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IN THE DISTRICT UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF IDAHO

CITIZENS ALLIED FOR INTEGRITY AND ACCOUNTABILITY, INC,; CHARLENE QUADE and RACHEL HOLTRY Plaintiffs, v. THOMAS M. SCHULTZ, in his official capacity as Director of the Idaho Department of Lands; CHRIS BECK, MARGARET CHIPMAN, SID CELLAN, JIM CLASSEN and KEN SMITH, all in their official capacities as members of the Idaho Oil and Gas Conservation Commission Defendants.	CASE NO. 1:17-cv-264-BLW **PLAINTIFF'S BRIEF IN SUPPORT OF MOTION FOR SUMMARY JUDGMENT**

I. BACKGROUND

Plaintiffs challenge the recently redesigned Oil and Gas Conservation Act ("OGCA"), Idaho Code Title 47 Chapter 3, which provides a structure in which oil and gas exploration companies are

able to compel sales of mineral rights at commercially favorable rates, without rational basis. The OGCA itself fails to provide due process. The first public hearing under the new law compounded the due process failures when the hearing officer rejected relevant inquiry and evidence Plaintiffs sought to introduce regarding the value of their mineral rights, the risks associated with oil and gas exploration, and the reasonable rates of return that should be applied to their investments as well as that of applicant Alta Mesa, Inc.

Plaintiffs Char Quade ("Quade") and Rachael Holtry ("Holtry") own residential property in Fruitland, Idaho. On November 25, 2016, they were notified by mail that the mineral rights to their properties could be leased, without their consent, to Alta Mesa, Inc. Alta Mesa sought to develop the pool of hydrocarbons they believed to lie in a pool beneath Quade and Holtry's properties, as well as other properties in the area. Recently adopted Idaho law provides that mineral rights can be pooled and "integrated" to allow for exploration and development of resources. The integration can be forced, as it was for Quade and Holtry, but only after a hearing purporting to provide due process protection.

Plaintiff Citizens Allied for Integrity and Accountability ("CAIA") is a non-profit corporation that advocates for responsible fossil fuel development. Many of their members are concerned about the taking of their property rights without their consent or just compensation, as well as potential environmental impacts to their communities.

A hearing was held on December 14-15, 2016. As hydrocarbon development is new to Idaho, this was the first hearing under the new law. With little time to prepare, Plaintiffs were unable to secure counsel knowledgeable or experienced in oil and gas development but were, nonetheless, represented by counsel at the hearing. Plaintiff's counsel attempted to elicit relevant

testimony and introduce relevant documents concerning the value of Plaintiff's property and the oil and gas believed to lie beneath. Plaintiffs sought to elicit and introduce evidence that would establish just and reasonable rates of return on their investments in their real property, the rates of return that Alta Mesa anticipated on its investments in planned or potential well development, the risks to the Plaintiffs' property values, and how those risks related to the likely payments they might receive under the compelled leases.

Plaintiffs' counsel offered relevant evidence on several occasions which the Hearing Officer excluded. The Hearing Officer did not allow full cross examination of Alta Mesa's witnesses. On more than one occasion, their Hearing Officer herself testified. The Hearing Officer did not allow testimony concerning Plaintiffs' investments in their property, the financial risks involved in leasing the property, or how a reasonable rate of return could be calculated. No evidence was presented or allowed about the likely value of the minerals the Plaintiffs were being forced to sell, or the relative risks and rewards that might be experienced by property owners and/or Alta Mesa.

At the conclusion of the hearing the property was ordered integrated, forcing Plaintiffs Quade and Holtry to lease their valuable property rights, without their consent, for a payment that was fundamentally arbitrary as no evidence of actual value had been introduced.

The Hearing Officer's final order was appealed to the Oil and Gas Commission, which affirmed the Hearing Officer's decision. This action followed.

II. STANDARD OF REVIEW

The summary judgment standard is well-familiar to this Court: where a party moves for summary judgment, "[t]he judgment sought shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there

is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." F.R.C.P. 56(c). Where, as here, the party moving for summary judgment bears the burden of proof at trial, it must come forward with evidence which would entitle it to a directed verdict if the evidence went uncontroverted at trial. *Houghton v. South*, 965 F.2d 1532, 1536 (9th Cir. 1992), citing *International Short Stop, Inc. v. Rally's, Inc*., 939 F.2d 1257, 1264-65 (5th Cir. 1991); *Celotex Corp. v. Catrett*, 477 U.S. 317, 331 (1986) (Brennan, J. dissenting). Once the moving party meets its burden, the non-moving party must come forward with evidence refuting the moving party's case, i.e., submit evidence sufficient to create a genuine issue of material fact such that a reasonable trier of fact could find in the non-moving party's favor. *Bank Melli Iran v. Pahlavi*, 58 F.3d 1406, 1409 (9th Cir. 1995); *California Architectural Building Products v. Franciscan Ceramics*, 818 F.2d 1466, 1468 (9th Cir. 1987), citing *Celotex*, 477 U.S. at 323 and *Anderson v. Liberty Lobby*, 477 U.S. 242, 248-252 (1986). Applying these standards, the Ninth Circuit has had little difficulty granting summary judgment in favor of moving party plaintiffs or defendants who bore the burden of proof on issues and claims at trial. *United States v. Carter*, 906 F.2d 1375 (9th Cir. 1990); *Watts v. United States*, 703 F.2d 346 (9th Cir. 1983); *Bank Melli Iran*, 58 F.3d at 1413.

