

The three Baker heirs – a doctor, an investor and a former university executive – all had moved away from Southwest Virginia but have several advantages most royalty owners do not enjoy.

Bill Baker, the original heir to his father's estate, was an engineer and kept detailed records of the family holdings. He became friends with Bartlett, a longtime geology professor at Emory & Henry College who agreed to look after the estate following Baker's death. Bartlett testified as an expert for Glubiak during the Harrison-Wyatt case.

"We were fortunate enough to have Dr. Bartlett's assistance," Betty Anne Cox, one of the heirs, said by phone. "All of my generation were living away," said Cox, who lives in Hartford, Conn., and retired as the director of external affairs for Trinity College.

"It was very good to have somebody who was both knowledgeable and who we trusted and who knew all the players," she said.

Even so, their struggle did not end with Brillhart's 2004 letter that waived a claim to all coalbed methane royalties.

In late 2007, tiring of requesting royalties in piecemeal fashion, Bartlett asked Pine Mountain, which had since been acquired by Range Resources, to authorize a "complete release for these wells and any other remaining wells that may be drilled in the future on this same tract."

Bartlett said that when he approached Jerry Grantham, a vice president at Range Resources, to ask him to waive his claim, Grantham offered to split the royalties, giving 75 percent to the Bakers.

Grantham, who is also president of the Virginia Oil and Gas Association, declined to comment on a private contract, but said his company found such a split "to be a pretty effective agreement in trying to get money out of escrow, benefiting all parties involved."

In a March 7, 2008, letter, Range Resources registered a change in its approach toward the Baker heirs. Grantham wrote that the company would waive its claim for certain wells if the heirs signed a confidentiality agreement.

The Baker heirs retained Glubiak to help them collect money from escrow, and on March 19, 2008, Glubiak wrote to Grantham with a 10-day ultimatum.

"We have no intention of signing any confidentiality agreement," he wrote. "In the alternative, I have been authorized to pursue a declaratory judgment action in Dickenson County pursuant to the Harrison-Wyatt case, and I feel confident of a successful result."

The company agreed, and the Baker heirs began receiving their royalty payments, Cox said.

But at the time of Glubiak's letter, the Harrison-Wyatt case was quickly losing currency as a decisive precedent on coalbed methane ownership.

**Coming Wednesday:** *A coal company fights back.*

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*Editor's Note: This article was corrected on Dec. 10, 2009.*

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[Flag Comment](#) Posted by Ken on December 08, 2009 at 6:49 pm

I have 100 acres in Harmon, VA. and a contract with CNX for a gas well and road. I was not pleased with the agreement and understood there was no recourse. Now I know why.

The VA. government sides with business in the appalachan mountains as did all levels of government side with coal mine owners during the coal mine wars and battle of Blair Mountain...Ken Barlow

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## Coal companies block efforts to access natural gas royalties



DAVID CRIGGER/BRISTOL HERALD COURIER

Mike and Ferrell Whited look over paperwork concerning gas wells on their property near Swords Creek, Va.

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By [Daniel Gilbert](#) | Reporter / Bristol Herald Courier

Published: December 9, 2009

Updated: December 9, 2009

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On an early November day, Michael Whited, mounted on an all-terrain vehicle, checked the meter at a highly productive well named AY-112. Coalbed methane was flowing out of the ground and into a pipeline at the rate of 176,000 cubic feet a day – enough gas to satisfy the heating and cooking needs of the average American home for almost two years.

“I just check it to see how much they’re ripping us off,” Whited said.

Since 2001, 14 wells on the Whited land have produced 4.4 billion cubic feet of coalbed methane. That volume would generate about \$30 million in gross proceeds for the gas operator, based on historical monthly averages of natural gas prices for two major interstate pipelines in the region.

As the owners of the surface land and the gases beneath it, the Whiteds are entitled to a one-eighth sliver of the proceeds from coalbed methane drained from their property. But because they do not own the coal, the Virginia Gas and Oil Board ordered that their royalties be placed into an escrow fund until the ownership of coalbed methane could be decided.

In the spring of 2004, the Supreme Court of Virginia issued a decision that spread like wildfire among mineral owners in Southwest Virginia, upholding a lower court ruling that a surface owner who sold only the coal from his property retained rights to all of the coalbed methane. The ruling in *Harrison-Wyatt v. Ratliff* buoyed landowners like the Whiteds, who had stood by empty-handed as gas companies drained their coalbed methane.

Earl Whited, the family patriarch who started out as a school bus driver, knew he had a claim to at least several hundred thousand dollars in escrow. In 2005, he retained Peter Glubiak, the attorney who had won for the Buchanan County surface owner in the *Harrison-Wyatt* case.

Glubiak had spent four years litigating the ownership of coalbed methane, and armed with the high court’s ruling, he figured getting the Whiteds’ royalties out of escrow would be smooth sailing.

But it didn’t turn out that way.

### **A trial of each tract**

The large amount of royalties at stake had made it possible for Earl Whited to hire Glubiak, who worked on a contingency basis and charged a percentage of whatever his client recovered from escrow. But it also stirred a vigorous defense from another party – the company that owned the coal beneath the Whited land, who asserted a right to the coalbed methane royalties in spite of the *Harrison-Wyatt* ruling.

From the outset, Buckhorn Coal Co. made it clear it would not respect the Supreme Court’s ruling that a surface owner who sells only the coal retains rights to the coalbed methane.

“We think it’s a bad decision,” Charles Hart, managing partner of Tazewell, Va.-based Buckhorn, said in a phone interview. “You have to defend your interests. You can’t just roll over and say, ‘Here it is.’ ”

The defense went like this, as argued by Buckhorn’s lead counsel, Eric Whitesell: Coalbed methane ownership “can be reached only after a trial of the title of each tract” of land.

