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Every Landman Wants One!

Volume X, Issue VII | March, 2017

LAAPL
Los Angeles Association of Professional Landmen

Presidents Message

John R. Billeaud, RPL
President
Sentinel Peak Resources

Dear LAAPL members and friends,

As I am writing this message, oil prices are moving in the wrong direction and WTI has just dipped below $50/bbl – the first time since December of last year when the OPEC production cut deal was announced. Apparently, the reason behind the descending prices is a recent report released by EIA showing considerable increases in U.S. production output; I suppose this is due to the undying eagerness of the U.S. oil industry to ramp-up and maximize production again and heeding the advice of J. Paul Getty, "formula for success: rise early, work hard, strike oil". It may be best to slow down a bit and find a happy, economic medium to keep prices from this somewhat precipitous decline.

Moreover, there is some good news to report regarding our industry in that the Dakota Access Pipeline and Keystone Pipeline projects are moving forward, with Dakota Access projected to be in operation by the end of the month. The Dakota Access Pipeline will likely go down in history as one of the most controversial U.S. midstream projects ever for no valid reason. What's better - hundreds and hundreds of eighteen-wheelers/heavy duty trucks carrying flammable product(s) and eating up Mid-West roadways? Or one 30-42" pipeline buried below the surface, capable of transporting half of the total production from the Bakken shale to major refineries throughout the Mid-West? Not to mention over 12,000 people have jobs because of the project and it is anticipated to create an impact to the North Dakota economy of roughly $100 million annually. Just imagine what kind of impact to the economy and job creation Keystone will have. Joe Munsey will tell me I'm

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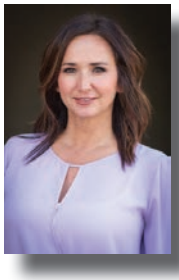
Meeting Luncheon Speaker



Debra Montalvo Russell, Vice President Community Relations and Real Estate Operations, has served as Director of Business Development and Community Relations for Signal Hill Petroleum, Inc. since 2005, and was promoted to Vice President Community Relations and Real Estate Operations in 2017.

In her multi-faceted role, she manages real estate operations, government affairs, urban seismic ventures and leads the community relations team, which promotes giving and events that improve the quality of life in Signal Hill and beyond. Mrs. Russell is a strong advocate for the oil and gas industry.

She earned her Bachelor's Degree in international business from California State University, Fresno and is deeply involved with her community. Mrs. Russell currently serves on the boards for the Long Beach Chamber of Commerce, The Ukleja Center for Ethical Leadership at California State University Long Beach, and Signal Hill Police Foundation.

Opinionated Corner

Joe Munsey, RPL
Director
Publications/Newsletter Co-Chair
Southern California Gas Company

Spring is in the air. California appears to be thawing out from its deep freeze of a winter. The much sought after California weather we all moved here to enjoy is finally back. As far as I can remember, at least since 1991, this has been one brutal winter with cool days and bitter nights. California certainly needed the rain but the distressing weather that came with it was not welcomed. Alas, we are back to living in Paradise.

However chilly the days or nights have been, it did not help moderating the heat index coming off the hot collar of our Governor Brown. Writing for *The Nation*, Michael J. Mishak, the Center for Public Integrity, on February 13, 2017, as reported in *Energy In Depth* on February 20th, admitted California is well known nationally as a laboratory of progressive values and environmental protection, California is perhaps the last place one would expect Big Oil to hold sway. The State has passed some of the toughest energy regulations in the country and set aggressive new goals to cut greenhouse-gas emissions.

Since the election of Donald Trump, Governor Jerry Brown has positioned California as a bulwark against a new president who sees climate change as a "hoax" and a White House that promises to appoint the most pro-drilling Cabinet in American history. **"We've got the scientists, we've got the lawyers, and we're ready to fight,"** the governor thundered during a speech in San Francisco in December of last year.

Well, that is a mouthful of rhetoric coming from our illustrious Governor. Why stop with scientists and lawyers? Just tell it to us straight, what you really meant to say, as inspired by the hit tune penned by Warren Zevon, **you are bringing lawyers, guns and money to the fight.** We guess Governor Brown wants certainty that everyone in the Golden State will bend to his idea on who is right on the science of climate change, even if it takes putting the proverbial gun to their heads.

According to a Wiki-Leaks dump several years ago, the numbers had been cooked, [pun intended]. Climate change was based upon nebulous data - hey, wait a minute, I think it was called global warming back in the day. The University of East Anglia in Norwich, United Kingdom [Britain], ground zero of the climate change community, had been caught red handed manipulating the indicators.

As reported in the *National Review*, dated March 6, 2017, John Bates, a climatologist who recently retired from the National Oceanic and Atmospheric Administration, aka NOAA, pronounced as Noah – as in Noah and the Ark, has also cast doubts on the matter. The scientists behind some of the miscalculation processed used incomplete, unverified data; processed it with the unfinished, buggy software; ignored contrary evidence and relied on unsound assumptions.

Maybe we should invite some of those fellows from that scientific community to join us at our upcoming luncheon at the Long Beach Petroleum Club. Our guest speaker, Debra Russell, Vice President Community Relations and Real Estate Operations, for Signal Hill Petroleum will discuss "Industry Ethics and Stewardship." If you are an RPL or CPL, you will receive one (1.0) hour for continuous education credits (ethics) from AAPL.