Also, where no genuine issue of material fact exist on the issue of liability, "[a] summary judgment, interlocutory in character, may be rendered on the issue of liability alone although there is a genuine issue as to the amount of damages." F.R.C.P. 56(c). Applying this provision, the Ninth Circuit has affirmed orders for partial summary judgment on liability issues, leaving damages issues for trial. *Pacific Fruit Express Co. v. Akron*, C. & Y.R. Co., 524 F.2d 1025, 1029-1030 (9th Cir. 1975).

III. UNDISPUTED MATERIAL FACTS

4. Brief in Support of Plaintiff's Motion for Summary Judgment

1. Plaintiff Holtry owns real property near Fruitland, Idaho. The property is in a small subdivision and is the home she shares with her young daughter. Deposition of Rachel Holtry, 54:5-10; Exhibit A, Declaration of Marty Durand in Support of Plaintiffs' Motion for Summary Judgment ("Holtry Deposition"). Holtry thoughtfully selected the lot on which she built her home. Holtry Deposition, 47:16-49:9. This is where she plans to live and raise her daughter. She carefully planned the location of the house for access to the park, open space behind and orientation to the sunset. Id. Holtry planned for several years and this home is a substantial investment which she and her daughter hope to enjoy for many decades. Id; Holtry Deposition, 55:12-14. "Everything about it I planned for a lifetime." Holtry Deposition, 49:4-5. If she had known of oil and gas drilling, she would have picked somewhere else. Holtry Deposition, 49:10-18.

2. Plaintiff Quade owns property nearby. She bought the residence as a home for her adult daughter. Deposition of Char Quade, 65:5-9; Declaration of Marty Durand in Support of Plaintiffs' Motion for Summary Judgment, Exhibit B ("Quade Deposition"). She rents the home to her daughter and her family, which includes young children. Quade Deposition, 65:19-25; 69:7-14; 70:22-71:1; 70:1-2; 70:18-21 The property was a significant investment. Quade Deposition, 77:5-7. Quade she had hoped to eventually sell the property to her daughter. Quade Deposition, 69:12-14. Quade's daughter and granddaughter suffer from respiratory ailments (Quade Deposition, 75:25-76:2) and they keep the windows closed and do not go outside as often as they would like due to the flaring from the well and concern with impacts on their health. Quade Deposition, 76:2-18. 104:17-105:1. Quade's daughter and her family have considered moving because of the drilling activity. Quade Deposition, 74:12-25-75:2. The assessed value of the property has declined in the past year. Quade Deposition, Exhibit 7.

5. Brief in Support of Plaintiff's Motion for Summary Judgment

3. Plaintiff CAIA is a grass roots, all volunteer, Idaho non-profit corporation active in protecting communities from irresponsible oil and gas development. Deposition of Shelly Brock, 16:1-4; 36:2-8; Exhibit C, Declaration of Marty Durand in Support of Plaintiffs' Motion for Summary Judgment ("Brock Deposition") CAIA members have testified at the legislature and have sought to provide accurate information to the public, elected officials and affected land owners, regarding the history, methods, and risks and benefits of oil and gas extraction. Brock Deposition, 101:16-102:23. CAIA has informed local officials and has been involved in amending local laws to better protect citizens and the environment. Brock Deposition, 44:9-25. CAIA has participated in administrative rulemaking. Brock Deposition, 103:2-8.

4. CAIA was formerly allowed to intervene in administrative proceedings on behalf of property owners. However, Idaho law was changed in 2016 to restrict those who could object to only affected property owners. Brock Deposition, 51:17-21. As a result, CAIA's membership has decreased. Brock Deposition, 84:19-85:13, 89:8-15. The 2016 law also restricted CAIA's access to information and records. Brock Deposition, 91:4-14. Holtry and Quade are both members of CAIA. Holtry Deposition, 20:24-21:3; Quade Deposition, 116:3-11.

