

Post-Production Costs The Value for Leaseholders

What are the benefits to the landowner?

Activities reflected in post-production expenses add significant value for both the leaseholder and operator. By processing and preparing the natural gas and delivering it for ultimate sale, both the leaseholder and operator will receive a higher payment per mcf, reflecting the value which has been added to the natural gas.

What can property owners negotiate when they lease their natural gas rights?

Natural gas cannot be extracted without the consent of the property owner, which is typically the landowner. Therefore, no lease can be executed without the consent of the property owner, meaning just about any facet of the proposed lease can be negotiated until it meets with the property owner's approval. Typical provisions include:

- The duration of the initial term of the lease (how long an operator has to drill).
- The amount of the signing bonus (typically an amount per acre leased).
- The royalty rate (provided that it is at least one-eighth, or 12.5 percent of the net value of the gas).
- Where the operator may drill on the leased property or whether the natural gas must be accessed from an adjacent property, or other considerations of importance to the property owner.

However, no lease provisions can be in conflict with applicable federal, state or local laws. For example, no lease provisions can ease the environmental protection and permitting standards required of the operator to extract the natural gas.

If Pennsylvania has a minimum royalty act, why is my royalty rate less than 12.5 percent?

Pennsylvania's minimum royalty act specifies that leases entered into after September 18, 1979 must provide a royalty rate of at least 12.5 percent to the leaseholder (property owner). Under the law, operators and leaseholders also share proportionally in post-production costs in order to get product in a marketable state and to an ultimate point of sale. Once these costs are deducted from the gross value of the natural gas, the leaseholder receives at least 12.5 percent - or more, if agreed to in the lease - of the net sale proceeds. It is important to remember that the post-production costs are shared proportionally, unless otherwise specified in the lease, meaning that the operator's proceeds are also based upon the net sale proceeds.

What other leaseholder protections are included in the Oil & Gas Lease Act?

Act 66 of 2013 amended the Oil and Gas Lease Act to require that an operator provide, at a minimum, the following information: month, year and amount of natural gas produced; price received per mcf; severance tax and other production taxes and deductions permitted under the lease; net value of total sales received; the leaseholder's interest, expressed as a decimal or fraction; gross and net amount of the leaseholder's share of the proceeds; and contact information for the producer. The required information shall be provided to the leaseholder as part of the royalty check stub or in some other appropriate manner furnished to the leaseholder on a regular basis.

Further, Act 66 states that if a conflict arises between the operator's division order and an oil or gas lease, then the terms and conditions of the lease shall control. A division order may not amend or supplement the terms and conditions of a lease.

Additionally, under the Pennsylvania Constitution's impairment of contracts clause, no ex post facto law may be enacted which alters or impairs the obligations, terms and conditions of a lease.