President's Message
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preaching to the choir.

In other news, we are pleased to announce the new LAAPL website was launched on February 20th providing LAAPL and its members/friends with a more modern, user-friendly platform. A special thanks goes out to Sarah Bobbe (LAAPL Vice President) and Suzy Husner (LAAPL Treasurer/interim Website/Communications Chair) for making this happen. Please note, we are still making improvements to the website and welcome any feedback so that we may continue to develop and improve the website for our members and interested parties. Also, we are looking for someone that is interested in assuming the role of LAAPL's Website/Communications Chair, so please let us know if you are interested.

In case you have not heard, AAPL will hold its Annual Meeting in Seattle this year and the dates are June 21-24. This is a great opportunity for California to gain recognition from AAPL as we are often forgot about on the West Coast. Therefore, we strongly encourage everyone to attend and represent California Landmen on a national scale.

Our March luncheon will be held on Thursday, March 16th at the usual time (11:30 am) and location, Long Beach Petroleum Club. We will have Debra Russell, who is Vice President of Community Relations and Real Estate Operations at Signal Hill Petroleum, speak about industry ethics and stewardship. We hope all of you can make it on Thursday and look forward to seeing you there.

Regards,

John R. Billeaud, President

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310-349-0051

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Leah Hoover

Chapter Board Meetings

Brandi Decker
California Resources Corporation
LAAPL Secretary

The LAAPL Board of Directors and Committee Members held a conference call on Tuesday, February 7, 2017, led by President John R. Billeaud, RPL. The topics discussed at the meeting are as follows:

- Submit and finalize LAAPL name change with CA Secretary and Franchise Tax Board
- Education Chair and Nominations Chair positions have been filled
- Remind members that they can receive an hour credit for Ethics at the meeting in March
- Map Right may be interested in writing an article for the newsletter of speaking at a meeting
- Send out monthly reminders about membership dues

We encourage all members to attend our LAAPL Board Meetings. The meetings are typically held in the same room as the luncheon immediately after the meeting is adjourned.

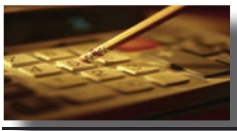
Scheduled LAAPL Luncheon Topics and Dates

March 16, 2017
Debra Russell, Community Relations Director
Signal Hill Petroleum
"Industry Ethics and Stewardship"

May 18, 2017
Wayne Rosenbaum, Esq., Partner, Opper & Varco, LLP
Jerermy N. Jungreis, Esq., Rutan and Tucker
"Stormwater Regulations and Their Impacts on the California Oil and Gas Industry"

Officer Elections

Dark for the Summer



Treasurer's Report

Suzy Husner
Treasurer
Independent

As of 12/30/2016, the LAAPL account showed a balance of	$25,249.99
Deposits	$480.00
Total Checks, Withdrawals, Transfers	$235.03
Balance as of 2/28/2017	**$25,494.96**
Merrill Lynch Money Account shows a total	Not available

Call for Dues

LAAPL Call For Annual Dues

Suzy Husner, Independent
LAAPL Treasurer

Per Chapter by-laws, a Notice for Dues will be sent out to LAAPL Chapter Members. Renewal is $40.00; upon receipt please send your renewal notices along with your payment as follows:

Suzy Husner
LAAPL Treasurer
16126 S. Western Avenue, #149
Gardena, CA 90247-3710

Taylor Land Service Inc.

Randall Taylor, RPL
Petroleum Landman

Taylor Land Service, Inc.
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Suite 200
Laguna Niguel, CA 92677
949-495-4372
randall@taylorlandservice.com

Lawyers' Joke of the Month

Jack Quirk, Esq.
Bright and Brown

Once upon a time, a blond became so sick of hearing blond jokes that she had her hair cut and dyed brown.

A few days later, as she was out driving around the countryside, she stopped her car to let a flock of sheep pass. Admiring the cute woolly creatures, she said to the shepherd, "If I can guess how many sheep you have, can I take one?" The shepherd, always the gentleman, said, "Sure!"

The blond thought for a moment and, for no discernible reason, said, "352." This being the correct number, the shepherd was, understandably, totally amazed, and exclaimed, "You're right! O.K., I'll keep to my end of the deal. Take your pick of my flock."

The blond carefully considered the entire flock and finally picked the one that was by far cuter and more playful than any of the others.

When she was done, the shepherd turned to her and said, "O.K., now I have a proposition for you. If I can guess your true hair color, can I have my dog back?"

Our Honorable Guests

January's luncheon was a successful joint meeting with the Los Angeles Basin Geological Society and Los Angeles Association of Professional Landman held at the Grand at Willow Street Conference Center. LAAPL were the guests of honor.

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New Members and Transfers

Cambria Rivard, JD
Membership Chair
California Resources Corporation

Welcome! As a Los Angeles Association of Professional Landmen member, you serve to further the education and broaden the scope of the petroleum landman and to promote effective communication between its members, government, community and industry on energy-related issues.

