-Lessors cited cases wherein payment of delay rentals was not automatically limited to a primary term. See *also* Richardson, 46 Akron L.Rev. at 1147 (New York precedent supports a finding that a lessee can extend even a term lease indefinitely by paying delay rentals). The language in the Beck Lease provides that development may be postponed by the payment of delay rentals “until the commencement of a well”—not “during the primary term.” Lease, ¶3.

That courts construing different leases with different language—and often addressing delay rentals in dicta where the subject lease had entered a secondary term before the

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<sup>3</sup>XTO submitted a single brief as an appellee and an amicus curiae. As was noted in Appellants’ response to XTO’s tolling motion in this Court, the trial court denied XTO’s motion to intervene, and the appellate court deemed XTO’s appeal of that ruling moot. App. Op., ¶130. XTO thus remained a non-party. XTO did not appeal its status to this Court, but simply filed its motion, and now its brief, as an appellee.

conflict arose—have held or observed that delay rentals were not paid during a secondary term does not mean that delay rentals are limited to the purported “primary term” under the language of any other lease, including the Beck Leases. Merit Brief of Appellants at 22-27, section I.C.3.

[T]hat an esoteric lease term has traditionally been understood one way does not, pursuant to the law of contracts, necessarily bind every oil and gas lease to that same understanding. “[A]n oil and gas lease must be determined by the terms of the written instrument, and *the law applicable to one form of lease may not be, and generally is not, applicable to another and different form.*” *Harris v. Ohio Oil Co.*, 57 Ohio St. at 129 (emphasis added).

(Emphasis sic.) *Beaverkettle Farms, Ltd. v. Chesapeake Appalachia, LLC*, N.D. Ohio No. 4:11CV02631, 2013 U.S. Dist. LEXIS 124509, \*39 (Aug. 30, 2013).

It is undisputed that Beck has not “commenced” any “operations” on the Lessors’ lands herein. It is also undisputed that when Appellant Larry A. Hustak telephoned Beck’s offices in July 2010, June 2011, and July 2011, to ask whether Beck intended to drill on his land, he was told that even though Beck “had no intentions of drilling because there is no pipeline in that part of the county,” Beck would not cancel the Lease. Affidavit of Larry A. Hustak, Exhibit A to Brief in Support of Motion for Summary Judgment, ¶¶6.

Beck acknowledges that “a contract is to be read as a whole and the intent of each party gathered from a consideration of the whole.” *Saunders v. Mortensen*, 101 Ohio St.3d 86, 2004-Ohio-24, 801 N.E.2d 452, ¶¶16; Beck Merit Brief at 10; Merit Brief of Appellants at 11-12. However, Beck maintains that the dry hole and shut-in clauses are irrelevant to the Court’s interpretation of the Lease because all Leases herein are still in the purported “primary term.” Beck Merit Brief at 16-17.

Both clauses demonstrate that delay rentals (or, in the case of a shut-in well,

“advance royalties” equivalent to delay rentals) may be paid after the end of said “primary term,” with no time limitation. In the case of a dry hole, after plugging the well, Beck is not required to do anything for twelve months, after which Beck may commence another well, or “resume[ ] the payment of delay rentals \* \* \*.” Lease, ¶7. If Beck elects to shut in a producing well, Beck has one year from the completion of that well, or from the cessation of production, or from the shutting in of a producing well—the Lease fails to specify the circumstances under which any of these options applies—to pay advance royalties until production is marketed or until Beck elects to plug and abandon the well. Lease, ¶8. There is no time limitation beyond which Beck must surrender the Lease or market production from the well. Like paragraph 3, neither paragraph 7 nor paragraph 8 limits the delay rental or advance royalty payments to the ten-year term set forth in paragraph 2.

E. Construed as a whole, the Beck Lease is a no-term, perpetual lease which offends public policy and should be declared void.

In *Ionno v. Glen-Gery Corp.*, 2 Ohio St.3d 131, 134, 443 N.E.2d 504 (1983), this Court held that long-term mineral leases under which there is no development impede the mining of mineral resources and are against public policy.

[E]very unproductive lease that is held by the lessee without production harms not only the lessor, but the state and local economies as well. \* \* \*  
*[T]he only person that is not harmed financially is the lessee, who holds on to a lease at minimal expense and enjoys the privilege of waiting for either a technological discovery or a higher price, which would make the asset more valuable.*

(Emphasis added.) Richardson, 46 Akron L.Rev. at 1155.

