

No. 33527

IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

ST. LUKE'S UNITED METHODIST CHURCH,
MARY MAXINE WELCH, and
JAY-BEE PRODUCTION COMPANY,

Plaintiffs Below,

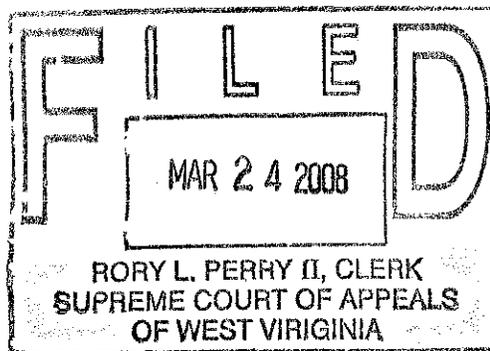
MARY MAXINE WELCH,
Appellant,

v.

CNG DEVELOPMENT COMPANY,
TRI COUNTY OIL AND GAS, INC.,
EAST RESOURCES, INC., and
ENERVEST OPERATING, LLC,

Defendants Below,

CNG DEVELOPMENT COMPANY,
Appellee.



FROM THE CIRCUIT COURT
OF RITCHIE COUNTY
No. 03-C-65

REPLY BRIEF OF APPELLANT

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COMES NOW Appellant Mary Maxine Welch (“Appellant Welch”), by and through counsel, in Reply to the “Brief of Appellee,” and states as follows:

I. ARGUMENT

A. THE “KIND OF PROCEEDING AND NATURE OF THE RULING BELOW” SECTION OF APPELLEE DOMINION’S¹ RESPONSE BRIEF CONTAINS CERTAIN OMISSIONS AND MISREPRESENTATIONS THAT ARE RELEVANT TO THIS COURT’S ANALYSIS AND CONSIDERATION

In its Response Brief, Appellee CNG (now known as “Appellee Dominion”) provides a lengthy, argumentative section titled “Kind of Proceeding and Nature of the Ruling Below,” which contains several omissions and misrepresentations that are relevant to this Court’s consideration of this appeal. The Court is cautioned that much of Appellee Dominion’s presentation in this section is an in-depth account of the pleadings, motions, memoranda and orders in the lower court from Appellee’s “point of view” and that reference to the parties’ original documents is essential for an objective analysis of the proceedings below. Nevertheless, Appellant has identified four areas from this section of Appellee Dominion’s Response Brief where clarification is particularly necessary.

First, Appellee Dominion states erroneously that the initial two-count Complaint “did not demand damages as a remedy, but instead demanded only equitable relief.” (“Brief of Appellee,” p. 3) While Plaintiffs asked the court to declare the ancient Flanagan Lease “forfeited, canceled, terminated and removed as a cloud upon the title to the Plaintiff’s land,” they also demanded that they “have such other

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For consistency, Appellant Welch will continue to reference Appellee CNG as “Appellee Dominion,” noting that Appellee identifies itself as “Appellee Dominion Exploration & Production, Inc. (DEPI), successor to CNG Development Company” in its motion and response brief.

and further relief, both general and special, to which they are entitled in or about the premises.”

(Complaint, “Demand,” ¶¶ 1 and 2)

Second, Appellee Dominion relates that prior to filing the Complaint, Plaintiffs “issued no demand to DEPI to drill additional wells” and that after the lawsuit was filed, Appellee Dominion “undertook to obtain permits and to drill additional wells on the Flanagan Lease.” *Id.*, p. 4. Appellant Welch asserts that West Virginia law does not require that such demand be made prior to filing a law suit of this nature,² and that Appellee’s belated attempt to drill after litigation had commenced was only in strategic response to the filing of the suit and had come too little, too late. As discussed in Appellant Welch’s Brief, Appellee Dominion does not operate any gas wells upon the grossly underdeveloped Flanagan Lease, and Enervest Operating, LLC³ owns three marginally productive oil and gas wells upon the subject leasehold. (*See* “Brief of Appellant,” pp. 2, 5, 10, 11, 22 and 28) Moreover, Appellee Dominion’s statement that it “undertook further development in an effort to satisfy Plaintiffs” (“Brief of Appellee,” p. 5) underscores the fact that these measures could only be characterized as attempts or offers to compromise Plaintiffs’ claims, which have absolutely no effect upon Appellant Welch’s legal rights with regard to prosecution of the case *sub judice*. Appellee Dominion further recounts that prior to the bench trial date of February 23, 2006,

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Later, at page 26 of its Response Brief, Appellee Dominion also states that “Welch made no demand that DEPI commence drilling.” There is no requirement under West Virginia law that demand be made prior to the filing of the instant litigation.

