STATE OF NEW YORK
DEPARTMENT OF ENVIRONMENTAL CONSERVATION

In the Matter of the Integration of Interests Pursuant to Environmental Conservation Law ("ECL") § 23-0901(3) within an Individual Spacing Unit Known as,

WINTER 1-A.

RULING ON MOTION TO STAY PROCEEDING

DEC Order No. DMN 08-04

Appearances of Counsel:

-- Alison H. Crocker, Deputy Commissioner and General Counsel (Jennifer Hairie of counsel), for staff of the Department of Environmental Conservation

-- The West Law Firm, PLLC (Thomas S. West of counsel), and Nixon Peabody, LLP (Ruth Leistensnider of counsel), for Fortuna Energy Inc.

-- Lipman & Biltekoff, LLP (Michael P. Joy of counsel), for WhitMar Exploration Co.

Fortuna Energy Inc., the well operator for the above referenced natural gas well, moved during the issues conference in the above referenced proceeding convened pursuant to part 624 of title 6 of the Official Compilation of Codes, Rules, and Regulations ("6 NYCRR Part 624") for a stay of proceedings pending the resolution of a title dispute between Fortuna and WhitMar Exploration Co. commenced in Supreme Court, Tioga County. For the reasons that follow, Fortuna's motion is denied with leave to renew.

Background and Proceedings

The Winter 1-A natural gas well is a sidetrack from the original Winter 1 well. Staff of the Department of Environmental Conservation ("Department") issued a permit to drill Winter 1 to Fortuna on May 10, 2006, and convened a compulsory integration proceeding pursuant to Environmental Conservation Law ("ECL") § 23-0901(3) to integrate uncontrolled mineral interests in the Trenton-Black River formation in the spacing unit associated with the Winter 1 well.

Uncontrolled interests in the Winter 1 well were subsequently integrated by DEC Order No. DMN 06-30 issued August 29, 2006 (see Exhibit ["Exh"] DMN 4). The ownership tabulation attached to DMN 06-30 showed that a certain tract in the Winter 1 spacing unit owned by Stephen M. Huntington (Tax ID No. 92.00-1-19.1) was controlled by Fortuna through a lease (see Exh "B" attached to DMN 06-30). Consequently, well costs associated with the Huntington parcel were assessed to Fortuna as the lessee of record at the time.

Fortuna subsequently filed an application for a permit to drill the Winter 1-A sidetrack. Department staff issued a well permit on August 28, 2007 authorizing Fortuna to drill the Winter 1-A well as a subsequent operation in the Black River formation in the Winter 1 spacing unit.

The Department also convened a second integration proceeding for the Winter 1 spacing unit. The ownership tabulation submitted by Fortuna for the Winter 1-A well showed that the Huntington parcel was no longer controlled by Fortuna (see Exh "B" attached to DEC Order No. DMN 08-04, Exh DMN 1). Based upon information supplied to the Department at least in part by Fortuna, staff understood that Fortuna's lease for the Huntington parcel had expired and the parcel had subsequently been leased to WhitMar. Accordingly, a second integration proceeding was required to allow WhitMar, as a new uncontrolled owner, to make an election with respect to participation in well costs associated with the Winter 1-A well. The Department's draft Order No. DMN 08-04 provided that it would supercede DMN 06-30 on a prospective basis only for those well costs associated with the Winter 1-A well.

Notice of the January 9, 2008 compulsory integration hearing was published in the Sayre Morning Times and the Elmira Star-Gazette on December 10, 2007. By letter dated December 11, 2007, Fortuna raised an objection with the Department indicating that it had a title dispute with WhitMar concerning the validity of WhitMar's lease for the Huntington parcel. Fortuna asserted that its original lease for the Huntington parcel remained in full force and effect.