New Members

Gregg Kozlowski
President
Makoil Inc.
910 Calle Negocio, #210
San Clemente, CA 92673
(949) 462-9010
Makoil@msn.com

Rose Pickenpaugh
Manager Land
California Resources Corporation
10000 Stockdale HWY
Bakersfield, CA 93311
(661) 412-5159
Rose.pickenpaugh@crc.com

New Member Requests

Brennan Guldner
Chevron USA Inc.
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Bakersfield, CA 93311
(661) 412-6251
BrennanGuldner@Chevron.com

Blake Barton
Signal Hill Petroleum
Land Technician
2633 Cherry Ave
Signal Hill, CA 90755
(562) 326-5249
bbarton@shpi.net

Corrections

None

2017 – 2018 Officer Election

John R. "JR" Billeaud, RPL, Chapter President, appointed L. Rae Connet, Esq., of Petroland Services, Inc., as LAAPL's Nominations Committee Chair. A partial list of qualified candidates[1] has been set forth below and the elected officers will serve from July 1st, 2017 – June 30th, 2018. Nominations Chairwoman Connet will provide an amended slate of officers and will send out to the membership via email no later than April 15th. **Additional nominees may be submitted to Rae Connet, Esq., rconnet@petrolandservice.com to be included on the final candidate's list until May 18, 2017, which will be published in the May newsletter**. Officers will be elected by a vote of membership in attendance at the May 18, 2017, chapter meeting held at the Long Beach Petroleum Club. Nominations will also be accepted from the floor at the May 18, 2017, regular meeting.

President[2]	Sarah Bobbe, CPL, Land Manager, Signal Hill Petroleum
Past President[3 & 4]	John R. Billeaud, RPL, Senior Landman, Sentinel Peak Resources

OFFICE		**CANDIDATE**
Vice President	☐	
	☐	
Secretary	☐	Brandi Decker, California Resources Corporation
	☐	
Treasurer	☐	.
	☐	
Directors (Vote for two only)	☐	
	☐	
	☐	
	☐	Joseph D. Munsey, RPL, Senior Land Advisor, Southern California Gas Company

[1]Per Section 7(7)(a) prior to the regular meeting scheduled nearest to April 15th of each membership year, the membership will be provided with a list of the nominees for officers of Vice President, Secretary, Treasure and the two (2) Directors.
[2]Per Section 7(3) the Vice President shall succeed to the office of the President after serving his or her term as Vice President and shall hold the office of President for the next twelve (12) months.
[3]Per Article 8 (2) the outgoing President shall serve as Past President.
[4]Per Article 8 (2) the outgoing President shall serve as Director.

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rconnet@petrolandservice.com

EDUCATIONAL CORNER

Joseph D. Munsey, RPL
Education Char

AAPL's Home Study program allows members to earn continuing education credits at their own convenience and schedule. The courses cover the issues most relevant to today's landman and cost between $30 and $75 to complete.
To receive continuing education credits via a home study course:

- Download or print out the course (PDF format)
- Answer all questions completely
- Submit the answers as instructed along with the appropriate fee

If you have questions or would like more information, please contact AAPL's Director of Education Christopher Halaszynski at (817) 231-4557.

DATE	EVENT	CREDITS
3/23/2017	Due Diligence Seminar- Denver, CO	5.00 CEU
3/24/2017	Microsoft Excel for the Landman - Fort Worth, TX (Webinar Available)	7.00 CEU
3/28/2017 - 3/31/2017	Oil and Gas Land Review, CPL/RPL Exam - Lafayette, LA Great opportunity to catch up on RPL/CPL credits!	18.00 CEU 1.00 ETHICS
3/30/2017	Field Landman Seminar - Midland, TX	2.00 CEU
4/4/2017	One Day JOA Workshop - Oklahoma City, OK	7.00 CEU
4/21/2017	Landman 2.0 Series: Workout, Workover & DoOver? - Fort Worth, TX (webinar available)	4.00 CEU
4/24/2017	2017 Southwest Land Institute - Dallas, TX (webinar available)	7.00 CEU
4/28/2017	Due Diligence Seminar- Midland, TX	5.00 CEU
5/2/2017 - 5/5/2017	Oil and Gas Land Review, CPL/RPL Exam - Pittsburgh, PA Great opportunity to catch up on RPL/CPL credits!	18.00 CEU 1.00 ETHICS
5/11/2017	Oil and Gas Lease Fundamentals - Fort Worth, TX (webinar available)	6.00 CEU
5/17/2017 - 5/18/2017	RMMLF Oil and Gas Agreements: Surface Use	12.50 CEU 1.00 ETHICS

General Credit Courses:

Environmental Awareness for Today's Land Professional Credits approved: 10 CPL/ESA/RPL/RL
$75.00

#101 Due Diligence for Oil and Gas Properties
Credits approved: 10 CPL/RPL/RL
$75.00

#102 The Outer Continental Shelf
Credits approved: 5 CPL/RPL/RL
$37.50

#104 Of Teapot Dome, Wind River and Fort Chaffee: Federal Oil and Gas Resources
Credits approved: 5 CPL/RPL/RL
$37.50

#105 Historic Origins of the U.S. Mining Laws and Proposals for Change
Credits approved: 4 CPL/RPL/RL
$30.00

#106 Going Overseas: A Guide to Negotiating Energy Transactions with a Sovereign
Credits approved: 4 CPL/RPL/RL
$30.00

#108 Water Quality Issues: Safe Drinking Water Act
(SDWA)/Clean Water Act (CWA)/Oil Pollution Act (OPA)
Credits approved: 4 CPL/ESA/RPL/RL
$30.00

#109 Common Law Environmental Issues and Liability for Unplugged Wells
Credits approved: 4 CPL/ESA/RPL/RL
$30.00

Ethics Credit Courses: Two ethics courses are available. Each course contains two essay questions. You may complete one or both of the questions per course depending on your ethics credits needs. Each question answered is worth one ethics continuing education credit.