With that, Buckhorn heaved the burden of proving ownership squarely onto the Whiteds.

The plaintiffs, Buckhorn claimed, failed to identify the exact location of the boundaries where they claimed mineral interests. They failed to include a survey. They failed to name other parties who might have mineral interests in the same drilling units. They got the names wrong on the pleadings.

Complicating the plaintiffs' case was that Earl Whited died early on in the litigation, in October 2006, and left his estate – and his active lawsuit – to his six children. Discord broke out among the heirs, and the two who had been designated executors ceded their authority to a professional administrator, Ralph Snead.

In a June 2007 letter briefing Snead on the case, Glubiak wrote, “We have been battling Buckhorn Coal over what proved to be extremely complex title issues, as well as boundary and ownership issues.”

A year later, with Buckhorn promising an appeal to the state Supreme Court if it lost, Snead presented the Whited heirs with three options: Pay \$12,000 out of pocket for a survey and title opinion; negotiate with Buckhorn to split royalties; or none of the above, and Glubiak would withdraw from the case.

The heirs balked at the fee for additional title work, but could not agree on how to proceed. Snead, as administrator of the estate, unilaterally decided to authorize Glubiak to negotiate a split agreement.

### **Coal goes on the offensive**

Buckhorn Coal has never won 100 percent of coalbed methane royalties, and Charles Hart never expected to in the Whited case.

“When there’s a conflict, we will split the royalties 50-50,” he said. “We like to do that, because once it gets into that escrow account, if nobody pushes the issue, you’ll never get any money.”

“Fifty percent is better than nothing,” he said.

And Hart is adamant that the Supreme Court got it wrong in the Harrison-Wyatt case.

J. Scott Sexton, a Roanoke, Va., lawyer, represented the losing coal owner, Harrison-Wyatt, in that case. Asked recently whether he thought the Supreme Court’s ruling resolved the ownership of coalbed methane, Sexton reflected, carefully parsing his words.

“The Harrison-Wyatt decision established the law in Virginia that a coal owner claiming title under an unambiguous coal-only deed does not own the coalbed methane,” he said.

In plain language, when a surface and gas owner sells only coal, the coal does not include coalbed methane; the surface owner keeps that. But that decision has come under increasing assault – in and out of court – by coal owners in the years since the courts ruled on coalbed methane ownership.

Coal owners routinely propose royalty split agreements they tout as “the most economical and expedient way” to collect money from escrow, according to split agreements reviewed by the *Bristol Herald Courier*.

Some outright deny the Supreme Court’s ruling in Harrison-Wyatt.

In November 2008, one coal owner wrote to Jimmy Smith, of Coeburn, Va., and proposed to split royalties: “The Commonwealth of Virginia has not made a judicial determination of ownership of

coalbed methane.”

The offer was signed by John Mooney, vice president and regional manager for NRP Operating LLC, a subsidiary of Houston-based Natural Resource Partners LP, which earned gross revenues of \$292 million in 2008 – including \$8 million in gas and oil royalties, according to its financial filings. Mooney did not respond to phone or e-mail messages seeking comment.

Glubiak, in representing various clients’ mineral interests, has encountered this assault firsthand.

“It’s my contention that the coal industry decided that if they put up a united front, then they can scare people off and into doing these godforsaken split agreements,” he said. “Most people say, ‘I can’t pay some lawyer \$50,000 to fight my case with you.’ There are millions of dollars at stake, and [coal companies] used this as a bludgeon to beat up people and threaten what they’re going to do.”

As for the argument that the Harrison-Wyatt decision is limited to the deeds in one case, Glubiak said, “I will defend to my dying breath [against] this crap that’s going on now that it’s only a Buchanan County case. If the severance deed says ‘coal only,’ the surface owner wins; the surface owner owns the gas.”

### **The split**

By 2008, Glubiak was pursuing for the Whites the very type of agreement he abhors – a 50-50 split – and four of the heirs retained another law firm to halt the negotiation. They spent \$7,500 before eventually, in February 2009, endorsing the split.

The upshot is this: The White heirs will receive 50 percent of the royalties in escrow, minus 30 percent for the services of Glubiak and Snead. After that payout, the Whites and Buckhorn evenly will split the one-eighth royalty. As of October, Snead had collected more than \$300,000 from escrow to distribute among Glubiak, the Whites and himself.

“We didn’t really have much choice, I don’t guess you’d say,” Cathy Ward, a White heir who favored the split agreement, said in an interview. “When you’re up against these big companies, you’re not going to win. You don’t have much of a chance. I knew the way Buckhorn was dragging it out in court, they was just going to keep fighting us.”

Ferrell White, a disabled coal miner and the oldest of the heirs, is still angry about the split.

“Glubiak sold us out. And the judge. They sold us out. And our administrator – they sold us out.”

Glubiak and Snead, for their part, contend they did their all for the Whites – a difficult, conflictive group of clients, they said, and that the unhappy result is a reflection of the extraordinarily complex requirements of collecting royalties from escrow. The Whites still will receive many thousands of dollars each in royalties, they pointed out.

“It is a lousy system,” Glubiak mused. “Could they have done a split at the beginning? I don’t know, maybe, maybe not.”

Turning to Buckhorn and the coal industry, Glubiak said, “You know what the most embarrassing part of this is? They beat me.”

After four years of absorbing the costs of the litigation, Glubiak said, “I just couldn’t do it anymore. I

just gave up.”

This, he acknowledged, handed the industry “tremendous support emotionally and legally” in its fight for coalbed methane royalties.

The split agreement did not settle everything for the Whites. They still have interests in other coalbed methane wells, and the Virginia Gas and Oil Board is funneling those royalties into escrow. None of the heirs seemed willing to go through another lawsuit, or to split them with Buckhorn.