5. Holtry and Quade were each contacted by Alta Mesa about leasing the mineral rights to their properties: Holtry Deposition, 28:13-16; Quade Deposition, 34:15-22. Holtry investigated and determined that she had no interest in leasing hers and did not respond to Alta Mesa's further inquiries. Holtry Deposition, 28:19-30:6. Quade also had no interest in leasing her mineral rights at the time and she did not respond to a letter from Alta Mesa. Quade Deposition, 34:15-22; Transcript of Hearing Before the Idaho Department of Lands, December 14-15, 2016 271:15-20, Exhibit D, Declaration of James Piotrowski in Support of Plaintiffs' Motion for Summary Judgment

("Hearing")

6. In late November, 2016, Holtry and Quade each received a large mailing from Alta Mesa, consisting of several hundred pages of documents with huge sections of information redacted. Holtry Deposition, 22:20-25; Quade Deposition, 29:14-30:13. The mailing (Holtry Deposition, Exhibit 4) was confusing (Holtry Deposition, 25:19-21) and difficult to understand (Quade Deposition, 27:21-28:5). Quade, an attorney, researched the Application in the mailing and wanted to contact other affected property owners. However, pages and pages of property owner names were redacted from the copy she received. Quade Deposition, 30:6-13. As she was not able to contact anyone directly, she reached out to CAIA and planned a community meeting to discuss what was happening and what people could do. Quade Deposition, 37:3-24. A representative from Alta Mesa attempted to attend this private meeting and was asked to leave. Quade Deposition, 34:4-8; 38:11-21.

7. Quade and Holtry were concerned about possible environmental impacts and potential risks of oil and gas development so close to their homes. Holtry Deposition, 75:15-77:20, Quade, 93:10 - 94:21. Holtry stated:

> Again, there is no way to know exactly what the risks and rewards are. What I do know is that there is not a dollar amount I would accept to gamble the value and environmental health of my home.

Holtry Deposition, 94:7-17.

8. Quade would consider selling her mineral rights in the property she owns for reasonable compensation. Quade Deposition, 84:9-11. Her decision would be based on complete information and knowing the risks and rewards. Quade Deposition 84:12-87:17; 139:20-141:5. The information provided and available at the time was inadequate. Quade, 144:21-147:4. Quade had no

knowledge of the value of the hydrocarbons when she purchased her property. Quade Deposition, 112:21-24

9. Holtry is not willing to lease her mineral rights. Holtry, 31:19-32:13; 94:18-95:9. Holtry has no knowledge of the value of the hydrocarbons, before or after the application was filed. Holtry Deposition, 81:7-12.

10. The mailing from Alta Mesa included a date and time for a hearing. Holtry Deposition, Exhibit 4. This left little time for Plaintiffs to research and prepare. Quade Deposition 47:11-22. The December 14th hearing, in Boise, was for the purpose of considering Alta Mesa's Application forcing property owners, such as Quade and Holtry who did not want to lease their mineral rights, to pool and integrate their mineral rights to benefit Alta Mesa for commercial oil and gas production. Holtry Deposition, Exhibit 4.

11. Quade contacted the Deputy Attorney General identified in the mailing to ask about the process and what information would be made available before the hearing, but got no useful information or assistance from the Attorney General's office. Quade Deposition, 28:9-29:6; 42:3-13; 47:4-10.

12. Plaintiffs were represented by counsel at the hearing. Plaintiff's Counsel attempted to elicit testimony and introduce documents concerning the value of Plaintiff's property interest in the oil and gas believed to lie beneath their homes. The Hearing Officer did not allow evidence of the likely value of the mineral pool to be drilled. Hearing, 169:16-24.

13. The Hearing Officer did not allow inquiry of the possible effect of the lease terms on property values (Hearing, 213:15-19; 214:22-24; 241:3-7) or the economic terms of existing leases with other property owners (Hearing 189:6-18).

8. Brief in Support of Plaintiff's Motion for Summary Judgment

14. The standard lease imposed on non-consenting property owners (OGCA) provides a 1/8 royalty and a $100 bonus. Mr. Pepper, the land man for Alta Mesa, testified that the $100 bonus payment was just and reasonable:

> Q: And it's – how do you come upon that $100 lease bonus number?
> A: Lots of things. You know, you look at, you know, the economics of the play that you are doing, the cost you have to put into developing. Your play or your well, your infrastructure, what is economic in cost. Looking at the area in history, what has been done previously. Lots of different factors go into the 100.
> Q: And in your experience that's a fair lease bonus offer for this area?
> A: Yes.

Hearing, 90:12-19.

All property owners receive the $100 bonus. Hearing, 188:1-5. Not all property owners receive the standard 1/8 royalty:

> Q. So are some of the owners in this proposed unit receiving more than a one-eighth royalty?
> A. I'm not going to answer it specifically. Those are individuals who were willingly and actively involved in negotiations on signing leases. The specific terms of those are private and shouldn't be part of this process.

Hearing, 189:10-16.

All non-consenting owners receive the standard 1/8 royalty. Terms can be modified if owners "willingly negotiated" different royalties. Hearing, 190:18-22.