#103 Ethics Home Study (van Loon) – 1 or 2 questions
Credits approved: 2 CPL/RPL/RL & 2 Ethics
$15.00 per question

#107 Ethics Home Study (Sinex) – 1 or 2 questions
Credits approved: 2 CPL/RPL/RL & 2 Ethics
$15.00 per question

Mike Flores
Flores Strategies LLC

State of California

Weak Cap and Trade Raises Concerns

The recent Cap and Trade auctions were estimated to bring in billions per year, but results of the March 1st auction revealed that just 16.5 percent of the 74.8 million metric tons of emission allowances were sold at the floor price of $13.57 per ton. CARB was offering 43.7 million tons of state-owned emission allowances, but sold just 602,340 tons of advance 2020 allowances, which means the state will see only $8.2 million, rather than the nearly $600 million it could have received from a sellout. While many lawmakers once saw the Cap and Trade auctions as a cash cow, they may have to narrow spending from the fund to the program's intended purpose: reducing greenhouse gas emissions.

California Senate President Pro Tempore Kevin de Leon (D-Los Angeles) had the following statement as a reaction to the March 1st results, " Today's anemic auction results demonstrate the state's landmark cap and trade program is in need of reform and the kind of market certainly that only the Legislature and Governor can provide via statute. We need a program that both reduces pollution and provides stable funding to clean climate emissions."

The following is a statement from WSPA President Catherine Reheis-Boyd on the quarterly cap and trade auction results:

"Today's auction results are a clear indication that there's room for improvement in the state's existing cap and trade program. Western States Petroleum Association and its member companies believe focusing on a market mechanism to achieve California's climate goals is the prudent approach.

Low Carbon Fuel Standard (LCFS) and other direct command and control regulations are artificially depressing the market and some stakeholders are pushing to get rid of the cap and trade program entirely, which undermines the certainty of the program, leading to meager results and an unsustainable market.

WSPA and its members look forward to working with state regulators and other stakeholders on a climate program that works towards achieving California's climate goals while protecting the economy and California families, consumers and businesses."

New Joint Committee on Climate Change Created in the Legislature

Assembly Speaker Anthony Rendon (D-Southgate) and the Senate Rules Committee announced their appointments to the newly created Joint Legislative Committee on Climate Change Policies (JLCCCP) that is tasked to, "ascertain facts and make recommendations to the Legislature concerning the state's programs, policies, and investments related to climate change."

Legislative Update continued on page 11

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Legislative Update
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The six-member Committee is composed of three representatives from the Assembly and three from the Senate.

Santa Barbara County Supervisors Oppose Oil-By-Rail in San Luis Obispo

Santa Barbara County joined a long list of cities, counties and school districts opposing an oil-by-rail project in southern San Luis Obispo County. Eighteen months ago, the Santa Barbara County Board of Supervisors agreed to ask their counterparts to the north to reject the request to expand a rail spur at the Phillips 66 refinery just north of the county line. The refinery currently receives its oil by pipeline, and the Houston-based energy company wants to process oil transported by train.

The plan is for 5,200-foot trains that the new tracks would be built for can each transport nearly 2.2 million gallons of oil. Phillips 66 proposed that three trains arrive at the refinery per week. In 2015 the San Luis Obispo County Planning Commission denied the rail-spur extension after days of hearings and, according to Litten, more than 24,000 letters of opposition. Several other counties, a number of school districts, and numerous cities, including Santa Barbara, Goleta and Carpinteria, have also sent letters of opposition. The San Luis Obispo supervisors will consider an appeal of that decision on Monday, March 11.

Senator De León Wants 100% Renewable Mandate by 2045

The California Senate leader has introduced legislation that would require the Golden State to get 100 percent of its electricity from climate-friendly energy sources by 2045. That's a big step up from the state's current renewable energy mandate, 50 percent by 2030 — a target that's only been on the books for a year and a half, and that California is still a long way from meeting.

De León's bill would require California to hit 50 percent renewable energy by 2025, five years sooner than under current law, and phase out fossil fuels entirely by 2045. It's not yet clear whether the Senate leader will move forward the proposal, which he introduced before the state's bill-filing deadline on Friday, almost certainly to serve as a placeholder for more detailed legislation that could be fleshed out later.

LA County Versus DOGGR Suit is Related to Earthquake Concerns

In a move prompted by the "very real" threat of earthquakes, Los Angeles County has sued state regulators to keep the Aliso Canyon natural gas storage facility closed. The facility was closed after a massive leak was discovered on October 23, 2015, and lasted four months, in the process releasing nearly 100,000 tons of methane.

The lawsuit accuses California state oil and gas regulators of prematurely ending a safety review before fully knowing the seismic risk of Aliso Canyon and the cause of the 2015-2016 gas leak. There has been no response from DOGGR. Aliso Canyon is in northwest Los Angeles County, approximately 40 km from downtown Los Angeles. Since 2006, there have been 16 thousand, 2.0-4.7 Richter scale earthquakes in the canyon.