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As discussed in “Brief of Appellant,” former Defendant Enervest was first joined, pursuant to Appellee Dominion’s Motion to Dismiss, and then dismissed by mutual consent after the filing of the Amended Complaint seeking only partial release of the subject oil and gas lease. (*See* “Brief of Appellant,” Footnote 2)

it offered to drill up to eleven additional wells on the Flanagan Lease. *Id.* p. 9. Certainly, Appellant Welch had no obligation to acquiesce, settle or compromise her cause of action at that point of the litigation. Appellee states that “[a]stonishingly, Welch claims she is damaged by DEPI’s failure to drill.” *Id.* at p. 5. Again, Appellee’s supposed eagerness to drill came only **after** the lawsuit was filed. Remember, there was absolutely no effort on the part of Appellee Dominion to develop the leasehold until litigation had begun.

Third, referencing several arguments set forth in its motion for summary judgment, served December 3, 2004, Appellee Dominion stated that “the express terms of the lease required the drilling of one well by the lessee.” *Id.* A review of the “Flanagan Lease” reveals no such “express terms” that only one well was required pursuant to the lease agreement. Rather, the lease states:

Provided that this lease shall become null and void unless operations shall be commenced on the premises and a well completed, unavoidable delay or accident excepted, within 3 months after Dec. 1, 1898 . . . or, unless lessee shall pay at the rate of \$212.50 Dollars per quarter, payable quarterly in advance or within ten days thereafter for each additional 3 months such completion of well is delayed.

It is agreed between the parties hereto that the completion of one well shall stop the rental on 283 1/3 acres only. The completion of a second well shall stop the rental on 238 1/3 acres more and the completion of a third well shall stop the rental on the balance of the land hereby leased.⁴

As discussed in Appellant Welch’s Brief, oil and gas leases, such as the Flanagan Lease, are usually for a specific term of years, during which the lessee must drill on the leased premises, and for a further period of time as either oil or gas may be produced in paying quantities. The Flanagan Lease was for a term of five years and “as much longer as oil or gas is produced in paying quantities or the rental paid thereon...”

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The underlined text herein notes where Counsel has supplied terms that were represented by “ditto marks” by the makers of the Lease.

There was no express agreement in the lease that “one well was sufficient,” as asserted by Appellee Dominion. (See “Brief of Appellee,” p. 5) There is absolutely nothing in the language of the lease that would relieve Appellee Dominion from its implied obligation to drill the number of wells reasonably necessary to develop the property and to prevent drainage by operation on adjoining lands. (See *Adkins v. Huntington Development & Gas Company, Inc.*, 113 W. Va. 490, 492-493, 168 S. E. 366, 367 [1932])

Fourth, Footnote 12 of Appellee Dominion’s response brief states erroneously that “Welch does not argue on appeal that she is entitled to the remedy of reformation.” The Circuit Court has not made any ruling regarding the equitable remedy of reformation, which was demanded by Appellant in the Amended Complaint, and presumably has not been foreclosed herein. There are numerous references throughout Appellant’s Brief to “reformation.” (See pp. 1, 5, 6, 7, 10, 21, 25, 37, 40, 43) That remedy has not been taken off the table, as Appellee Dominion suggests, but remains a viable equitable remedy.

B. APPELLEE DOMINION’S ARGUMENT SET FORTH IN ITS “STATEMENT OF FACTS” AND “DISCUSSION” THAT THIS COURT SHOULD STRIKE AND DISREGARD CERTAIN ASPECTS OF APPELLANT’S BRIEF, INCLUDING DONALD C. KESTERSON’S REPORT, KESTERSON’S AND RANDY BRODA’S AFFIDAVITS, AND DR. KHASHAYAR AMINIAN’S DEPOSITION TESTIMONY, IS WITHOUT LEGAL BASIS

Appellee Dominion argues in a single paragraph section titled “Statement of Facts” and in its “Discussion” section that certain evidence, including Donald C. Kesterson’s report and affidavit, Randy Broda’s affidavit, and Dr. Khashayar Aminian’s deposition testimony, should be stricken and disregarded by this Court in its consideration of this appeal. Appellant Welch posits, however, that this evidence is proper for this Court’s consideration, pursuant to its *de novo* and plenary review herein.