15. Mr. Pepper was asked how royalties are determined and if transportation costs are deducted:

> Q. Right. So if the gas has to be sold at a spot distant from the well, who pays for the cost of moving the gas?
> A. Well, depending on the contract in which I sold it. There might be more transportation costs. There may not be.
> Q. For the purpose of my clients, you know, what they are trying to determine is will Alta Mesa deduct the cost of transportation before

> determining royalties?
> A. You know what, I would have loved to have the opportunity to discuss that with your clients.
> Q. You have the opportunity right now?
> A. I am. You know, specific to your clients, sir, who is what we're here for, they have refused to discuss or refused to engage with me in any manner of negotiation on a lease, nor gather information to maybe answer or have that knowledge in order to make that decision. So now we're sitting here today because they've refused to lease. But now you are claiming you want information because -- or they weren't given the information. So which is it?

Hearing, p. 198:19-199:15.

Pepper went on to testify that it would be impossible to determine where the gas would be sold (Hearing, 202:10-12), what price the gas would be sold for (Hearing, 202:13-15), the exact value of the proceeds from the well (Hearing, 202:16-19) and the value of the gas Alta Mesa is entitled to for its operations (Hearing, 203:11-204:4).

16. Counsel for Plaintiffs attempted to explore Mr. Pepper's conclusion and inquire further about the value, to Alta Mesa, of the product Plaintiffs would be forced to sell. Hearing, 159:4-160:1. The Hearing Officer stated that "the value of the product is speculative, at best, at any rate" and that she did not think "asking about projections on costs and potential recovery is probably going to be helpful in terms of determining whether or not the terms of the lease are fair and reasonable." Hearing, 160:2-25.

17. Counsel for Plaintiffs attempted to inquire regarding the value of royalties and was told that such questioning was "not productive" and that potential royalties are not relevant to determining what bonus payment is just and reasonable. Hearing, 161:1-11.

18. Counsel for Plaintiffs asked what a reasonable estimate of royalties would be, and was told that "internal estimates" were "proprietary." Hearing, 168:15-25. An objection to the question

as irrelevant was made by Alta Mesa's attorney and the Hearing Officer sustained the objection but went on to tell the witness that he was "free not to answer" as the question was "hypothetical." Hearing, 169:1-24 The witness did not answer.

19. When Counsel for Plaintiffs sought to inquire about the risks associated with the proposed plan of operations and how that affects homeowners, Alta Mesa's attorney and the Hearing Officer agreed that the reasonableness of the terms of the lease agreements are "irrelevant" because the agreements are "standard." Hearing, 238:20-240:8.

20. The lease agreement terms were not reasonable to Quade, "The fact that I'm taking a risk should be otherwise compensated at the same reasonable amount that they have a risk of making an incredible profit." Quade Deposition 111:20-23.

21. The Hearing Officer allowed no inquiry of the effects of drilling operations on property values. Hearing, 248:8-11.

22. Counsel for Plaintiffs attempted to ask numerous questions regarding the risk of potential environmental impacts, but the Hearing Officer determined the following inquiries to be irrelevant in determining what was just and reasonable:

- Potential groundwater contamination, Hearing, 247:8-11.
- Potential air pollution, Hearing, 248:13-17
- Potential radioactivity, Hearing, 249:11-14
- Noise level of drilling operations, Hearing, 249:4-9
- Light pollution from drilling operations, Hearing, 251:5-10
- Impacts on soil quality, Hearing, 251:13-15
- Potential impacts of fracking, Hearing, 251:17-21
- Increased local traffic, Hearing, 254:16-23
- Additional property tax burdens of development, Hearing, 255:1-13.

The Hearing Officer stated that "none of this goes to the issue of the lease being fair or reasonable." Hearing, 252:6-25. She also stated that the Hearing was not the forum for discussion of

those matters. Hearing, 250:1-4.

23. Counsel for Plaintiffs noted that his clients had no other forum. Hearing, 251:25-252:1-3. Shelly Brock testified at the hearing that there was no other venue to object to forced pooling. (Brock Deposition, 100:22-25) or the risks associated with drilling. Hearing, 284:18-285:1.

24. Counsel for Plaintiff attempted to inquire about the terms of the lease allowing Alta Mesa additional rights to Plaintiff's land if oil is found including, "the right of ingress and egress over the lands owned by the lessor to construct and maintain pipelines, telephone and electrical lines, tanks, towers, ponds, roadways, plants, equipment and structures." Hearing, 193:4-23. The lease also grants Alta Mesa exclusive rights to "inject air, gas, water, brine, and other fluids from any source into the subsurface strata" as deemed to be economic by Alta Mesa. Hearing, 193:24-194:20. Plaintiff's Counsel asked the witness to give his opinion if oil was likely under Plaintiff's land. The witness stated that had an opinion, but refused to answer and the Hearing Officer declined to direct him to answer. Hearing, 195:8-197:7.

25. The Hearing Officer noted that the paperwork Plaintiffs received was confusing, but that they "should educate themselves" and talk to an attorney. Hearing, 263:14-20. She went on to tell property owners that they should talk to the Department, while noting that the Department cannot give legal advice. Hearing, 265:12-24.