Said Ferrell Whited: “We’ll just sit back and let the escrow build and just will it to our grandkids.”

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*Coming Thursday: Who knew that the escrow fund was losing money?*

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[Flag Comment](#) Posted by Heather Provencher on December 10, 2009 at 1:19 pm

**\*\* The following comment was emailed to TriCities.com from a reader \*\***

I too, like many other ancestors of the Tiller clan, have a very small interest and share of the royalties involved. However, we do live in America and I believe our rights are being trampled on by the gas companies and unfortunately by the state of Virginia. It appears the only course we can pursue is through your articles, which is bringing this injustice to light. Keep up the good work.

~ Mason Tiller

Flag Comment Posted by BP on December 09, 2009 at 3:09 pm

Profit over people. Profiteers over people. Government at every level has abandoned “We, the People. . .” to serve the will of corporations. Demonstrated with compelling clarity in this article.

Flag Comment Posted by LillLudkowski on December 09, 2009 at 2:13 pm

My father also refused to sign an agreement with Equitable. He told them to go around his land, but they went ahead and destroyed our ancestral property located at Priest Fork in Dickenson County. Roads were bulldozed, large numbers of trees were cut down and left for us to clean up, and no remuneration for damages has of yet been forthcoming. When my father became too ill to make legal decisions for himself, I assumed the position of his power of attorney. I attempted to collect back compensation from Equitable for damages, but they offered to settle for a pittance, and in return they expected me to sign away my father’s rights, my rights, and the rights of any and all descendants into perpetuity. Yet, I still pay the taxes on the property, but my family is made to feel like trespassers on our own land when we encounter anyone from the gas company on our property. I live in Chicago, so it is difficult to keep an eye on what Equitable is up to from 500 miles away. Although I no longer live in Dickenson County, my heart is still there, and I am incensed by the way the residents of SW Virginia continue to be abused and taken advantage of. Between the destruction of our beloved mountains by the coal companies, the methodical robbing and pillaging of our people and our land by the corporations, and the apathy of our elected officials and our court system, I worry about the future of the mountain way of life. Thank you, Mr. Gilbert, for writing such a well-researched and thought provoking series of articles. I hope they will make a difference.

Lillian Duty Ludkowski

Flag Comment Posted by lswark on December 09, 2009 at 1:45 pm

It’s Erin Broekovich all over again! How many times do we have to fight this battle before the Legislature takes action?

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## Natural gas escrow fund bleeding money



Greg Moore/WLSL

The Wachovia Bank branch, at 201 S. Jefferson St. in Roanoke, Va., has been the physical address of the Virginia Gas and Oil Board's escrow fund since 2006.

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By [Daniel Gilbert](#) | Reporter / Bristol Herald Courier

Published: December 10, 2009

Updated: December 10, 2009

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On the morning of Sept. 29, 2008, as the world woke up to unprecedented turmoil in financial markets,

the normally placid director of the state Division of Gas and Oil considered a worst-case scenario for the \$23 million escrow fund he administered.

The millions were compensation for Virginia landowners whose mineral rights the state had leased to private energy corporations, often against owners' will or without their knowledge. The money waited in escrow for safekeeping until the question of individual ownership could be resolved.

Suddenly, it seemed in jeopardy.

Managing the fund was Wachovia Bank, which by the fall of 2008 had been brought to its knees by its ill-fated acquisition of junk mortgages at the height of the housing bubble. With investor confidence plummeting, the Federal Deposit Insurance Corp. swooped in to facilitate an emergency sale of Wachovia to Citigroup early on Sept. 29.

At 9:06 a.m., DGO Director David Asbury e-mailed his contact at Wachovia and floated a question with a quivering parenthetical: "Under a worst case scenario, assuming Wachovia fails. . . what value (if any) would remain in the Escrow Account?"

It also occurred to Asbury, who had been in the job for just five months, to ask if each sub-account in the fund was FDIC-insured. The answer, it turned out, was that the entire \$23 million fund was insured for \$250,000.

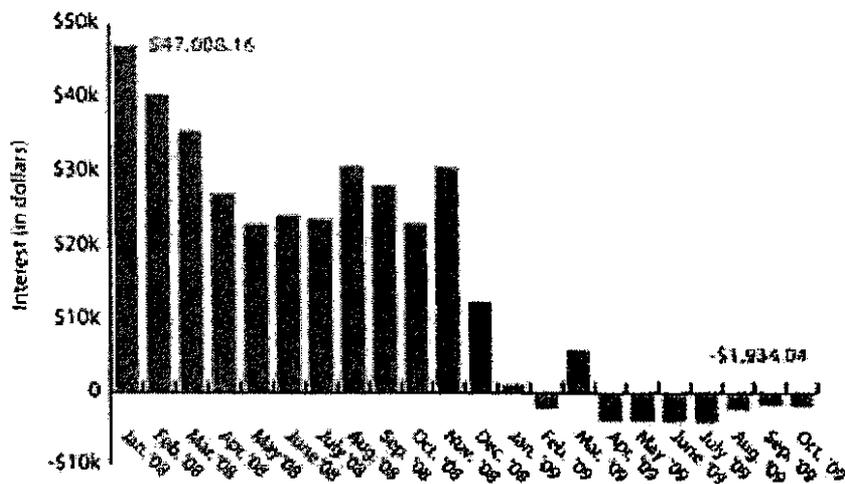
This particular financial drama unfolded out of the view of thousands of royalty owners, who receive no accounting of their funds in escrow. At the end of the tumultuous week, Wachovia was acquired by Wells Fargo, and the escrow fund did not lose value – at least not immediately.