Beck asserts that although perpetual leases are not favored, a lease that evidences a clear intention to create a perpetuity is enforceable. Beck Merit Brief at 10. The G&T (83)

form lease does not reflect a clear intention to create a perpetual lease—at least not from the perspective of a lessor. In most of the Leases herein, paragraph 3 purports to require the commencement of a well within twelve months from the date of execution, and then imposes an apparent penalty, in the form of an annual delay rental to be paid by the lessee if no well is commenced during that initial one-year period or during subsequent years. The provisions that enable the lessee to perpetuate the Lease without development are scattered throughout the Lease in paragraphs 2, 3, 7, 8, and 9, in fine print with no headings, bold type or other characteristic designed to alert the lessor to potentially onerous terms.

Beck may well have intended to create a perpetual lease that it could hold until such time as it could maximize its profits with no significant effort or investment. However, the Lessors had nothing to gain by surrendering control of their land for an indefinite time, during which Beck had no obligation to drill even a single well. *See Ionno*, 2 Ohio St.3d at 134, 443 N.E.2d 504. Under these circumstances, there was no clear, mutual intention to create a perpetual lease. Accordingly, if the Court concludes that the Lease is perpetual, it should be declared void—not enforced.

The dilemma faced by Appellants and other Lessors was succinctly summarized over a century ago, in a West Virginia case:

The lessor executed this lease with the expectation of a prompt development of his land. The lessees deceived him by the covenant to sink a well in six months, and then, under the pretense of fixing a penalty, in the shape of rental, for failure to complete the well in the time prescribed, skillfully turned it into a speculative lease for rental merely, which, according to their claim, they had 18 months, and so much longer as they could postpone the same, to decide to pay or not. This evidences a plain intention on their part not to explore for oil or gas, and the covenants in relation thereto were simply a blind to deceive the confiding lessor. It is decidedly a one-sided lease, and,

if the lessor had remained quiet, they could have held it for an indefinite period without either exploring for oil or gas or paying any rent.

*Eclipse Oil Co. v. South Penn Oil Co.*, 47 W.Va. 84, 34 S.E. 923, 925-926 (1899).<sup>4</sup>

The Beck Lease is a virtual minefield of loopholes allowing the lessee multiple opportunities to defer any development and any significant expenditure of funds while exerting unilateral control over Lessors' property until its speculation and minimal investment pays off (which has already occurred through the sale of deep rights to XTO for \$84,000,000).

Beck asserts that it "partners with Ohio landowners to develop their oil and gas interests." Beck Merit Brief at 1. In fact, Beck has deferred development and partnered with XTO to quietly strip its lessors of the most valuable asset many have ever owned or will ever own. While any "fracking" operations performed by XTO may severely reduce the value of the surface estate retained by its lessors, Beck has reaped a windfall by assigning the deep rights to XTO and retaining all the profits for itself.

### **Proposition of Law No. II**

Where the express terms of an oil and gas lease effectively allow the lessee to postpone development indefinitely, and any stated time limits can be unilaterally extended by the lessee in perpetuity without any development, the lease is subject to an implied covenant of reasonable development

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<sup>4</sup>*Eclipse* was cited in *Brown v. Fowler*, 65 Ohio St. 507, 519, 63 N.E. 76 (1902). In *Eclipse*, the lessee was not required to pay the delay rental in advance, and unlike the lessor, could cancel the lease at any time. In the instant case, the lessee may cancel at any time, while the lessor has few options if the lessee's performance is unsatisfactory. Although Beck's delay rental payments are to be made in advance, the nominal amount of the delay rentals is not only negligible, but not the consideration the Lessors anticipated upon signing their Leases.

notwithstanding a general disclaimer of all implied covenants.

Beck contends that the implied covenant to develop the land cannot arise under its Lease because (1) the Lease purports to establish a timetable for development; (2) the delay rental payment is not offset against future royalties and is therefore an adequate substitute for development; and (3) the ambiguity arising from the provision in paragraph 17, setting forth a procedure in the event a lessor believes Beck to have breached “any of its obligations hereunder, either express or implied” does not conflict with the blanket disclaimer of all implied obligations in paragraph 19. However, (1) the timetable for development is illusory because Beck can extend the Lease in perpetuity without development; (2) the delay rentals are not the consideration for which the Lessors bargained when they entered their Leases and are no substitute for development, but are in fact equal to the “advance royalties” provided for in paragraph 8, upon Beck’s decision to shut in a producing well; and (3) the provision in paragraph 17 addressing Beck’s potential breach of an implied obligation does conflict with a blanket disclaimer of implied covenants or obligations.

- A. In light of Beck’s ability to extend the Leases with no development, the “timetable for development” suggested in the Lease is illusory and cannot preempt the implied covenant to develop the land.