26. Quade has worked extensively with disabled children and has an adult daughter with a developmental disability. Hearing, 273:1-7. At the hearing, she attempted to testify that she had done research and discovered credible research linking environmental impacts of drilling to developmental disabilities. Hearing, 274:14-275:19. The Hearing Officer excluded her testimony for lack of foundation, and further told her that she could not lay a foundation. Hearing, 276:11-

277:10. Quade could not testify, based on her own knowledge, of the potential economic impacts of the increased risk of developmental disabilities on the tax base. Quade Deposition 123:2-5; 123:23-124:16; 125:23-126:14. Reasonable compensation, to Quade, must include at least a consideration of the risks and rewards of drilling. Quade Deposition, 126:15-128:18.

27. State law requires that property owners be offered the option to enter into a Participation Agreement. The Participation Agreement offered by Alta Mesa specifically incorporates a prior Participation Agreement with another company, Bridge Resources. Hearing, 224:7-225:8; 230:12-233:6. When Plaintiff's counsel inquired about this agreement and if a copy had ever been provided to non-consenting property owners, the Alta Mesa witness, Pepper, refused to provide a copy. Hearing, 233:7-9. Alta Mesa's attorney, Mr. Christian, went on to testify that any inquiry into the reasonableness of the agreement is not relevant because the agreement is standard and had been approved. Hearing, 239:7-16.

28. During the hearing, the Hearing Officer interjected to provide her own testimony regarding:

- Her interpretation of contract terms and what was standard in the industry. Hearing, p. 220:10-21
- The impossibility of determining the value of ultimate recovery from the well. Hearing, 163:8-10.
- What point a witness was going to make regarding the likely production life of a well, concluding that it was between five and fifty years. Hearing, 171:17-24. The witness did not answer the question asked.
- Royalties are commonly not disclosed to the public, because "sometimes neighbors fight about it" and it "causes problems." Hearing, 189:19-25
- The difficulty of determining deductions taken from royalties. Hearing, 200:12-17
- The terms of the leases comply with industry standard of "reasonably prudent operator" and that "the just and reasonable is not intended to be a constitutional challenge to any kind of term." Hearing, 221:10-19
- The terms of the lease regarding the timing and number of wells is standard. Hearing, 222:6-223:11.

- It is standard in the industry to bind land owners to undisclosed agreements incorporated into the leases. Hearing, 224:14-24.

29. Plaintiff's Counsel attempted to ask Alta Mesa's witness, a geologist, about the effect of drilling operations and what it could do to the value of the homes. Hearing, 241:3-7. The Hearing Officer did not allow this questioning and informed Plaintiff's Counsel that he had to call his own geologist. Hearing, 241:19-242:6. The next day Plaintiff's Counsel brought a geologist to testify on behalf of Plaintiffs. The Hearing Officer did not allow this testimony either. Hearing, 327:4-22.

30. The December hearing resulted in a Final Order integrating the pool and forcing Plaintiffs to lease their mineral rights without additional compensation. Holtry Deposition, Exhibits 5, 6. The Order provided five options to non-consenting property owners, such as Holtry and Quade. Holtry Deposition, Exhibit 5, p. 25. None of the options were acceptable to Holtry. Holtry Deposition, 40:12-41:6. Quade would sign a lease with additional compensation if it were reasonable. Quade Deposition, 141:13-17.

31. The Order of the Oil and Gas Commission Director Schultz concluded that the terms of the forced leases were "just and reasonable" based solely on Alta Mesa's representation. Holtry Deposition, Exhibit 5, p. 21, ¶ 26.

32. After the hearing, Dr. Ron Throupe, Professor of Real Estate at the University of Denver, was asked to provide his opinion regarding potential risk to property value of nearby oil and gas drilling. His report, and deposition testimony, concludes that while actual property damage from drilling may not occur, it presents a very real risk to property value. Public perception of oil and gas drilling can create a stigma affecting the property value Deposition of Ronald Throupe, 65:12-66:22; 94:3-9; Exhibit E, Declaration of James Piotrowski in Support of Plaintiffs' Motion for Summary

Judgment ("Throupe Deposition") which can result in a smaller pool of prospective buyers (Throupe Deposition, 135:9-25) resulting in a likely diminution of property value. Throupe Deposition, 59:25-60:7. Throupe Deposition, Exhibit 1, p. 6.

33. Alta Mesa has recently filed a Petition to Amend Order in which it seeks to extend the terms for an additional eighteen months. Declaration of James Piotrowski in Support of Plaintiffs' Motion for Summary Judgment, Exhibit F. In support of the Petition, Alta Mesa now reveals the approximate cost of the test well and seeks to build facilities for storing, transporting and servicing the wells. No estimate of production is provided, nor is any estimate of anticipated royalty payment.