Additionally, the Santa Susana fault within the Sierra Madre fault zone runs right underneath and next to the natural gas storage facility. Furthermore, one of the state's Alquist-Priolo fault zones is right next to the facility.

Around the USA

Ohio Court Rules Landmen Need to be Licensed Real Estate Broker to Receive Compensation

Ohio's Seventh District Court of Appeals recently held that landmen are subject to the requirements of R.C. Chapter 4735 requiring real estate broker's licenses in order to be entitled to compensation for brokering deals with landowners on behalf of oil and gas companies.

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Legislative Update
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In *Dundics v. Eric Petroleum Corp.*, plaintiff landmen alleged that they were not compensated by the defendant oil and gas company for their work in assisting the company with negotiating and obtaining oil and gas leases in Ohio. The company moved to dismiss the lawsuit, asserting that the landmen were not licensed Ohio real estate brokers, and therefore, were barred from recovering under R.C. 4735.21, which precludes the recovery of compensation for "real estate. . . brokerage transaction[s]" unless the person brokering the transactions is a licensed estate broker.

Agreeing with the lower court's ruling, the appellate court held that "real estate," for purposes of the statute, was broadly defined to include "leaseholds as well as any and every interest or estate in land" – which, under Ohio law, includes oil and gas rights. And so, to be entitled to compensation for brokering in oil and gas rights, the landmen needed to be licensed. The court rejected the landmens' argument that R.C. 4753.21 was inapplicable because oil and gas was different from traditional real property, noting that "the fact that oil and gas rights are different does not excuse third parties who ask the courts to enforce their engagement with either owners of surface real estate or those who wish to extract subsurface oil and gas from the real estate broker's license requirement at issue here." Also, based on its conclusion that the statute was unambiguous, the Court declined to consider "legislative intent, legislative history, public policy, [or] the consequences of [its] interpretation."

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Farmout Agreements

By **Manning Wolfe, Esq.**

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Definition:

An oil and gas Farmout agreement is a commitment by the owner of an oil and gas lease, the Farmor, to assign all or part of the working interest in that lease to another party, the Farmee. It is not clearly established when the first Farmout agreement was executed, but by the 1940's the term Farmout was freely used.

Farmout Agreements are often the most commonly negotiated agreements in development of a field, after the oil and gas lease. In a Farmout agreement, the primary consideration being services, rather than the exchange of money, makes it different from the conventional drilling transaction. The Farmee agrees to exchange services for an assignment of a future percentage of ownership in a certain lease or leases, which occurs when the required acts are accomplished. The typical acts to be performed under a Farmout agreement is the drilling of one or more oil and/or gas wells.

Acts Required:

Farmout agreements typically provide that the assigned working interest will be transferred to the Farmee upon the completion of:

1. The drilling of an oil and/or gas well to the defined depth; or
2. The drilling of an oil and/or gas well that produces at viably commercial levels as defined in the agreement.
3. Both 1 & 2 must be accomplished within a certain timeframe.
4. Farmout agreements usually include a complete definition of "payout" by stating exactly what will be deducted in calculating the payout amount.

Reasons to Enter Farmouts:

Farmors often enter into Farmout agreements in order to:

1. Preserve a lease by satisfying a primary term requirement, avoid Pugh clause consequences, satisfy continuous drilling obligations, etc.
2. Obtain production;
3. Share risk or monetize an abandoned project; and
4. Obtain geological information from the Farmee and the Farmee's operations.

Farmees often enter into Farmout agreements in order to:

1. Obtain an acreage position quickly;
2. Obtain acreage without leasing operations, and without expending capital on buying leases;
3. Utilize equipment and personnel that would otherwise not be utilized;
4. Develop an area while sharing risks;
5. Obtain geological information; and
6. Gain interest in a prospect area that is already leased, but the Farmor is not developing.

The Structure:

The negotiation of a Farmout agreement primarily rests on the goals and strengths of the negotiating parties. In a Farmout, the Farmor usually reserves an overriding royalty interest, with the option to convert the overriding royalty interest to a working interest in the lease, upon payout of drilling and production expenses, otherwise known as a back-in after payout (BIAPO). As an example, the agreement may provide for:

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BPO - Before Payout of Costs: 3% overriding royalty.
APO - After Payout of Costs: Option to keep 3% ORRI or convert to 25% WI (subject to royalty burden)

Payout occurs when the Farmee has recovered all of its drilling costs out of its share of production after deducting its operating costs, certain taxes, and other expenses.