As has been addressed in the Lessors’ first proposition of law, although the Lease purports to establish a timetable for development, the lessee can unilaterally extend the Lease without any development, simply by paying delay rentals until commencement of a well—and nothing in the Lease requires the lessee to commence a well within any time frame. Because the lessee under the Beck Leases can defer development indefinitely, the

mere reference to nonbinding timetables should not defeat the implied covenant to develop the land.

Moreover, the stated purpose of the Beck Lease is “drilling, operation for, producing and removing oil and gas and all the constituents thereof.” Lease, ¶1. The Lease contains no suggestion that the Lessor had any other objective. There is no explicit indication that Beck’s true goal was to encumber the Lessors’ lands for an indefinite period for investment purposes or otherwise. The implied covenant to reasonably develop the land effectuates the parties’ intent as reflected by the express purpose of the Lease.

B. Delay rentals, like nominal “advance royalties,” are no substitute for development.

The implied covenant to develop the land with reasonable diligence serves to allow lessors “to secure the actual consideration for the lease, *i.e.*, the production of minerals and the payment of a royalty on the minerals mined.” *Ionno*, 2 Ohio St.3d at 134, 443 N.E.2d 504. To allow lessees to hold land under an oil and gas lease without making any effort to develop that land would contravene the nature and spirit of the lease. *Id.* In *Ionno*, this Court held that advance royalties are no substitute for timely development. *Id.*

Although Beck insists that there is a significant difference between delay rentals and the advance royalties that the *Ionno* lessees paid in lieu of development, the terms “advance royalties” and “delay rentals” are used interchangeably. *See Ionno* at 131; *Jacobs v. CNG Transmission Corp.*, 332 F.Supp.2d 759, 785 (W.D. Pa. 2004). Although the advance royalties in *Ionno* were to be set off against future royalties, there never were any royalties because the lessee made no effort to develop the land. As in *Ionno*, the actual consideration for the Beck Leases herein was the anticipated royalties from

production—not minimal rental payments.

Any determination of whether an implied covenant to develop the land arises in the Beck Leases should be predicated on the true nature of the parties' rights and obligations under the Lease, and not upon superficial distinctions. A suggestion in the Lease concerning the timeliness of development that is not binding on the lessee, and the use of different terminology to describe annual payments in lieu of development, should not be the determining factors with respect to whether the Leases include an implied covenant to develop the land. The implied covenant to develop arises in the Beck Leases because the Beck Leases contain no enforceable timetable for development, and the delay rentals are no better substitute for development than the advance royalties in *lonno*.

C. The provision setting forth a procedure for addressing the breach of implied obligations conflicts with the blanket disclaimer of all implied obligations, rendering the disclaimer ambiguous and thus ineffective.

The Beck Leases set forth a procedure through which the lessor can address any perceived breach of an implied obligation by the lessee. Lease, ¶17. Two paragraphs later, the Lease purports to disclaim all implied covenants. Lease, ¶19. Because the Leases can reasonably be interpreted to allow or disallow a lessor to seek redress for breach of an implied obligation, the Leases are ambiguous and must be construed against Beck.

Where general provisions of a contract conflict with specific provisions of the same document, the specific provisions generally control. *Edmondson v. Motorists Mutual Ins. Co.*, 48 Ohio St.2d 52, 53, 356 N.E.2d 722 (1976); *Hoepker v. Zurich Am. Ins. Co.*, 3d Dist. Union No. 140318, 2003-Ohio-5138, ¶11; *Monster v. Cincinnati Cas. Co.*, 74 Ohio App.3d 321, 330, 598 N.E.2d 1203 (10<sup>th</sup> Dist. 1991). The specific provision in paragraph

17 setting forth a lessor's rights and a procedure to follow in the event a Lessor believes Beck to have breached an implied obligation should control over the general disclaimer in paragraph 19, rendering the disclaimer ineffective.

### CONCLUSION

The G&T (83) form lease is a no-term perpetual lease that the lessee can unilaterally extend with no development, by paying delay rentals until "commencement" of a well. Moreover, the Lease fails to specify what actions constitute commencement of a well, and fails to set any time limits for commencing a well. Accordingly, the Lease should be declared void as against public policy. The attempt to disclaim the implied covenant to develop the land is inconsistent with this Court's pronouncements in *Ionno* and with a specific provision in the Lease addressing the lessee's breach of implied obligations, and is thus ineffective to disclaim that covenant. Appellants respectfully request that the Court reverse the decision of the Court of Appeals and reinstate the decision of the trial court or otherwise enter judgment voiding said Lease.

Respectfully submitted,



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**CERTIFICATE OF SERVICE**

I hereby certify that a copy of the foregoing Reply Brief of Appellants was served by regular U.S. mail on this 10<sup>th</sup> day of May, 2015, to each of the following:

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