IV. UNDER THE RELEVANT LEGAL STANDARDS, PLAINTIFFS ARE ENTITLED TO SUMMARY JUDGMENT ON THE LIABILITY ASPECTS AND SOME PORTIONS OF THE REMEDIAL ASPECTS OF THEIR CLAIMS FOR VIOLATION OF DUE PROCESS RIGHTS.

The fundamental problem addressed by statutes such as Idaho's Oil and Gas Conservation Act is to protect the "correlative rights" of mineral rights owners. Real property ownership, and thus, often, mineral rights ownership, is most often tied to the subdivided surface estate, without regard to the pools of hydrocarbons underlying those estates. While surface estates are easily subdivided and clear boundaries can be drawn, hydrocarbons in liquid and gaseous form are migratory without respect for surface divisions. In short, a well placed on the surface of one parcel of land is almost certain to draw oil and gas from under the adjoining parcels. The State of Idaho, the Director of the Department of Lands, and the Oil and Gas Conservation Commission can be properly empowered to rectify the problems that arise from these realities. But neither the statutes that Idaho has developed, nor the particular procedures that were utilized to compel the leases of mineral rights held by

Plaintiffs and their members meet constitutional standards for due process of law.

The compelled lease of one's property rights implicates the due process clause of the U.S. Constitution which provides "nor shall any person . . . be deprived of life, liberty, or property without due process of law," U.S.Const. Amend. 5, and, similarly "nor shall any state deprive any person of life, liberty, or property, without due process of law." U.S. Const. Amend. 14. Idaho has chosen to use the power of the state to give to third parties (oil and gas development companies such as Alta Mesa) the property rights of its citizens. The statutory system which it has created to do so establishes the prices that will be paid for the natural gas and other hydrocarbons that it allows third parties to take from others, but in doing so, has failed to create a system that properly sets those rates. The statutory scheme is thus inherently defective, and will necessarily result in violations of due process. In the particular application of that scheme to these Plaintiffs, the Defendants utterly failed to protect the due process rights of the Plaintiffs and other property owners, running what amounted to a sham hearing in which the Plaintiffs were prevented from exercising their rights and in which the decision maker failed to consider the vast bulk of the evidence and considerations which he was constitutionally required to consider.

A. Section 1983 is the Appropriate Vehicle for Challenging and Provides a Remedy for Administrative Agency Conduct and State Statutes that Violate Due Process.

The Supreme Court of the United States has held that 42 U.S.C. § 1983 is the appropriate statutory vehicle for remedying violations of federal constitutional provisions, including the due process clause of the Fourteenth Amendment. *Collins v. City of Harker Heights, Texas*, 503 U.S. 115, 199-200 (1992).

B. Due Process Requires that Before the State May Compel the Sale of Privately Owned Resources It Must Provide A Meaningful Opportunity To Contest the Sale and to

Establish Just and Reasonable Terms.

The Supreme Court of the United States has long held that "a state has constitutional power to regulate production of oil and gas so as to prevent waste and to secure equitable apportionment among landholders of the migratory gas underlying their land, fairly distributing among them the costs of production and of the apportionment." *Hunter Co. v. McHugh*, 320 U.S. 222, 227 (1943), *citing Lindsley v. Natural Carbonic Gas Co.,* 220 U.S. 61, 77 (1911); *Bandini Pentroleum Co. v. Superior Court*, 284 U.S. 8, 22 (1931); *Champling Refining Co. v. Corporation Commission*, 286 U.S. 210, 232-4 (1932); *Thompson v. Consolidated Gas Corp.*, 300 U.S. 55, 76-77; *Patterson v. Stanolind Oil & Gas Co.*, 305 U.S. 376, 379 (1939).

> If the statute be viewed as one regulating the exercise of the correlative rights of surface owners with respect to a common source of supply of oil and gas, the conclusion that the statute is valid upon its face, that is, considered apart from any attempted application of it in administration which might violate constitutional right, is fully supported by the decisions of this Court.

Bandini Petroleum Co., 248 U.S. at 22 (emphasis added). Thus, the Court has held that while statutes similar to Idaho's Oil and Gas Conservation Act may be valid, their validity will depend in the first instance upon whether the particular methods established meet constitutional standards, and in the second instance on whether the statute's application meets those standards. In short, such statutes are subject to both facial and as-applied challenges.

In assessing similar Federal statutory schemes, the Supreme Court has made clear that the requirement to determine "just and reasonable" terms of sale are co-extensive with the constitutional requirements of due process of law. "The Congressional standard prescribed by the statute coincides with that of the Constitution," and thus the Court's holding above sets out the standard of review for both Constitutional challenges (like the present one) and federal statutory challenges (not relevant

here). *FPC v. Natural Gas Pipeline Co.*, 315 U.S. 575, 586 (1942)("the Congressional standard prescribed by the statute coincides with that of the Constitution").