The compulsory integration hearing convened as scheduled on January 9, 2008. With respect to the title dispute, the parties agreed that the issue would not be adjudicated in hearings before the Department, but would be submitted for resolution to Supreme Court, Tioga County. In addition to the title dispute, three other issues were raised during the integration hearing. First, Fortuna objected to a provision in

the draft order requiring it to provide well data and well site access to integrated participating owners ("IPOs") and integrated non-participating owners ("NPOs") without the imposition of terms of confidentiality. Second, Fortuna objected to the Department's proposal to assess against WhitMar, which had elected to participate as an IPO, only those well costs associated with the Winter 1-A sidetrack and not those costs associated with the portion of the original Winter 1 well used for the Winter 1-A sidetrack. Third, WhitMar objected to Fortuna's drilling of the Winter 1-A well prior to the completion of the compulsory integration process.

The matter was referred to the Department's Office of Hearings and Mediation Services for Part 624 adjudicatory proceedings on the three issues raised at the integration hearing, and Chief Administrative Law Judge ("ALJ") James T. McClymonds was assigned as presiding ALJ. A legislative hearing and issues conference was scheduled for May 13, 2008 in Montour Falls, New York. Timely notices of appearance to participate in the issues conference on the Winter 1-A well (see Matter of Dzybon 1, ALJ Ruling on Procedural Issues, June 6, 2007) were filed by Fortuna and WhitMar.

Fortuna's Motion to Stay Proceedings

The issues conference was convened as scheduled, and attended by Department staff, Fortuna and WhitMar. At the issues conference, Fortuna moved to stay the proceeding on the Winter 1-A well pending resolution of the title dispute in Tioga County Supreme Court. Fortuna informed the ALJ that after the integration hearing, Fortuna had commenced the quiet title action pursuant to the Real Property Actions and Proceedings Law ("RPAPL"), and that WhitMar had joined issue the previous day. Fortuna asserted that its inclusion of WhitMar in the ownership tabulations submitted for the Winter 1-A permit to drill was Fortuna's mistake. Fortuna further argued that until the RPAPL action was decided by Tioga County Supreme Court, WhitMar lacked standing to raise any issues concerning the Winter 1-A draft integration order.

In response to Fortuna's motion to stay proceedings. Department staff explained that its policy is not to refer title disputes to OHMS for hearings under Part 624, preferring instead that such disputes be resolved in a judicial forum (see DEC Program Policy DMN-1: Public Hearing Processes for Oil and Gas Well Spacing and Compulsory Integration ["DMN-1"], ¶ V.B). Department staff further explained that when title disputes are raised at compulsory integration hearings, staff does not

adjourn, but proceeds based upon the information supplied by the well operator with the subject permit to drill application, and the elections filed by uncontrolled owners. In this case, those documents showed WhitMar as holding the mineral interests for the Huntington parcel and making an election to participate as an IPO.

Accordingly, staff urged that, consistent with its practice in integration hearings and with the adjudication in Matter of Dzybon 1 (see ALJ Ruling on Issues and Party Status, March 14, 2008, at 26-28, appeals pending [Frank title dispute issue]), hearings should proceed while the title dispute is being litigated in Supreme Court. While staff agreed that the resolution of issues concerning WhitMar may be rendered academic if Fortuna prevails in Tioga County Supreme Court, it asserted that the issue concerning the costs chargeable to a newly-found uncontrolled owner on a subsequent operation could recur. Moreover, staff argued that WhitMar would suffer some prejudice if the hearing did not proceed based on the ownership tabulations submitted by Fortuna. Staff noted that for at least a period of time, Fortuna agreed that its lease expired. Finally, staff urges that the Department should not establish a precedent of adjourning the compulsory integration process whenever a party raises a title dispute.

WhitMar opposed Fortuna's motion. WhitMar asserted that Fortuna only discovered its mistake after WhitMar objected to the assessment of costs for the Winter 1 well, and that these proceedings should not be stayed pending resolution of the quiet title action.

At the issues conference, the ALJ reserved decision on Fortuna's motion pending a written ruling.

Discussion

The presiding ALJ has the broad authority and discretion to grant adjournments (see 6 NYCRR 624.8[b][1][ii]). However, the cautious exercise of such discretion is appropriate in the context of compulsory integration proceedings. The Department is statutorily charged with conducting compulsory integration proceedings as expeditiously as possible (see ECL 23-0501[3]). Moreover, compulsory integration proceedings generally involve multiple parties, including the well operator and multiple uncontrolled mineral interest owners. Thus, the determination whether to stay an administrative adjudicatory hearing in the compulsory integration context requires the

balancing of a variety of often competing interests.