What the episode reveals is how little members of the Virginia Gas and Oil Board – the state regulatory body with exclusive authority over the escrow fund – know about the fund's operations, leaving the details to Asbury, according to interviews, hundreds of pages of board hearing transcripts and internal correspondence obtained by the *Bristol Herald Courier* through a Freedom of Information Act request.

Board members often lack seemingly important information, such as the interest the escrow fund is earning and how its deposits are insured. They do not receive monthly statements from the bank, and some were unaware – as recently as November, when they voted on awarding a new contract for escrow services – that the fund has been losing interest on its deposits for more than half a year.

### A Precipitous Fall

Wachovia's fees for managing the escrow fund have exceeded the amount of interest earned on the fund's deposits for most of 2009, resulting in a loss of almost \$17,000 for the first 10 months of the year.



### A precipitous fall

The man in charge of administering the escrow fund has a quiet, polite manner in person. He is responsive to media inquiries, but speaks only through e-mails; he declined interview requests for this story and others.

As director of the Division of Gas and Oil, David Asbury is also the “principal executive to the staff of the [Virginia Gas and Oil] Board” – a somewhat grand-sounding job title for a staff of just two. Asbury and Diane Davis, programs administrator for the DGO, are the only state employees who handle the escrow fund and the board’s records.

“He’s not a guy who goes home when the clock goes off,” Donnie Ratliff, a board member who represents coal interests and who worked with Asbury at Pittston Coal Co., where the director was an engineer, said in an interview. “There is no one more dedicated and conscientious than David.”

On Oct. 10, 2008, Wachovia representatives traveled to Abingdon, Va., to meet with Asbury at the Division of Gas and Oil’s former office there. After several tense weeks, the bank officials were eager, as one wrote, “to more broadly discuss our mutual relationship and services being provided.”

At the meeting, Wachovia recommended that the board shift its investment policy to a more conservative asset allocation.

Eleven days later, at the board’s October hearing, Asbury advised members to adopt the bank’s suggestion.

“We are giving up about a percent of earnings potential, but it is also reducing our risk to as close to zero risk as we can,” he said.

Bruce Prather, a consulting geologist who represents the gas and oil industry on the board, asked Asbury, “During the upheaval [ . . . ] did we lose any money?”

Asbury replied, "No, we did not."

But even as he spoke, the fund's interest income had begun to flat-line.

The escrow fund started off January 2008 by earning \$47,000 in interest. By October, interest had dropped by half to \$23,000.

Now, with the fund's more conservative investment mix, the interest income plunged – to \$1,170 in January, and into negative territory in February at a \$2,173 loss.

The reason for this, as a bank representative explained to the board six months later, was that interest rates were "very, very compressed" – so much so that the bank's servicing fees were higher than the interest that escrow deposits were earning.

It is unclear if any board members were aware of this when, in March 2009, they voted to extend Wachovia's contract through the end of the year. The evidence suggests that they were not.

At the board's June 16, 2009, hearing, Asbury presented members with the first-quarter report for the escrow fund, which had a net interest income of \$5,000 – \$118,000 less than what it netted over the same period the previous year.

The first-quarter report masked the worsening situation; by May, the escrow fund had experienced three months of income loss since the beginning of the year. But Asbury did not address this during the hearing, and board members asked no questions. The "investment risk assessment" on the docket was continued.

Two days later, on June 18, Asbury and Diane Davis traveled to Roanoke to discuss the escrow fund with the Wells Fargo-Wachovia investment team.

Late that night, Asbury sent an e-mail to Butch Lambert, chairman of the Gas and Oil Board, and copied Sharon Pigeon, the senior assistant attorney general who advises the board, on what he learned.

"Recent analysis of the Escrow reflects a significant decline in monthly interest income," Asbury e-mailed at 10:57 p.m.. "For the second time in the account's history, monthly expenses have exceeded monthly interest income."

In conclusion, Asbury wrote, "We were very pleased with today's focused but productive meeting and have a high level of confidence in the new Wells Fargo-Wachovia."

June would be the fourth month of the year that the escrow fund lost interest. But Asbury's e-mail was the first written acknowledgment to a board member of the negative income.

#### **"He handles this account"**

In July 2009, with the escrow balance now at nearly \$25 million, board members received the fund's second-quarter report from a Wachovia official, who broke the bad news this way.

"Income from investments and then netted from expenses of servicing the account were negative \$6,793," Patrick Dixon, a senior vice president for Wachovia, told the board.

Board members also learned that although the bank charged a service fee of \$8 per sub-account – nearly \$6,000 a month – the entire fund was FDIC-insured for only \$250,000. For the other \$24.5 million, Wachovia pledged collateral to a third-party trustee, the Bank of New York.

This was in fact a substantial improvement in the security of the fund, thanks to a February change adopted by the Treasury Board of Virginia to require banks holding more than \$250 million in public funds to pledge 100 percent collateral for every dollar not insured by the FDIC. As of September, Wachovia held \$487 million in public deposits, according to treasury records, making it the second-largest such holder in the state.

In September 2008, Wachovia had collateralized only half of the assets it held for the board.

“With the instability last fall, there was concern that possibly that requirement was not adequate,” Kristin Reiter, director of operations for the Virginia Department of Treasury, said in explaining the new regulation.

The escrow fund’s negative income, in particular, caught board members by surprise.

“Do you let somebody know when you think that we’re going to run a deficit on these costs?” Bruce Prather asked Dixon, the Wachovia vice president. “It’s rather a surprise to us that we find out we’re running in the deficit because we’ve got a lot of money in there.”

The ensuing discussion focused on whether to shift assets into a higher-earning combination; only one board member, Katie Dye, asked the bank if it was “negotiable” on the \$8 charge per account.