Issues with Farmouts:

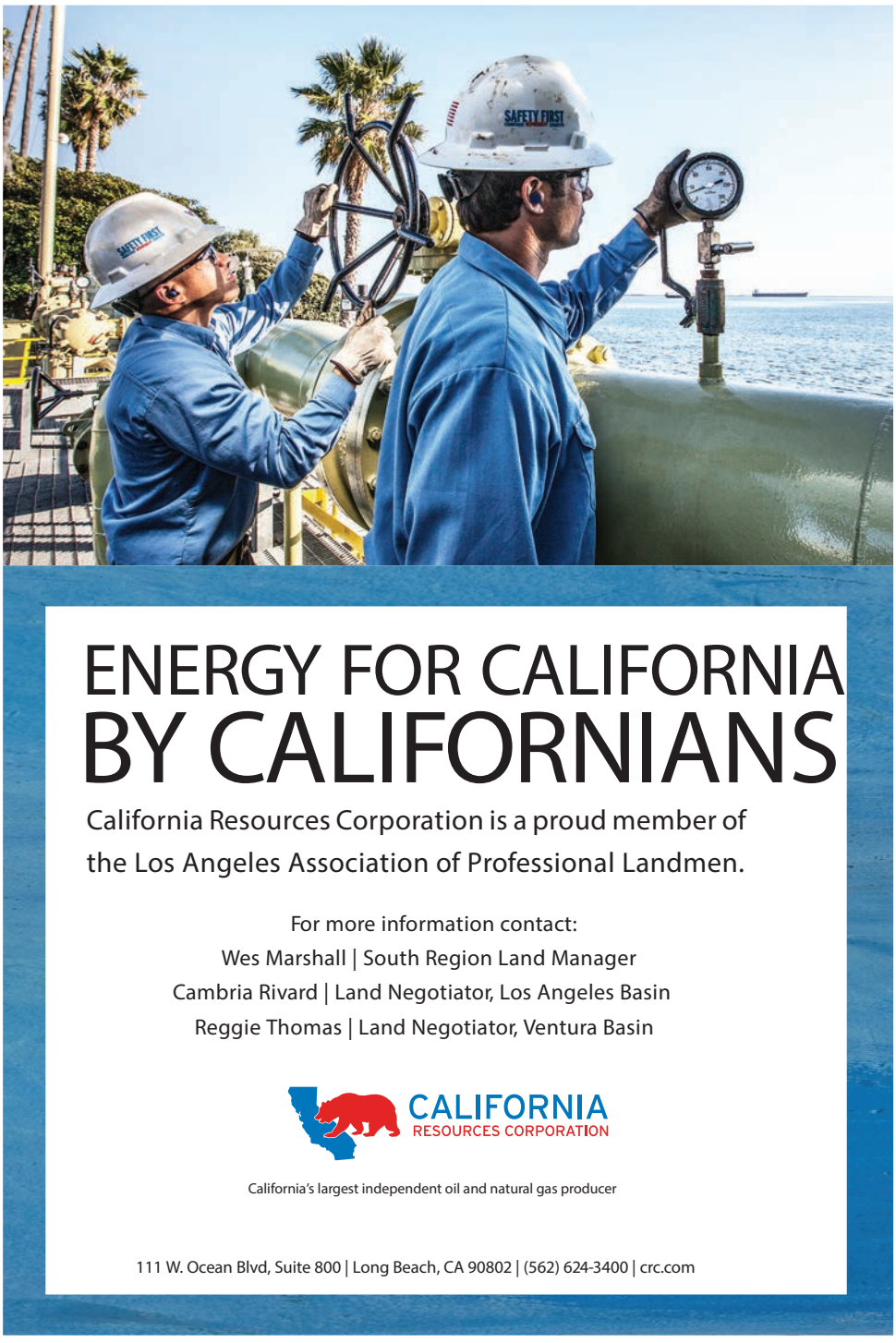
1. For land departments and title examiners, failure to record notice of the Farmout may result in lack of notice and therefore failure to protect the operator's lien rights. Recording of a memorandum of the Farmout agreement in the pertinent county solves this issue.

2. The conditions for earning an assignment and when the assignment will be delivered to the Farmee should be clearly drafted in the Farmout. Once the Farmee receives the assignment, it should be timely recorded in the county where the lands are located for the same reasons as discussed above.

3. Third, the election of the Farmor to retain an overriding royalty interest or convert it through a "convertible override" to a BIAPO working interest affects the rights of both parties and their successors-in-interest. Therefore, the Farmor's election must be clear from the records. The election should be reflected either in the recorded assignment or in a subsequently recorded instrument.

4. Other Farmout provisions of note include the formation of an AMI, or area of mutual interest, which obligates one party to the Farmout to offer the other party a certain percentage of the interest the first party acquires in oil and gas rights within the defined geographic boundary of the AMI.

5. A Farmout may contain a call on production clause, under which the Farmor has a continuing preferential right to purchase all oil and gas production from the Farmout acreage.



Conclusion:

Since there is no model form currently being used, Farmout clauses and construction may differ. Therefore, a Farmout must be carefully dissected in order to fully understand the obligations of each party to the agreement.

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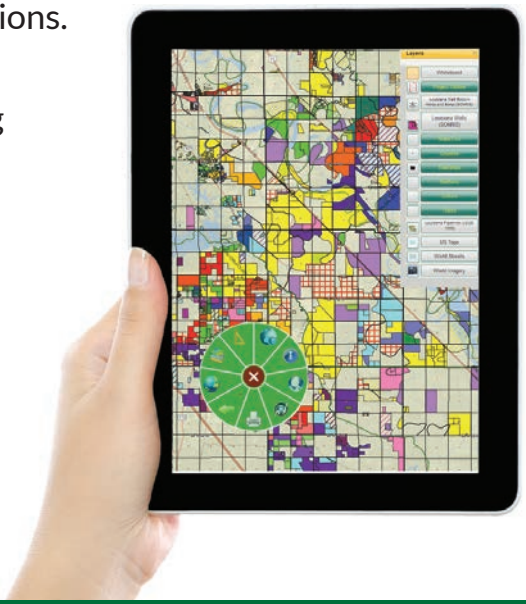

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The Cap Rate - A Potential Value Trap

By Chuck West, Esq., CCIM

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A capitalization rate or "cap rate" is a common method of valuing income producing property. It is commonly calculated by dividing a property's annual "net operating income" by its "market value." Hence an apartment complex having an annual net operating income of $100,000 and a value of $1,250,000 would have a cap rate of 0.08 or 8%. Using this rate with closed sales of "similar" apartment projects an appraiser or investor could compute the value of another property by applying the rate of 8% to the annual net operating income the property under consideration.