Idaho Code similarly requires that a hearing be held to establish terms of the compelled leases that are "just and reasonable." I.C. §47-320(1). But merely reciting that terms shall be "just and reasonable" does not ensure that due process requirements are satisfied. This is because due process further requires both (1) "the opportunity to be heard 'at a meaningful time and in an meaningful manner," either before or after property is taken, *Mathews v. Eldridge*, 424 U.S. 319, 333 (1976); and, (2) ascertainable standards which avoid leaving the determination of "just and reasonable" terms solely to the discretion of an appointed decision maker. *Hornsby v. Allen*, 326 F.2d 605, 609 (5th Cir. 1964); *Holmes v. New York City Housing Authority*, 398 F.2d 262, 264 (2d Cir. 1968); *Powers v. Canyon County*, 108 Idaho 967, 978-979 (1985). In this case, as set out herein, the hearing provided was not meaningful, and the standards applied were not reasonably ascertainable.

C. The Right to Due Process of Law Further Requires that Before the State May Establish Rates Setting the Sale Price of Privately Owned Resources, It Must Consider and Account for A Wide Range of Relevant Factors.

In Idaho, the Oil and Gas Conservation Act not only establishes a procedure for defining gas production pools and establishing correlative rights, it also establishes the rates that will be paid to owners of those mineral rights. The statute provides that upon issuing a spacing and pooling order, the Director of the Department of Lands (and the Commission reviewing his decision) shall provide that mineral rights owners shall receive a 1/8 royalty, as well as the bonus payment that was provided by the development company to the voluntary lessors. I.C. §47-310(c). Such a system necessarily results in standardized and low bonus payments to non-consenting owners. As was the case here, companies like Alta Mesa will not increase their bonus payment to consenting lessors, they will,

instead, increase the royalties to such lessors, knowing that a higher royalty payment to one mineral owner will not result in higher payments to others because of the statute. Hearing, 90:12-19; 190:18-22. On the other hand, any increase in bonus payment would result in increases for all non-consenting owners under the terms of the statute. The result is predictable, the rate for compelled natural gas mineral rights leases in Idaho is a de minimis bonus payment, and a 1/8 royalty, which rate is set by statute.

Just as the State is permitted to compel the sale of mineral rights, there is nothing inherently improper in the state setting a rate governing that otherwise private sale. In a long series of cases arising in multiple industries, but including oil and gas development, distribution and sales, the Supreme Court established the rules which the Constitution requires for the setting of rates governing private party sales. Those rules require a court to judge the constitutionality of rates by a process that involves balancing the public and investor interest. *Federal Power Comm'n v. Hope Natural Gas*, 320 U.S. 591, 603 (1944). In general, the court must ensure that the utility rates are high enough that the investors being compelled to sell at the regulated rate may make a moderate profit. John N. Drobak, *Constitutional Limits on Price and Rent Control: The Lessons of Utility Regulation*, 64 WASH. L. REV. 1, 108. While the Court has not provided a definitive test in determining whether or not a particular rate substantively satisfies due process, the Constitution requires courts and regulatory agencies to take the following factors into consideration: (1) the justification for the price regulation; (2) the duration of the regulation, and (3) the ability of a firm to withdraw from the regulated business. *Id.*, at 110. In setting the terms of sale where the government is establishing those terms, including price, an administrative agency must determine and then act within "a zone of reasonableness within which the [agency] is free to fix a rate varying in amount and higher than a

confiscatory rate." *FPC v. Natural Gas Pipeline Corp.*, 315 U.S. 575, 585 (1942), *citing Banton v. Belt Line Ry. Corp.*, 268 U.S. 413, 422, 423 (1925)*; Columbus Gas Co. v. Commission*, 292 U.S. 398, 414 (1934); *Denver Stock Yard Co. v. United States*, 303 U.S. 470, 483 (1938). That zone of reasonableness will be established by consideration of numerous factors including:

- a financial "return to the equity owner [that must be] commensurate with returns on [other] investments," *Hope Natural Gas*, 320 U.S. at 603;
- the establishment of returns "sufficient to assure confidence in the financial integrity" of all entities involved, *Id.;*
- "the requirements of the broad public interests" protected by the relevant rate setting statute, *Permian Basin Area Rate Cases*, 390 U.S. 747, 791 (1968);
- the avoidance of rates that are "unjust, unreasonable, unduly discriminatory, or preferential," *Natural Gas Pipeline Corp.*, 315 U.S. at 583;
- ensuring the established rates "fairly compensate investors for the risks they have assumed," *Mobil v. FPC*, 417 U.S. 283, 30 (1974).

In addressing a challenge to a rate setting statute or order which is required to utilize such factors, the scope of review is well established and while deferential to the agency, does require that the agency actually consider the relevant factors:

> First, [the reviewing court] must determine whether the Commission's order, viewed in light of the relevant facts and of the Commission's broad regulatory duties, abused or exceeded its authority. Second, the court must examine the manner in which the Commission has employed the methods of regulation which it has itself selected, and must decide whether each of the order's essential elements is supported by substantial evidence. Third, the court must determine whether the order may reasonably be expected to maintain financial integrity, attract necessary capital, and fairly compensate investors for the risks they have assumed, and yet provide appropriate protection to the relevant public interests, both existing and foreseeable**. The court's responsibility is not to supplant the Commission's balance of these interests with one more nearly to its liking, but instead to assure itself that the Commission has given reasoned consideration to each of the pertinent factors**.