Dixon, noting that the board soon would solicit bids for a new contract to manage the escrow fund, said Wachovia would wait to negotiate until submitting a bid.

As the discussion wore on, Asbury’s central role in handling the fund emerged.

“See, we as a board, we never have access to the information that you’re talking about because it comes through David,” Prather said to the bank representatives. “In other words, he handles this account.”

Asbury defended the investment policy.

“I think the board made a smart decision last fall during turbulent times to place them in the very lowest-risk potential that there was,” he told board members. “And although we are showing negative income during the second quarter, I believe there is a potential to reverse that by the calendar year end.”

Seeking to staunch the bleeding, the board voted to move half of its funds invested in AAA-rated U.S. government obligations into a higher-earning Wachovia money market fund.

The escrow fund lost \$4,000 in July, and it has lost money every month since April, for a nearly \$17,000 loss for the first 10 months of the year.

Asked by a reporter about the losses that are eroding the fund’s value, Asbury noted that the fund has not lost its principal – meaning that royalty deposits from gas operators are still higher than the losses of interest income.

“The negative interest income for 2009 is disappointing but is a result of financial market conditions,”

Asbury e-mailed the newspaper. “Losses may have been worse but for the safe investment posture required for public accounts and adopted by the Board.”

Prather, asked the same question, said: “We’re trying to resolve that.” He would not elaborate.

Bill Harris, a public board member from Wise County, said it was “not a good situation to be in.”

It was worse than he knew.

When informed of the total losses so far this year, he said, “No, I was not aware we were losing like that.”

Neither was Donnie Ratliff, the board member who represents the coal industry and who was not present at the July 2009 meeting when Wachovia officials explained the negative income.

“I don’t see those numbers,” Ratliff said when asked at the Nov. 17 board hearing, hours before the board voted on awarding a new contract for escrow services. “I don’t know how that happened.”

At that meeting, board members had to choose between Wells Fargo-Wachovia or First Bank & Trust, an Abingdon-based bank.

An evaluation team of five state employees – including Asbury and Diane Davis – ranked Wachovia higher in every category. First Bank, though, offered less expensive services.

The board voted to award the contract to First Bank, beginning in January.

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*Coming Friday: What’s missing from the escrow fund?*

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It would be nice, just one time, to see one of these "BIG" companies... do the right thing!  
Barry Tiller

[Flag Comment](#) Posted by oldman on December 10, 2009 at 2:16 pm

They learned how to rob you from how they rob the Veterans with the Agent Orange Trust Fund set up for Veterans.

They will transfer the fund around and change the rules over and over all the while stealing all they can then passing it along to another thief. Then they will offer all those with claims a settlement which will be pennys.

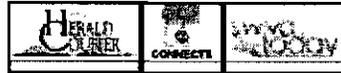
[Flag Comment](#) Posted by iwrose on December 10, 2009 at 11:50 am

as a landowner who has a gas well drawing gas from family property for over 20 years with no royalties paid. ill say that the gas companies can do just about anything they want to.they have about the same attitude as pittston did back in the early days.

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## Underfoot, Out of Reach, Part Six: Where are the gas royalties?



David Crigger|Bristol Herald Courier

Denny Sutherland visits one of the natural gas wells on his property near Birchleaf, Va.

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By [Daniel Gilbert](#) | Reporter / Bristol Herald Courier

Published: December 11, 2009

Updated: December 14, 2009

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In one 80-acre square in Buchanan County, a gas company sucked up 1.6 billion cubic feet of coalbed methane gas in 2½ years – enough to satisfy the heating and cooking needs of about 18,000 homes for a year.

Some of the gas in that unit – dubbed W-8 by state regulators – is the property of owners who are not getting paid for it, including Buchanan County, which owns 14 acres. The producer, CNX Gas Co., should have been making royalty payments into a state-run escrow fund for those owners.

For 2½ years, it didn't.

In March 2008, CNX discovered it never filed the necessary paperwork with the state Division of Gas and Oil to escrow royalties. Two months later, the company deposited more than \$861,000 into the escrow sub-account for W-8, making it the largest account in the \$24 million fund.

The W-8 case points to a significant regulatory gap, one in which the state agency overseeing the escrow fund didn't notice nearly a million dollars missing from an operator for years.

The company caught its own error. But W-8, it turns out, is not an isolated case.

The *Bristol Herald Courier* compared monthly gas production in units like W-8 that should generate payments into escrow with actual payments into escrow from January 2008 through June 2009. The analysis revealed that about one-third of the 750-plus active sub-accounts in escrow received no deposits for the months when the corresponding wells produced gas. Of those, nearly 100 sub-accounts received no deposits for all 18 months.

The Division of Gas and Oil has offered a series of evolving explanations in response to the *Herald Courier's* analysis. Initially, the DGO posited on Nov. 6 that the discrepancies were the result of changes in the status of a well, such as when a coalbed methane well is swallowed up into a larger unit and owners begin receiving royalties in a separate escrow account. Or, the DGO suggested, gas companies were waiting to pay royalties until they reached a \$1 threshold.

When presented with specific examples of escrow sub-accounts with very low balances – from 12 cents to \$2.30 – despite high production from corresponding wells, the DGO responded that they were reasonable given the small amount of acreage subject to escrow. That explanation, however, ignored the fact that in several of the cases, no royalties were escrowed because the necessary paperwork has never been filed.

When presented with specific examples of missing paperwork, the DGO's parent agency, the Department of Mines, Minerals and Energy, issued a statement Nov. 16 that it "has been aware of the discrepancies between reported production and deposits to the escrow account" and "has taken a number of steps to fix the problems. Your questions have been addressed to DMME in the middle of this work."