In common terms a cap rate could be compared to the savings rate on a passbook bank account where the savings account balance is equivalent to the value of the apartment complex in the above example and the simple interest earned per year is equivalent to the net operating income. Hence a passbook savings account with a $1000 balance yielding 5% annual simple interest (remember those days?) would have a net income of $50 per year. A higher cap rate is associated with a higher risk that an investment might not yield the expected return or net income.

The deficiencies of using a cap rate are many. The primary problem is based upon the fact that the net income used is generally that of the prior year or in some cases the prior year projected higher by a factor of expected increases in gross income and/or expected decreases in expenses where net operating income (NOI) is gross operating income less operating expenses (assuming a property is owned free and clear of debt). If the actual NOI is less than that which is projected one will in effect have paid too much for the property.

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Likewise the NOI as projected forward should only include operating expenses not capital improvements. Many sellers find that expensing capital improvements gives them favorable income tax treatment but then fail to back out the capital improvements from the NOI when marketing a property. This can hurt the seller in that the NOI will appear lower than it is and therefore the value might appear lower to a prospective buyer or lender.

A better yet more complicated tool for analyzing income property values is the internal rate of return (IRR) which measures the return of and on investments and takes into consideration the present value of an income stream over the life of an investment and computes the impact of initial investments, subsequent investments, income taxes and ultimately the net sales proceeds after the expected holding period.

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California to Consider Significant Change to Eminent Domain Law Regarding a Condemnee's Right to Recover Litigation Expenses

by David Graeler, Esq., Partner, Nossaman LLP

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On February 9, 2017, California Assembly Member Phillip Chen (a Republican from the 55th district) introduced Assembly Bill 408 (AB 408). AB 408 is styled as an "act to amend Section 1250.410 of the Code of Civil Procedure relating to eminent domain." There is very little history available on AB 408 and it appears that the next action is for it to be heard in committee on March 12, 2017. If AB 408 is ultimately approved in its current form, it would radically change the standards by which courts decide whether or not to award litigation expenses in eminent domain actions. This, in turn, could drastically impact public projects in California because property owners may have less incentive to settle pre-litigation or during early litigation. This could lead to increased costs, more trials, less judicial discretion, and more opportunity for mischief. Fundamentally, it could cause right-of-way costs to go up dramatically and projects may take longer to build.

Current Law

Currently, Code of Civil Procedure section 1250.410 enables a condemnee to recover litigation expenses (including attorneys' and experts' fees) only if a court finds that the condemning agency's final offer of compensation was unreasonable and that the final demand of the condemnee was reasonable viewed in light of the evidence admitted at trial and the compensation awarded in the proceeding. Section 1250.410 was originally enacted by the California Legislature in 1975. In the time that section 1250.410 has been on the books, a body of case law has developed that instructs a trial court to define reasonableness by looking at (1) the amount of the difference between the offer and the compensation awarded, (2) the percentage of the difference between the offer and the award, and (3) good faith, care, and accuracy in how the amount of the offer and the amount of the demand, respectively, were determined. (Los Angeles County Metropolitan Transportation Authority v. Continental Development Corp. (1997) 16 Cal.4th 694.)

In other words, the California Legislature trusted the courts to not only look at the numbers but also to look behind the numbers. It also imposed on a condemnee the obligation to make its demand in good faith and with care and accuracy. The idea that final offers that are less than 90 percent of the compensation awarded are per se unreasonable is an entirely new concept in California. Indeed, prior to Continental Development (which requires an analysis of good faith, care and accuracy), appellate courts at times applied a bright line numeric test. At least one court actually performed a survey of appellate cases and noted that "final offers which are 60 percent or less of the jury's verdict are found to be unreasonable while offers which are above 85 percent have been considered reasonable per se." (People ex rel. Dept. of Transportation v. Yuki (1995) 31 Cal.App.4th 1754, 1764.)

Changes Proposed by AB 408

AB 408 proposes to change section 1250.410 by essentially establishing a bright-line mathematical test. If the condemnor's offer is lower than 90 percent of the compensation awarded in the proceeding, the court shall award litigation expenses. If the court finds that the condemnor's offer was at least 90 percent and less than 100 percent of the compensation awarded in the proceeding, then litigation expenses may be awarded by the court. In other words, the court only has discretion when the ultimate compensation awarded is not more than 10 percent of the condemnor's final offer. Presumably, the trial courts would then be able to look at the good faith, care, and accuracy of the offer and demand. Notably, if the condemnor's offer is lower than 90 percent of the compensation awarded in the proceeding, the condemnee's final demand would appear to be irrelevant to the determination.