C. CONTRARY TO APPELLEE DOMINION’S ASSERTIONS IN THE “DISCUSSION” SECTION OF ITS RESPONSE BRIEF, APPELLANT WELCH IS ENTITLED TO THE REMEDY OF PARTIAL RESCISSION IN THAT SHE DOES NOT HAVE A COMPLETE AND ADEQUATE LEGAL REMEDY WHERE APPELLEE DOMINION HAS NOT DILIGENTLY DEVELOPED THE 850-ACRE TRACT, RESULTING IN DEMONSTRABLE EXTREME HARDSHIP TO APPELLANT

There is simply no merit to Appellee Dominion’s argument that “Welch is not entitled to the remedy of partial rescission because damages are an adequate remedy” (“Brief of Appellee,” p. 13), as this argument ignores unimpeachable facts of this case and controlling West Virginia law which recognizes “a lessor’s right to a complete or partial cancellation of an oil and gas lease on the ground of abandonment and upon circumstances of fraud or extreme hardship.” *Adkins v. Huntington Development & Gas Company, Inc.*, 113 W. Va. 490, 492-493, 168 S. E. 366, 367 (1932) (Citations omitted) (Emphasis added). Here, Appellant Welch is entitled to relief in equity, as she has no complete and adequate remedy at law.

The often cited case of *Jennings v. Southern Carbon Co.*, 73 W. Va. 215, 80 S. E. 368 (1913) is relevant to this discussion. The *Jennings* Court stated that the phrase “‘adequate remedy at law’ is often misinterpreted,” and stated further, as follows:

“The controlling question is not, has the party a remedy, but is that remedy fully commensurate with the necessities and rights of the parties under all the circumstances of the particular case?” . . . (Citation omitted) To defeat equitable cognizance, the legal remedy must be full, it must be complete, it must be adequate. If it does not reach the end intended and actually compel performance of the duty, the breach of which is alleged, it can not be said to be fully adequate to meet the justice and necessities of the case.

73 W. Va. at 223, 80 S. E. at 371.

See also Syllabus Pt. 7, *Warren v. Boggs*, 83 W. Va. 89, 97 S. E. 589 (W. Va. 1918) which states: “To deny equity jurisdiction because of a remedy at law, the legal remedy must be adequate to the demands of the particular case, and as full, complete and efficacious as that given in equity, and must not leave open for future litigation matters really and substantially involved.”

Only an equitable remedy, such as partial rescission, will provide a complete and adequate remedy for Appellant Welch under the facts of this case. The Circuit Court committed reversible error in its ruling that partial rescission of the Flanagan Lease is not the appropriate remedy herein although Appellee Dominion has intentionally allowed the subsurface resources to remain grossly underdeveloped. Appellee Dominion has sought exclusively to protect its own speculative financial interests, dishonoring its obligation to protect Mrs. Welch’s interests. In addition to its failure to develop the resource, Appellee Dominion has also permitted competing contiguous oil and gas drilling operations to drain oil and gas from the leasehold.

Under precedent established long ago by this Court and throughout the United States, such gross underdevelopment – particularly when accompanied by so clear a failure to protect the resource from being diverted to competitors – entitles an owner of subsurface minerals like Mrs. Welch to the equitable remedies of partial rescission or reformation of the lease. Only by such equitable remedies can Mrs. Welch put a willing and able developer in charge, to develop the oil and gas under the best practices standard, and to stop the draining away of her oil and gas. Contrary to Appellee Dominion’s assertions, damages alone will not accomplish these ends.

The 850-acre tract involved in this case now hosts three old, closely grouped, and marginally productive wells. It is surrounded on adjacent properties by numerous competing wells which are draining

oil and gas from the leasehold. Appellee Dominion has violated its implied duty to diligently develop this significant holding. Its refusal to drill is transparently unreasonable, if not unconscionable, and betokens its choice to instead tie up the oil and gas for speculative purposes, in violation of the common law and legislatively established public policy of West Virginia. Under this Court's precedent, production on a small portion of the leasehold does not justify the lessee's indefinite refusal to develop the balance of the tract, which most certainly has resulted in "extreme hardship" to Mrs. Welch – depriving her of substantial royalties and preventing her from implementing other reasonable arrangements to recover the minerals.