The statement also acknowledged that DMME has been aware of a "backlog" of incomplete board files since "early 2009," and declared that the agency has assigned additional staff to clear it, as well as review individual account information. These incomplete files raise questions about how much money is missing from the escrow fund, as well as the DGO's ability, at current staffing levels, to ensure that gas companies comply with the governing law and regulations.

There are also uncertain implications for sub-accounts in escrow that should be receiving royalty

payments but are not, landing awkwardly at the intersection of the Virginia Gas and Oil Act and the Uniform Disposition of Unclaimed Property Act. In all, 190 sub-accounts in escrow received no royalty payments for the entire 18-month period, which makes their combined contents of \$3.8 million look like unclaimed property, ripe for the Virginia Department of Treasury to seize.

Queried about how the DGO determines when funds in escrow are unclaimed property, its director, David Asbury, responded that royalties in an escrow sub-account would be considered abandoned “once active production payments stop and there is no evidence of activity for one year.” The DGO has no records of surrendering any funds to the state treasury.

In fact, the Treasury’s Unclaimed Property Division only recently became aware of the escrow fund, and division officials met with their DMME counterparts in October, a Treasury official said.

“We really haven’t made a determination. We’re still in discussions,” Vicki Bridgeman, the Unclaimed Property Division’s director, said in late November.

Any money seized from escrow would go into a state fund that provides low-interest loans to localities that build public schools and could be claimed, in theory, at any time by owners.

### **Missing for years**

What happens when a gas corporation authorized by the state to produce someone else’s gas fails to file the proper paperwork?

A 90-year-old woman whose family did not want her named is owed thousands of dollars but doesn’t get paid for four years.

The heirs of Ercil Cook check his balance in escrow and think they are entitled to 12 cents. And it’s impossible to know what happened to the mineral interests of Ducinia Stacy, of Grundy, Va.

Instead, the royalties that should go into the pockets of owners, or into escrow, stay parked in limbo within corporate accounts of gas operators.

Denny Sutherland knew he should be getting paid. He signed a lease, and he could read the gas meter on well V-505254 – a very hot well that drained as much as 26.5 million cubic feet a month – approximately enough to heat 10 households for about 30 years.

Four years passed, V-505254 drained half a billion cubic feet of gas, and Sutherland never received a check. Whenever he spoke with an agent of the gas operator, Equitable Production Co., he got a different answer.

Sutherland, a 63-year-old builder and ex-Marine who lives near Haysi, Va., wasn’t thinking of himself; he had very little acreage in the gas unit. But a 90-year-old relative of his in Bristol had a substantial interest.

“I knew if she didn’t get it pretty soon, she never would,” Sutherland said in an interview.

In July, Sutherland and a cousin visiting from New Mexico decided to get to the bottom of the issue.

Lois Wark, who retired as an assistant managing editor at *The Philadelphia Inquirer*, trekked to the

Division of Gas and Oil in Lebanon, Va., to inquire about the royalties. There, Diane Davis, one of two DGO employees who monitor Virginia Gas and Oil Board's records, discovered that Equitable had never filed a supplemental order – the crucial document that shows which owners in a gas unit have leased, and which should receive royalties in escrow.

Within the month, Denny Sutherland received a check for \$4,900; his 90-year-old relative received \$23,000. The royalty statements each received do not indicate whether the royalties earned interest, according to copies reviewed by the *Herald Courier*.

The system did not self-correct in the case of V-505254. It took someone who was expecting a payment to discover the error and push for answers. In the case of someone whose royalties are escrowed, no one is waiting for a check.

### **The board files**

The Division of Gas and Oil keeps a file for gas units in which the Virginia Gas and Oil Board has forced landowners to lease their mineral rights to a private energy company, a practice known as forced pooling. The files correspond to individual sub-accounts in escrow, and they contain the details that reveal which owners have royalties in escrow.

Anyone can examine the files, as long as they do so where a DGO staff member can see them.

In recent months, on the advice of its attorney, the DGO has zealously guarded its files, requiring anyone who wants to look at them to do so “where we can oversee the process,” a spokesman explained.

“It’s not a mistrust of anyone in particular,” said Mike Abbott, public relations manager for the Department of Mines, Minerals and Energy. “We’re the sole keeper of those files. These are the original copies of records, and we may not have duplicates.”

Abbott said he knew of no cases when documents had been taken or compromised. Actually, at least two files are missing.

The files for units Z-12 and V-12, both for wells in the Vansant area of Buchanan County, could not be located three months after the *Herald Courier* requested access to them. Neither unit received any deposits in escrow from January 2008 to June 2009; combined, their balances total almost \$690,000.

Davis, programs administrator at the DGO, said the files were not lost, but that she would recreate them by going to local courthouses and copying the orders that have been recorded there.

Occasionally, a board file contains a forlorn objection from a force-pooled owner, like the letter Ducinia Stacy wrote on July 6, 2004.

“I do not think the Gas Company should be allowed to just take people’s property (the gas rights) when they do not own them and the property owner does not want them to have them,” she wrote. “I don’t think this is right and I object for all the good it does me.”

It isn’t clear what happened to Stacy and other force-pooled owners in unit I-39 because the gas operator, CNX, has not submitted a supplemental order.

Gas operators are required to file this paperwork within two months of the board’s order giving a

company the right to produce gas belonging to force-pooled owners. Without a supplemental order, the escrow account for a unit cannot receive any royalties, and many contain only the initial “rental” payment of \$5 an acre for force-pooled owners.

“I’m unaware of any case where our system hasn’t caught up with [paying royalties] as it did in the W-8 instance,” said Cathy St. Clair, a CNX spokeswoman. “We’re convinced we’re paying royalty monies that are required on wells we drill into that state account, or into an internal suspense account awaiting transfer” to the escrow fund, she said.