Mobil v. FPC, 417 U.S. 283, 307-08, 94 S. Ct. 2328, 2345 (1974) *quoting Permian Basin Area Rate Cases*, 390 U.S. 747, 791-92 (1968)(emphasis added). In the case of the Federal rate setting statute at issue in *Mobil v. FPC, Permian Basin* and many of the other rate setting cases, "the Congressional standard prescribed by the statute coincides with that of the Constitution," and thus the Court's holding above sets out the standard of review for both Constitutional challenges (like the present one) and federal statutory challenges (not relevant here). *FPC v. Natural Gas Pipeline Co.*, 315 U.S. at 586.1

D. Defendant Schultz Failed to Comply With Well-Established Standards of Due Process.

In the present case, the Defendants not only failed to protect but actively violated the constitutional rights of the Plaintiffs and the other landowners affected by the integration order. As noted, due process requires "the opportunity to be heard 'at a meaningful time and in a meaningful manner," *Mathews v. Eldridge*, 424 U.S. 319, 333 (1976). In this case, the opportunity to be heard was not meaningful.

The Plaintiffs were barred from fully cross-examining the witnesses against them, were prevented from introducing evidence that related to the potential costs they would incur if drilling occurred, were prevented from introducing evidence about the likely receipts that Alta Mesa would receive from the sale of Plaintiffs' minerals, and faced a hearing officer who overstepped appropriate boundaries and testified about the justness and reasonableness of the very leases whose terms she was supposed to be judging. In addition, Plaintiffs were denied access to portions of the very leases which they were being subjected to, which also meant the hearing officer and Defendant Schultz

1 "And the fact that the distribution here involved is by wholesale rather than retail sales presents no differences of significance to the protection of the public interest which is the object of price regulation." *Natural Gas Pipeline Co.,*

made findings that those leases were "just and reasonable" without even knowing their terms.

As specifically applicable to the due process standards governing setting rates for the forced sale of natural resources such as oil and gas, the Plaintiffs were entitled to a decision that considered the economic impacts on all parties, including the impact of mineral rights development on the total return on their investment in their properties, the requirements of all of the relevant public interests, the avoidance of unjust, unreasonable and discriminatory outcomes, and at least an attempt to ensure that sellers such as the Plaintiffs received fair compensation for the risks (financial and otherwise) that they were required to undertake. The decision in this case could not possibly have taken account of those factors, because the Hearing Officer refused to admit evidence on those factors.

V. UNDER THE RELEVANT LEGAL STANDARDS, PLAINTIFFS ARE ENTITLED TO REMEDIES INCLUDING RECISSION OF THE COMPELLED CONTRACTS AND REVERSAL OF THE OFFENDING ORDER.

Both the Ninth Circuit "and the Supreme Court have repeatedly held that the appropriate remedy for deprivation of a liberty and/or property interest without due process is to order the process that was due and any attendant damages which directly resulted from the failure to give the proper procedure." *Brady v. Gebbie*, 859 F.2d 1543, 1551-52 (9th Cir. 1988), *citing* Vanelli v. Reynolds School District No. 7, 667 F.2d 773, 778 n. 8 (9th Cir. 1982); *Cary v. Piphus*, 435 U.S. 247, 259-64 (1978). In the present case, that requires rescinding the lease contracts which Plaintiffs Quade and Holtry were "deemed" to have entered into by state law, reversal of the Final Order of the Oil and Gas Conservation Commission, and a direction that no such leases shall be compelled unless and until the Commission and the Director hold hearings fully complying with the requirements of due process, and that no rates governing the sale of natural gas shall be set without consideration of

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315 US at 583.

the constitutionally required factors.

At this time, issues of disputed fact exist as to whether Plaintiffs have suffered financial damages, the scope of those damages, and whether those damages may be mitigated if the Defendants provide the full scope of legal process that is due. But where it is still possible to order provision of that process, a court should do so.

DATED this 15th day of May, 2018.

HERZFELD & PIOTROWSKI, PLLC

/s/
James M. Piotrowski
Marty Durand
Attorneys for Plaintiff

CERTIFICATE OF SERVICE

I hereby certify that on the 15th day of May, 2018, I electronically filed the foregoing document with the Clerk of the Court using the CM/ECF system. The CM/ECF system will send notification of such filing to the following:

Steven Strack Joy Vega Kristina Fugate Deputy Attorneys General P.O. Box 83720 Boise, Idaho 83720-0010	[X] electronic mail [ ] U.S. Mail postage prepaid [ ] Facsimile [ ] Hand-Delivery

/s/
James Piotrowski