D. CONTRARY TO APPELLEE DOMINION'S ASSERTIONS IN THE "DISCUSSION" SECTION OF ITS RESPONSE BRIEF, THE AMENDED COMPLAINT ADEQUATELY PLEADS ABANDONMENT, FRAUD OR EXTREME HARDSHIP, AND APPELLANT HAS OFFERED EVIDENCE OF SAME

While Appellee Dominion acknowledges that the controlling decision of *Adkins, supra*, recognized "a lessor's right to cancellation of an oil and gas lease on the ground of abandonment and upon circumstances of fraud or extreme hardship" ("Brief of Appellee," p. 16), Appellee nevertheless argues erroneously that "[n]one of the circumstances recognized by this Court as creating a possible remedy of rescission is present in this action." *Id.* To the contrary, the requisite elements set forth in *Adkins* have been adequately pled or have been shown through clear evidence presented to the Circuit Court through expert witness testimony, affidavits and other factual evidence.

Appellant Welch has continuously asserted throughout this litigation that her case effectively presents a *prima facie* case of "extreme hardship," as envisioned by this Court when it handed down its decision in *Adkins*, back in 1932. As more fully discussed in Appellant Welch's Brief, the Circuit Court of Ritchie County committed reversible error by failing to address the "hardship" factor set forth in *Adkins*.

The lower court merely stated: “The Court further finds no evidence of undue hardship on plaintiffs.”

(Order, November 15, 2006, p. 3)

The Circuit Court’s finding is erroneous in light of Appellant Welch’s clear evidence of hardship. In the 1970s, Appellee Dominion “farmed out” drilling operations to United Operating (Enervest’s predecessor in title, (*see* Complaint, ¶ 13), resulting in only three closely grouped wells on the immense 850-acre tract. Production figures show that in December, 2003 – the month that this litigation was initiated – Mrs. Welch earned less than \$30 per month in royalties from the entire 850-acre tract! Obviously, your Appellant has suffered emotional and financial hardship in the extreme, and has been frustrated with the knowledge – based on reliable expert information submitted to the Circuit Court – that this massive leasehold would certainly be highly profitable but for Appellee Dominion’s impermissible “tying up” of the land. As stated in *Hutchinson v. McCue*, 101 F.2d 111, 119 (4th Cir. 1939), quoting early West Virginia cases, in order for oil and gas operations to be effective, they “must be vigorous, diligent, and efficient, convincing that the real purpose is to strike ‘pay dirt’ at the earliest moment possible.” Thus, Appellee Dominion’s long term failure to develop has prevented the Flanagan lease from striking “pay dirt,” resulting in extreme hardship for Mrs. Welch!

Appellee Dominion has essentially abandoned the entire leasehold,⁵ should this Court choose to adopt the persuasive analysis of *Imperial Colliery Company v. OXY USA Inc.*, 912 F.2d 696, 1990 U.S.

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Appellant Welch recognizes the rebuttable legal presumption, provided by West Virginia Code § 36-4-9a, of a lessee’s intention to abandon, and confirms that she has not plead abandonment pursuant to that statute.

App. LEXIS 14835 (4th Cir. 1990), citing *Goodwin v. Wright*, 163 W. Va. 264, 255 S.E.2d 924 (1979) and *Clifton v. Koontz*, 160 Tex. 82, 325 S.W.2d 684 (1959).