In reviewing 12 board files for gas units with high percentages of owners who did not agree to lease, the *Herald Courier* identified six units operated by CNX that lacked supplemental orders. The combined balance of those units is less than \$250, even though the wells have been producing for at least four years.

St. Clair would not comment when presented with the unit names and identification numbers that lacked supplemental orders.

Two of these units show only one unknown owner, Ercil Cook, who has 1/100th of an acre in one tract, and 7/100ths of an acre in another. Over the six years that wells in these units have produced gas, Cook’s interest would entitle him or his heirs to about \$938, according to average monthly prices on the Columbia Gas Transmission, an interstate pipeline on which CNX moves gas.

The combined sub-accounts for Cook’s interest show 12 cents.

### Open questions

The *Herald Courier*’s analysis found 11 gas units in Dickenson County in which an unknown owner, the now-defunct Yellow Poplar Lumber Co., has rights to 100 percent of the gas underground. The wells on those units have produced 700 million cubic feet of gas since 2006, meaning substantial royalties should have been deposited into escrow.

Yet the sub-accounts in escrow received no deposits for a year and a half, and contained only the standard rental payment of \$5 per acre.

When presented with this information, Kevin West, managing director of external affairs for EQT, Equitable’s corporate parent, acknowledged that his company had failed to make required monthly payments into escrow, and pledged to deposit the correct amounts with interest.

With regard to the Yellow Poplar units, he said, “There are some situations which I can’t explain, you know, somebody made a mistake in the manner of making the instruction on things getting paid. Yellow Poplar could well have been one of those situations.”

The DGO already was aware of the Yellow Poplar discrepancies before fielding the *Herald Courier*’s questions, Director David Asbury responded.

“Staff expects the [ . . . ] subject issues to be resolved before year’s end,” he wrote.

In fact, the DGO was alerted to the Yellow Poplar issue more than a year ago. Catherine Jewell, a Bristol, Va., resident who has been a relentless critic of the Virginia Gas and Oil Board, e-mailed the DGO in November 2008, noting the low balances in several Yellow Poplar units.

She received no reply.

On Sept. 25, a Tazewell, Va., attorney named T. Shea Cook wrote a letter to Butch Lambert, chairman of the Virginia Gas and Oil Board, and copied several Southwest Virginia legislators. Cook attached an affidavit from Jewell, stating she had audited 24 gas units in which Yellow Poplar owned gas interests and estimating that the accounts were missing close to \$750,000.

“Your board has been charged with guarding these accounts and protecting the interests of the gas owners whose gas was essentially seized by the board,” Cook wrote. “These accounts need to be audited, and not just a checkbook audit.”

*Coming Saturday: In the past 10 years, the escrow balance has tripled – all without a single audit.*

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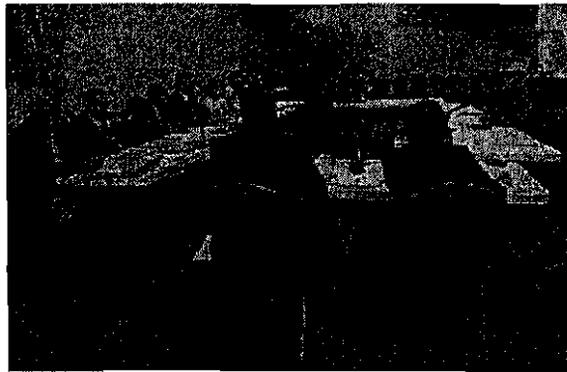
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## Underfoot, Out of Reach, Part Seven: An audit long delayed



Earl Neikirk|Bristol Herald Courier

Members of Virginia's Gas and Oil Board, shown in a public session, have clashed for a year over how thorough of an audit they wanted.

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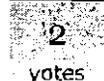
FOR MORE INFORMATION, including a database of accounts associated with wells, click [here](#).

By [Daniel Gilbert](#) | Reporter / Bristol Herald Courier

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Since 1999, energy companies have more than doubled the number of wells that drain natural gas in Southwest Virginia, producing 128 billion cubic feet of gas last year - a quantity that would fetch \$1.2 billion for gas producers at average regional prices for 2008.

As natural gas profits have soared, so has the balance of an obscure state-run escrow fund, which holds royalties belonging to thousands of landowners whose ownership is in dispute or whose whereabouts are unknown. In 10 years, the total funds in escrow have ballooned from \$3.6 million to more than \$24 million – all without a single audit to determine if energy companies are making the legally required deposits into escrow.

For the past year, members of the state regulatory board charged with overseeing the escrow fund have been locked in debate over how deeply to probe gas corporations' compliance with making royalty payments into the fund. Some on the board have called for a forensic audit, while another member strenuously objected that such an audit "will be opening a door that I do not think we want to or need to go through," according to interviews and internal communications obtained by the *Bristol Herald Courier* through a Freedom of Information Act request.

The documents shine a light on the board's private deliberations, and the deep division among members that discussion of an audit has provoked. They also reveal that board members actually voted to award a contract for an audit nine months ago.

On March 5, David Asbury, the main state official responsible for managing the Virginia Gas and Oil Board's business, announced to board members that they had voted 4-3 to hire a Colorado accountant to perform the audit. The accountant, Mary Ellen Denomy, came with a string of letters attached to her name, including abbreviations for "Certified Fraud Deterrent Analyst" and "Certified Forensic Financial Analyst." Her price tag for the audit: \$106,000.

At 11:57 a.m., Asbury e-mailed board members that they had selected Denomy and that all bidders would be notified of the board's decision that afternoon.

It never happened.

At 12:25 p.m., Sharon Pigeon, the senior assistant attorney general who advises the board, sent an urgent reply to Asbury, voicing a concern that he was about to take action "in an illegal closed session."

