Testimony of Madeline Bugh on Behalf of Dorchester Minerals, L.P.

House Bill No. 1520

Energy and Natural Resources Committee

Representative Porter, Chairman

February 9, 2023

Chairman Porter and members of the Energy and Natural Resources Committee, thank you for the opportunity to testify before you today in support of House Bill 1520. My name is Madeline Bugh, and I am in-house counsel for Dorchester Minerals, L.P. ("Dorchester"), which is located in Dallas, Texas. Dorchester actively owns and manages minerals, or some form of working interest or royalty interest associated with minerals located in roughly 37 counties in North Dakota. Dorchester has experienced many of the issues that House Bill 1520 seeks to address. My testimony, on behalf of Dorchester, is in favor of House Bill 1520 and will provide some key examples and explanations for the importance of the proposed amendments.

Section 1: Amendment to Section 38-08-04

Section 38-08-04 as currently written has caused confusion regarding whether issues of post-production deductions and various other issues regarding oil and gas royalty payments are properly within the jurisdiction of the North Dakota courts or whether they are within the jurisdiction of the North Dakota Industrial Commission ("NDIC"). The specific language of 38-08-04(b)(1) granting the NDIC the power to regulate "all other operations for the production of oil or gas" is confusing and misleading. In my own experience the current wording of this statute has caused both a delay in time and additional expense trying to determine proper jurisdiction. This is the crux of the issue. Whether a claim is within the jurisdiction of the NDIC versus the courts should be clear. The amendment as proposed would clear up much of this unnecessary confusion with regards to where jurisdiction is proper, thus saving mineral owners collectively an undoubtedly large amount of both time and money.

Section 2: Amendment to Section 38-08-06.3

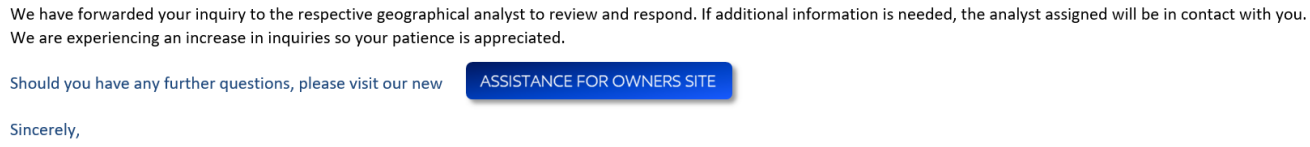
Dorchester supports the proposed amendments to Section 38-08-06.3, which seek to provide valuable information to minerals owners via electronic means rather than cumbersome paper checks. On their own, revenue checks are nearly impossible to determine the actual value attributable to a single well's monthly production. It is common to see reversals and reeboks going back several years—sometimes as much as eight or more years. When reversals and rebooks occur on a monthly basis, stretching back over the span of almost a decade, it becomes impossible to calculate what you are actually being paid for each month's production. Dorchester is fortunate to have an accounting system that puts together the "puzzle pieces" of each month's reversals and reeboks to see the full picture, but herein lays the issue: a fancy accounting system should not be necessary to see what you are getting paid. Further, it is egregious to expect mineral owners to pay for a service such as EnergyLink, when instead they could undoubtedly be provided this same information from the operator in excel format.

Additionally, Dorchester supports the amendment to Section 38-08-06.3 requiring an operator to keep its contact information current with the NDIC, as well as the associated penalty for non-compliance. Through my experience in dealing with operators, unfortunately, the general trend seems to be that operators are not concerned with compliance unless a penalty is associated with non-compliance.

Section 3: Amendment to Section 38-08-06.6

The creation of Section 38-08-06.6 as proposed is particularly important for mineral owners to verify that their ownership in a well is being calculated and paid correctly. Currently, there are no requirements that operators provide this necessary information, nor are there any penalties if an operator fails to respond to these inquiries. Thus, there is no incentive for operators to be responsive, because they have no liability or accountability for failure to respond. And unfortunately, this seems to be the modus operandi. Recently, Dorchester inquired with an operator regarding several Division of Interest ("DOI") calculations contained on a composite Division Order which did not match Dorchester's understanding of

its ownership, as analyzed by various Professional Landmen. Despite sending several emails requesting assistance, the only response Dorchester received merely stated that the operator forwarded Dorchester's inquiry:


We have forwarded your inquiry to the respective geographical analyst to review and respond. If additional information is needed, the analyst assigned will be in contact with you. We are experiencing an increase in inquiries so your patience is appreciated.

Should you have any further questions, please visit our new ASSISTANCE FOR OWNERS SITE

Sincerely,

However, nearly five months after this reply, despite sending several more emails, Dorchester still had yet to receive a substantive response from the operator. In fact, the only reason this issue was resolved (after more than nine months), was due to an unrelated mineral interest (located in a different state) for which the operator needed Dorchester's consent to assign a lease. Over the course of nine months, no progress was made in what Dorchester can only assume was the operator's error in calculating the DOI—Dorchester still has not been told why the DOI calculations had severely decreased Dorchester's interest. Unfortunately, this is not a single occurrence. This is a common issue, for which there is no redress under the current statute. The creation of Section 38-08-06.6 as proposed in this bill will provide much needed protection for the common mineral owner who does not have the added protection of an unrelated mineral interest to force an operator to fix an issue that is solely within their power to control and is their fault to begin with. This is why the creation of Section 38-08-06.6 is so important, particularly the penalty provision, without which leaves little incentive for operators to comply with the statute.