Is AB 408 a Good Idea?

In order to assess the possible impacts caused by new legislation, it is often good to look at the proponents of the new law. Assemblyman Chen represents the 55th district, which encompasses parts of Los Angeles, Orange, and San Bernardino counties. Prior to being elected to the state assembly, he was a school board trustee for the Walnut Valley Unified School District. In other words, he worked for a public agency. His website, however, indicates that he is currently a small business owner who owns and operates a property management company overseeing commercial and residential properties. As

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more details emerge concerning AB 408, it will be interesting to see who is supporting it monetarily. As they say, "follow the money."

For now, I provide my thoughts based on my experience as an eminent domain practitioner in California. One of the common questions we should always ask when it comes to public projects and eminent domain is whether society is placing too large of a burden on an individual citizen in order to promote the general welfare. Naturally, there are constitutional, statutory, and regulatory protections to afford condemnees with just compensation and rights to relocation assistance. But it is good to ask whether these protections are doing enough.

In my experience, section 1250.410 has worked well for many years to ensure that public agencies do not unreasonably "low ball" their final offers. It also ensures that property owners meet agencies half way by structuring their offers in good faith and with care and accuracy. This seems like the best way to promote settlement. AB 408 would appear to go too far in giving rights to condemnees. To best illustrate this, I'll provide three personal anecdotes.

The first involves an eminent domain action that I took to trial roughly 15 years ago. I represented the public agency in the case. The condemnee was a business tenant who was seeking compensation for lost business goodwill. The agency's expert believed that the business lost $75,000 due to the taking. Conversely, the business's expert opined that there was a goodwill loss in excess of $1.5 million. The agency's final offer totaled $150,000 and the condemnee's final demand totaled $700,000. The jury's verdict awarded compensation of $298,000. Clearly, the jury believed the agency's position was far more credible and its verdict resulted in the agency paying far less than the condemnee's final demand. The Court in this case denied litigation expenses because it found that the agency made its offer in good faith and with care and accuracy. Under AB 408, the agency's offer was only 50 percent of the compensation awarded, so the condemnee would have recovered its litigation expenses. Settlements are a two-way street. If a condemnee does not make a reasonable demand, it is forcing the case to go to trial. Should the condemnee be entitled to its litigation expenses under those circumstances?

In another trial involving a business's claim for loss of goodwill, my client prevailed at trial where the business received no compensation because it failed to prove its entitlement to compensation. The case was procedurally unusual because the court rendered its decision on goodwill entitlement after there had been a jury trial on compensation. The jury's verdict was higher than the business's final demand. Had there been no legal issue on entitlement, the business clearly would have been entitled to its litigation expenses. The trial court's decision on entitlement was later reversed on appeal, which meant the jury's verdict on compensation was reinstated. The business then filed a motion to recover its litigation expenses. While the agency's position on entitlement was wholly reasonable (indeed, it was accepted by the trial judge) and, thus, reflected in its final offer, the business was still awarded its litigation expenses. The court was able to use its sound discretion to look behind the numbers and to factor into consideration the total situation to arrive at what it believed was an equitable result.

More recently, I had a trial involving a goodwill claim that was made by a fast food restaurant. Once again, I represented the public agency in the case. The agency's expert believed the restaurant did not lose any goodwill. The business's expert testified that it would lose $550,000 in goodwill. The agency's final offer totaled $30,000, and the business's find demand actually exceeded $550,000 because it included numerous items that were not compensable under California law. In other words, the agency was presented with a choice of: (a) paying more than the best the business could hope for in trial, or (b) trying the case. This wasn't a difficult decision. The jury's verdict ultimately awarded the business $50,000. This was less than 10 percent of the business's total claim and even less than its final demand. But it was also 40 percent higher than the agency's final offer. Under AB 408, the business would have automatically been entitled to its litigation expenses. Under existing law, our trial judge denied the request by using her sound discretion. Clearly, the agency's offer was made with far greater care and accuracy than the condemnee's.

Final Thoughts

From a policy standpoint, a fundamental question that must be answered by our Legislature is whether it wants to eliminate virtually all discretion from the judiciary to reach a fair and equitable determination concerning litigation expenses. Generally speaking, this is not a good idea. Judges are in the best position to assess the facts and circumstances of a particular case to ensure that justice is achieved.

AB 408 carries a real risk that condemnees will simply refuse to make a reasonable final demand because their demands may be ignored if they beat the agency's final offer by 10 percent. Because jurors tend to compromise verdicts in eminent domain actions, we will likely see larger and larger claims for compensation because public agencies will have to effectively

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"split the baby" in order to avoid liability for litigation expenses. Even a relatively small partial acquisition of agricultural land worth $20,000 to widen a highway could result in wildly high claims for compensation because the property owner need only convince a jury to award 10 percent more than the offer in order to recover legal fees. Thus, instead of paying a nominal sum for the property, the agency may have to pay substantially more than the property is worth. These problems will likely be compounded by the reality that many, if not most, condemnees engage their counsel on contingency fees. Thus, there is very little downside for a condemnee to "roll the dice". The net impact is that public projects will become far more expensive to build because public agencies will have to offer far more money for claims that have no merit.

If the California Legislature wants to award litigation expenses in eminent domain actions more frequently, there must be a better way to achieve that goal.

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