In addition, with respect to title disputes, the Department's policy is not to resolve such disputes administratively (see DMN-1, ¶ V.B). Accordingly, the resolution of title disputes and the timing of such determinations are outside the Department's control. To efficiently and expeditiously administer the integration process, the Department must act based upon the best information provided to it by the parties to its proceedings. To adjourn the integration process whenever a party commences a title dispute in another forum runs counter to ECL article 23's statutory policy favoring the efficient administration of the integration process. Accordingly, in administrative adjudicatory proceedings conducted pursuant to ECL article 23, title 9, an ALJ's discretion to stay a proceeding should be exercised sparingly, and only when other remedies are inadequate and the equities involved are apparent and strong (see CPLR 2201; Matter of Estate of Weinbaum, 51 Misc 2d 538 [1966]).

In this case, several factors weigh in favor of granting the stay requested by Fortuna. First, the only parties to the draft integration order in Winter 1-A are Fortuna and WhitMar. No other uncontrolled owners are involved. In addition, Fortuna stipulated on the issues conference record to release all amounts not in dispute to the mineral interest owners in the unit. Thus, the only parties impacted by a stay would be Fortuna and WhitMar.

Second, two of the issues raised for adjudication -- (1) well data and access, and (2) the authority of a well operator to commence drilling prior to the completion of the integration process -- have been raised in other administrative proceedings pending adjudication and, therefore, will be resolved in those proceedings. The third issue -- the well costs chargeable to a newly-found uncontrolled owner for a sidetrack well -- appears to be a narrow issue. Third, all issues raised in Winter 1-A could be rendered academic if Fortuna prevails in its quiet title action.

On the other hand, the factors favoring denial of the stay request outweigh the factors in favor of a grant. First, no showing was made concerning how soon a resolution of the title dispute by Supreme Court might be expected. Moreover, although it was discussed at the issues conference, no showing was made demonstrating Fortuna's likelihood of success in the quiet title action.

Second, the issue concerning the costs chargeable against an uncontrolled owner for a sidetrack, albeit narrow, could recur. Moreover, the issue appears to be a purely legal one, not requiring the resolution of any threshold factual questions. At this stage of proceedings -- and without deciding the point -- the issue appears resolvable through an issues ruling after briefing only, and without the necessity of an evidentiary hearing. A decision on the issue would potentially provide guidance in future cases even if the specific title dispute is settled against WhitMar by the courts, and no administrative resources would have been wasted litigating case-specific facts.

Third, and most compellingly, the mistake in this case was Fortuna's. The ownership tabulations that triggered the commencement of compulsory integration proceedings by the Department were submitted by Fortuna itself, and were the subject of its control. It would be prejudicial to WhitMar if proceedings were adjourned based upon Fortuna's belated discovery of its mistake, particularly after Department staff and WhitMar proceeded based upon the tabulations supplied by Fortuna.

In sum, I agree with Department staff that so long as the Department refrains from adjudicating title disputes in compulsory integration proceedings, it must, as a matter of policy, proceed based upon the best information provided to it by the parties. Stays of proceeding while title disputes are litigated in other forums should be granted rarely, and only when a compelling demonstration is made. Such a demonstration has not been made in this case.

Ruling

Fortuna's request to stay this proceeding pending resolution of the quiet title action in Tioga County Supreme Court is denied with leave to renew. Fortuna may renew the motion upon a showing that a decision from Supreme Court, Tioga County is imminent, or upon a showing of a substantial likelihood of success on the merits of the quiet title action. In the alternative, these proceedings will be stayed if so ordered by Supreme Court, Tioga County.

A conference call will be convened with the parties in the near future to schedule closing issues conference briefs.

_____/s/_____
James T. McClymonds
Chief Administrative Law Judge

Dated: May 20, 2008
Albany, New York

TO: Attached Active Parties Service List (via email and regular mail)