

## Landowners and Leasing for Oil and Gas in Ohio

The process of drilling a well begins with a lease agreement between the producing company and one or more landowners who will make up a drilling unit. The unit can vary in size from one to forty or more acres depending on the depth of the proposed well.

As the prospective lessor, a landowner who is approached for a mineral rights lease must be aware of all the conditions of the lease that allows the producer to drill on his land. It's important to realize that once a lease is signed, a partnership is formed that may last for many years if oil and gas is found in paying quantities. Therefore, the landowner must have a certain level of confidence in the company that will drill and produce the well on his land. He must know that there will be an initial period of disruption to his property during the drilling, but a wisely executed lease agreement will protect him and the property during the life of the well.

### The Oil and Gas Lease

A lease is a legal document between the landowner (lessor) and an individual or company (lessee) that allows the company to drill and develop the oil and gas minerals beneath the property. A company representative or an independent landman will approach the landowner with a lease form and explain that they would like a lease agreement to explore for oil and gas. The lease may contain legal terms and because it is a legal contract, it should be carefully reviewed by the landowner or an attorney familiar with oil and gas leases if the landowner is uncertain as to any provision in the lease.

Most leases are standard in form and, at face value, tend to be weighted in favor of the lessee; however, many items in the agreement can be negotiated to the satisfaction of the lessor. Some of the main components of a lease are:

- **Cash bonus or spud fee** - A one-time payment paid upon signing the lease or prior to commencement of drilling the well.
- **Delay rental** - An annual payment made to the lessor usually on a per acre basis prior to a well being drilled.
- **Free gas** - An annual allocation of gas to the lessor for domestic heating purposes. This is commonly 200,000 cubic feet or more per year and goes to the person upon whose land the well is located.
- **Pooling or unitization** - A provision that allows the lessor's land to be combined with adjoining lands to form a drilling unit.
- **Primary or initial term** - The length of the lease in years, typically 2 years or more. The longer the term, the less likely a well will be drilled shortly after signing a lease.
- **Royalty** - The amount of production received by the lessor, usually one-eighth (12.5%) of the sales of oil and gas from the well. If there is more than one landowner in the drilling unit, the royalty is shared according to the amount of land each lessor has in the unit.
- **Secondary term** - The length of the lease after a well is drilled, usually for as long as the well produces in commercial quantity.



### ADDITIONAL INFORMATION

#### Frequently Asked Questions about Leasing and Drilling in Ohio

Requirements to Obtain an Owner  
Number--**Registration  
Requirements for New  
Domestic Owners (One Well  
Ownership)** pdf

### CONTACT INFORMATION

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- **Shut-in royalty** - Payment that is received in lieu of production royalty when the well cannot be produced due to production problems or other factors.
- **Termination** - End of the lease due to expiration of the primary term or when commercial production ceases and the well is plugged.

The prospective lessor should consider the following before signing a lease agreement:

- If the lessee is an independent landman, ask what he intends to do with your lease. Independent lease people will assign your lease to a producing company that you will have no contact with until the lease has been assigned. Check the references of the producing company. Do they have producing wells in your area? What is the company's violation/enforcement history with the Division of Mineral Resources Management?
- Request references from landowners the company has drilled wells on. Check them out. These references can give a good idea of what to expect from the company's practices and operations.
- Check with neighbors to see if they have been contacted and presented with similar proposals. Are there other leasing opportunities from different companies operating in your area?
- Discuss the lease payment. If the area is actively being drilled, a higher rental payment and/or spud fee is a reasonable request. The payment will hold the lease until a producing well is drilled at which time the lease is held by production until production ceases.
- Discuss the term of the lease. Ask when the company intends to drill. If you want a well drilled soon, insist on a shorter term. If the lease expires and no drilling is in progress, make sure that no automatic extension exists in the lease. If a lease renewal is proposed, it may be better to renegotiate a new lease.
- Discuss damage settlement in the event that crops, fences, trees or other assets on your property have to be removed to drill a well. Incorporate the settlement into the lease agreement.
- Discuss where the well, storage tanks, access roads and pipelines will be placed. Some well locations may be site specific for geologic reasons, but the other items should be subject to landowner approval. Pipelines should be buried below plow depth where practical and should be limited to one line per well. Any pipeline brought onto the property from adjoining lands should be negotiated in a separate pipeline right-of-way agreement. A location approval clause should be incorporated into the lease agreement.
- Ask about directional drilling and if it is planned for this lease. If it is, you may want to restrict it without additional approval.
- Discuss the "free gas" provision. If the lessor's annual usage exceeds the amount specified in the lease, the lessor should be able to purchase additional gas at the current wellhead price. The lessor may have to furnish the line and other equipment to get the gas from the well to the home and may be responsible for hiring a professional contractor to safely connect the gas into the house.
- If the lease contains a pooling clause, request a limit on the total acreage to be pooled. Remember that the landowner royalty in a shared unit is based on the ratio of lessor land in the unit to the total land in the unit. If only a small portion of lessor land is in a producing unit, the balance of the leased land is held by production even though only that small portion is receiving royalty from the well.
- Discuss a development clause. This compels the company to fully utilize all available acreage into drilling units and maximizes the royalty return to the landowner. Any leased land not developed within a reasonable time would revert back to the landowner.
- In addition to oil and natural gas extraction, some leases contain a storage provision that allows the company to inject gas from off the lease into the well. Brine disposal clauses are also present in some leases. An oil and gas lease is for extraction of the resource and any references to storage or disposal should be eliminated.
- Discuss the disposition of the well after commercial production stops. Although the well may no longer be economically viable, there may be years of domestic supply remaining. Commercial productivity and economic viability should be clearly defined to prevent maintaining lease validity by only producing a

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minimum amount of oil and/or gas. A landowner should consider assuming ownership of his well if a continuing source of domestic gas is desirable. Once ownership is assumed, the landowner becomes liable for plugging the well when it becomes incapable of production.

During lease negotiations, remember you were the one who was approached for the lease. There is no obligation or hurry to sign even though the lease person may try to instill a sense of urgency to do so. Once the terms and conditions of the lease are negotiated to the satisfaction of the landowner, the lease can be witnessed, signed, notarized and recorded. The lessor should request a notarized copy of the lease and keep it in a safe and handy place.