"Board action is not official until taken in an open meeting, so I assume you plan to call for a vote on this on the 17th," she wrote, referring to the board's hearing later in March. "I also assume there is reason to support the decision in the event there is a challenge to accepting the highest bid, so someone needs to be prepared to offer that information at the meeting."

Butch Lambert, the board chairman who Pigeon copied on her e-mail, responded at 1:06 p.m.

"Just so that we are above board with this, I think that we should follow Sharon's recommendation. We can do this first thing."

At the March 17 hearing, the board members went into a closed session to discuss the audit. When they re-emerged, public board member Mary Quillen moved to "drop those proposals that were received as not meeting the guidelines."

Bruce Prather, the board member who represents the gas and oil industry, seconded the motion, and the board voted to readvertise the contract.

### **“We’re not auditing it”**

Whenever gas companies make payments into escrow, they attach statements that show the volume of gas that a well produced, what it sold for and whatever deductions the company made in getting the gas to market. But bankers at Wachovia, which has managed the account since 2001, don’t look at these statements.

“I will tell you that the information is on there,” Patrick Dixon, a senior vice president for Wachovia, told Gas and Oil Board members at a July hearing. “We’re just not doing anything with that information. We’re not auditing it. We’re not in any way proving whether it’s right or wrong.”

It’s unclear how long board members knew they had access to this information; Asbury in April asked Wachovia for a “sample of the checks and the accounting that they receive [from gas operators] month over month,” which he said he provided to board members.

The last audit of the escrow fund was in 1999. It cost \$4,000. In their report, accountants at the Central Virginia firm of Robinson, Farmer, Cox Associates wrote that though they performed compliance tests with state laws and board regulations, “providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion.”

Asbury, in an e-mailed response to *Herald Courier* inquiries, wrote: “We balance the need to audit against the need to keep management fees charged to the account to a minimum.” Meaning: The people whose royalties are in escrow will foot the bill for any audit, not the agency in charge of ensuring the integrity of the fund.

Only two state employees are responsible for monitoring payments into about 950 sub-accounts in escrow – active and inactive – and ensuring that companies file the required paperwork: Asbury, the director of the Division of Gas and Oil, and Diane Davis, the DGO’s programs administrator.

Asbury said that the DGO’s parent agency is expanding its electronic reporting system with “automated quality checks” to include the escrow fund. Currently, the DGO has no such system in place.

Perhaps out of necessity, Asbury has outsourced part of his watchdog function to the companies he watches.

Asked if it was anyone’s job to review operators’ monthly accounting statements sent to Wachovia, Asbury sidestepped the question in a written response, noting that “major gas producers are publicly held companies” and that “payments into escrow [. . .] are internally and externally ‘audited’ transactions.”

The *Herald Courier*, in comparing escrow deposits with gas production during 2008 and 2009, found that hundreds of individual accounts did not receive royalty payments for months when the corresponding wells produced gas.

The analysis also revealed 20 duplicate sub-accounts that appear to receive payments from the same gas wells, underpayments and overpayments, accounts that should have been closed out years ago – and one account that was closed out, only to reappear months later with a negative 37 cents.

There is a cost to extraneous accounts: Wachovia charges \$8 per account each month. The bank's servicing fees have exceeded the amount of interest earned on the fund's deposits for most of 2009, resulting in a loss of nearly \$17,000 for the first 10 months of the year.

### Board divisions

On March 6, the day after Asbury notified board members the results of their votes on who would audit the escrow fund, an agitated Bruce Prather phoned the DGO director.

At 3:50 p.m., Asbury e-mailed Lambert about the conversation. "Board member Prather called and was upset about the pending decision for the [request for proposal] Escrow Audit," he wrote.

"Do you know what he is upset about?" Lambert replied.

"He had done research regarding the chosen candidate/proposal," Asbury wrote, referring to Mary Ellen Denomy, the Colorado CPA. "He has concerns about the candidate's testimony against certain gas companies and their interests out west in state court."

In his research, Prather may have seen a March 2007 article in the now-defunct *Rocky Mountain News*, in which western royalty owners christened Denomy "Erin Brockovich" – a reference to a tenacious woman who took on an energy giant in a pollution case and was lionized on the big screen by actress Julia Roberts.

When asked about his concerns in November, Prather said, "Me? I don't know where that came from." Asked if he denied making the comments Asbury referenced, Prather said, "I'm not saying anything."

In a phone interview, Denomy said, "There should be no reason for a company to feel threatened by an accountant. I'm trying to make sure monies are not being misappropriated. I'm just a bean-counter."

For a year, board members have clashed over how thorough of an audit they wanted.

In February, public member Peggy Barber, without having seen the bids from would-be auditors, informed Asbury, "I would like to choose the lowest bidder for this project as the end result should ultimately be the same." Barber, dean of workforce development and continuing education at Southwest Virginia Community College, did not return phone calls or an e-mail seeking comment.

Katie Dye, a public member from Buchanan County, has called for a "forensic audit," and Bill Harris, a public member from Wise County, has supported a more thorough audit.

On the other side, Mary Quillen, another public member, voiced a strong objection to auditing the financial records of gas operators. On Aug. 10, Quillen e-mailed Asbury with her comments on the pending escrow audit.

"I do not want this to be misinterpreted (sic) to mean we are going to audit each operators financial records," Quillen wrote. "This will be opening a door that I do not think we want to or need to go through. There are some on The Board and members of the public (regular attendees of the meetings) who will take this opportunity to jump on this as a means of addressing their own agendas."

Quillen, director of programs for the University of Virginia's Southwest Center in Abingdon, did not return phone messages or an e-mail seeking comment. When approached by a reporter during a break at