Section 4: Amendment to Section 47-16-39.1:

The proposed amendments to Section 47-16-39.1 seek to redress multiple issues with the current language of the statute. The first of which is the exclusion of Overriding Royalty Interest ("override") owners in the protections allotted by this statute, namely, the right to receive interest on wrongly withheld royalty payments. Currently, the case *Sunbehm Gas, Inc. v. Equinor Energy, LP,* No. 1:19-CV-94, 2020 WL 2025355 (D.N.D. Apr. 27, 2020) stands for the proposition that Section 47-16-39.1 does not apply to the holder of an override. But I implore you to ask yourself, why override owners are excluded from this

same protection allotted to royalty owners? Yes, an override is different from a royalty interest because it is carved out of a lease rather than the mineral estate directly. However, an override, just like a royalty interest, is paid to the owner directly by the operator/payor and in the same manner as a royalty. Why then can an operator hold onto the override owner's "royalty" interest free for years upon years but not a royalty owner's? Dorchester has unfortunately run into this issue frequently. Most recently, an operator failed to make payments to Dorchester for approximately 10 years for no apparent reason, yet due to current case law of this statutory language, was not entitled to any interest for the wrongly withheld revenue. As you can imagine, such interest *would* have amounted to tens of thousands of dollars. Although an override stems from a different part of the minerals estate than a royalty interest, there is no logical reason why an override owner should be excluded from receiving interest on late payments that have been wrongfully withheld by the operator/payor.

The second issue this amendment accomplishes is providing much needed clarity regarding what the applicable statute of limitations is for interest on late royalty payments. Recently, Dorchester commenced an action against an operator for failure to pay interest on late royalty payments. The operator argued that the applicable statute of limitations is 3 years, but if not, then it is 6 years from the time that the royalty payment was ***due***, not when the (late) royalty payment was actually paid. The Court's opined that a determination regarding which statute of limitations applied was unnecessary because Dorchester's claims were not barred under either. However, the applicable statute of limitations for the time in which a royalty owner has to bring suit should be known. It should not be a guessing game for the mineral owner, much less the judiciary branch. This simple amendment stating that "a claim for relief for compensation brought under this chapter must be commenced within the limitations period provided under Section 28-01-15" will provide much needed clarity to mineral owners and alleviate the need for a judicial determination as to which limitations period applies.

The third issue this amendment seeks to address is the outright refusal and denial by operators that interest on late royalty payments are due upon rendering the late royalty payment. This is a very common

issue that Dorchester faces. Despite the clear statutory language mandating the payment of interest on late royalty payments—"*without the requirement of needing to request the interest"*—even upon such request, operators/payors will flat out refuse to pay interest. Another common argument operators/payors will employ is that the statute of limitations for interest begins to run when the late royalty payment was ***missed*** (rather than when it was actually paid). This means that if a royalty owner gets paid 10 years late, the royalty owner would have lost all claims to interest, ***before they even receive the late royalty payments***. This is great for operators/payors because they can avoid liability for interest on late royalty payments by merely waiting until after the limitations period has run out, and just like magic, they have absolved themselves from any liability for their own malice.

As you can see, due to operators blatant disregard for the statutory mandate of interest on late royalty payments, as well as the confusion regarding when the statute of limitations begins to accrue and for how long it continues, the suggested amendments to Section 47.16.39.1 are necessary in affording minerals owners the intended protections of this statute.

Section 5: Amendment to Section 47-16-39.2:

The proposed amendments to Section 47-16-39.2 are needed in order to resolve multiple issues that have in essence defeated the intent of this statute. The intent of 47-16-39.2 was undoubtedly to protect mineral owners by forcing operators to provide transparency through mandatory audits. However, the statute fails to provide the protection for which it was created due to several issues.

The first issue is that the current language does not allow an unleased owner to inspect the production and payment records of the operator/payor. The proposed amendment would provide unleased mineral owners with the same rights as a leased mineral owner under this statute. This amendment is justified because unleased mineral owners are entitled to a statutory royalty under the North Dakota Century Code, yet with the statute as written, have no right to audit the records to ensure they are being paid correctly. The proposed amendments will eliminate an operator's/payor's ability to refuse audits merely

because the mineral owner is unleased. Regardless of whether a mineral owner is leased or not, if they are receiving royalties from the operator, then the right to audit is essential to providing the transparency and protection this statute intended to provide.

Second, the current language has created uncertainty regarding whom the lessor can audit. Operators have claimed that the statute as currently written only allows the mineral owner to audit its lessee. This interpretation is especially problematic. What happens when the operator, who is responsible for paying your royalties, is not your lessee? You have no recourse available to audit their records, even though they are paying your royalties. Dorchester has encountered this issue on more than one occasion. Below is an excerpt of a response to Dorchester's demand to audit the operator's records. Even though Dorchester was leased, the current statutory language provided a loophole through which the operator was able to avoid the audit requirement, merely because the operator was not Dorchester's lessee:

> [illegible] party to the contract. No statute or law in North Dakota provides a royalty owner with a right to audit the records of a well operator in the absence of a lease or other contractual arrangement that establishes that right. That said, your client's monthly royalty statements from Petro-Hunt

As you can see, the intent of the statute has been completely circumvented, thus rendering this statute essentially useless.

The final issue with this section is that the audit procedure is unduly burdensome because it requires the mineral owner to go to the physical location and look through the documents. Especially when the documents are already in a digital format. Companies routinely use this as a means to discourage audits. Thus, the requirement to provide the electronic versions, when available, is a crucial amendment.

In summary, Dorchester supports House Bill 1520 for the reasons previously stated. Thank you for the opportunity to testify before you today.