In her Brief, Appellant Welch asserts that the three “marginal wells” on the Flanagan Lease are not producing in “paying quantities” pursuant to the *Imperial/Clifton* analysis in that a reasonably prudent operator would not continue to operate the subject leasehold as it is currently being operated, if not for speculative purposes. Thus, Appellant Welch argues, the Flanagan Lease has effectively terminated due to a cessation of production in paying quantities. (See “Brief of Appellant,” pp. 35-37)

At page 17 of its Response Brief, Appellee Dominion offers a poorly contrived argument in opposition to Appellant Welch’s position set forth in her Brief, as follows:

For purposes of this Court’s *de novo* analysis, the equities herein must be evaluated with regard to relevant case law as well as the current public policy announced by the West Virginia Legislature, which is to “[f]oster, encourage and promote exploration for the development, production, utilization and conservation of oil and gas resources.” West Virginia Code § 22C-9-1(a)(1)

Appellee Dominion states erroneously that this Court “rejected a similar argument in *Powers v. Union Drilling, Inc.*, 194 W. Va. 782, 461 S.E.2d 844 (1995).” (“Brief of Appellee,” p. 17) Appellee’s analysis is entirely mistaken, as *Powers* contains no language that detracts from Appellant’s position that the current public policy, as espoused in West Virginia Code § 22C-9-1 (above) is relevant to this discussion. A review of the four corners of *Powers* reveals absolutely no reason why this Court should not consider this important public policy in considering the merits of this appeal, as Appellee Dominion suggests. (See Syllabus Pt. 6, *Wellman v. Energy Resources, Inc.*, 210 W. Va. 200, 557 S.E.2d 254 [2001], which references “the public policy favoring the conservation and maximum recovery of oil and gas . . .”)

Finally, pursuant to this particular line of argument, Appellee Dominion asserts that it has “attempted and offered to drill on Welch’s property” (“Brief of Appellee,” p. 21)⁶ It is important to this Court’s analysis that these “attempts and offers” have all come after the filing of the lawsuit. There was absolutely no effort on the part of Appellee Dominion to develop the subject leasehold prior to the filing of the lawsuit. As discussed earlier in this Reply Brief, Appellee Dominion does not operate any gas wells upon the grossly underdeveloped Flanagan Lease, and Enervest Operating, LLC owns three marginally productive oil and gas wells upon the subject leasehold. (See “Brief of Appellant,” pp. 2, 5, 10, 11, 22 and 28) As this Court must recognize, Appellant Welch was under no obligation to acquiesce to Appellee Dominion’s belated overtures at this point of the litigation – nor should there be any negative inferences drawn from her decision to have her claims against Appellee Dominion fully and fairly resolved in a court of law. Appellant Welch was not obligated to settle or compromise her cause of action at that point of the litigation. Syllabus Pt. 2, *Gooden v. Frisby*, 176 W.Va. 547, 346 S.E.2d 66 (W.Va. 1986), provides:

A mere proposal by plaintiff amounting to a proposition of compromise of a claim for damages for breach of contract, unaccepted by defendant will not estop or bar him of his right of action against defendant. *Syllabus Point 5, Smith v. Atlas Pocahontas Coal Co.*, 66 W. Va. 599, 66 S. E. 746 (1909).

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Later, at pages 23-24,26 and 29 of its Response Brief, Appellee Dominion again discusses its willingness to further develop the lease by attempting and offering to drill. For purposes of brevity, Appellant’s arguments in reply, which are set forth on this and the following page, will be sufficient response on that issue and shall not be repeated later herein.

Moreover, this Court's attention is directed to Rule 408 of the West Virginia Rules of Evidence which provides, in pertinent part, as follows:

Rule 408. Compromise and offers to compromise.

Evidence of (1) furnishing or offering or promising to furnish, or (2) accepting or offering or promising to accept a valuable consideration in compromising or attempting to compromise a claim which was disputed as to either validity or amount is not admissible to prove liability for or invalidity of the claim or its amount.

Therefore, Appellant Welch's refusal to accept Appellee Dominion's calculated, strategic and belated offers to drill and efforts to compromise her claims after the filing of the lawsuit, should not bar Appellant Welch's litigation rights in any way, nor should it lead to any inference or conclusion that she has not suffered "extreme hardship."

II. CONCLUSION

Therefore, for all of the foregoing reasons, and in addition to those discussed in the "Brief of Appellant," Mrs. Mary Maxine Welch respectfully requests that the Order of the Circuit Court of Ritchie County entered November 15, 2006, granting Defendant's Motion to Dismiss and Strike and dismissing those portions of the Amended Complaint relating to partial rescission, be reversed. Thus, your Appellant requests that this Court hold that the lessor of an oil and gas lease is entitled to the remedy of partial rescission or reformation of the lease where there is a lack of diligence on the part of the lessee in developing the lease and the lack of diligence results in extreme hardship to the lessor.



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