

The future: legal issues



# Tackling oil and gas projects in Ohio

With the newest boom must come an awareness that these projects get unique treatment under Ohio mechanics' lien law

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**I**n light of the recent oil and gas boom in Ohio, landowners, leaseholders, contractors, subcontractors and material providers must be aware of the special rules that apply to mechanics' liens on oil and gas projects. Though some aspects are identical to the process followed to obtain a lien on commercial or residential projects, several significant requirements differ. Those differences create additional traps for the unwary.

**Parties entitled to a lien.** A lien on an oil or gas project can be asserted by any person who either performs labor or work or furnishes materials pursuant to a contract (express or implied) with the owner of any oil or gas lease or mineral estate. Ohio Rev. Code §1311.021(A). Also, as with a typical commercial mechanics' lien, a subcontractor, laborer, or materials supplier that provides labor or work or furnishes materials for the original contractor or another subcontractor also can assert a mechanics' lien on an oil or gas lease as long as the work was in carrying forward, performing, or completing the contract.

**Type of project activities covered by a lien.** The Revised Code enumerates the activities covered in relation to oil and gas work. Ohio Rev. Code §1311.021(A). First, the work or materials can be used for digging, drilling, boring, operating, completing, or repairing a well or an injection well. The injection well must further the production of oil or gas or dispose of waste generated during the production of oil or gas. Second, the work or materials can be used for altering, repairing, or constructing any oil derrick, oil tank, or leasehold production pipeline.

**Property interests to which the mechanics' lien may attach.** A properly perfected mechanics' lien can attach to three different property interests related to an oil or gas project. Ohio Rev. Code §1311.021(A).

First and most obviously, a lien attaches to the oil or gas lease or the mineral estate. The lien attaches to the entire leasehold interest without regard to the narrow focus of the work. See *Moran v. Johnson*, 91 Ohio App. 120, 122 (1952) (mechanics' lien attached to entire leasehold estate even though work was performed exclusively on the nonproducing well).

The growth of these new infrastructure projects affecting Ohio's industrial future means contractors must get up to speed with their specific requirements regarding liens.



Second, a lien can attach to the oil or gas produced or the proceeds from the sale of that oil or gas. Such a lien, however, is not effective against a purchaser or a pipeline carrier until the lien claimant delivers an affidavit to that individual by certified mail. Ohio Rev. Code §131.021(B).

Finally, a lien attaches to all materials physically located on the property subject to the lease and to any materials used in connection with the work. To be subject to a lien, the materials must have been used in connection with one of the activities enumerated above. See, e.g., *In re Costal Petroleum Corp.*, Bankr. N.D. Ohio No. B85-00594, 1986 Bankr. LEXIS 5447, \*20 (Aug. 25, 1986) (finding that the compressor was not used for a listed activity and so not subject to a mechanics' lien).

Perfection rules unique to oil and gas projects. Unlike a typical commercial project, the owner or lessee of a gas and oil project does not have to post, provide, or record a Notice of Commencement. Ohio Rev. Code §1311.021(C)(1).

Also, a subcontractor or material supplier does not have to provide and serve a Notice of Furnishing. Ohio Rev. Code §1311.021(C)(2).

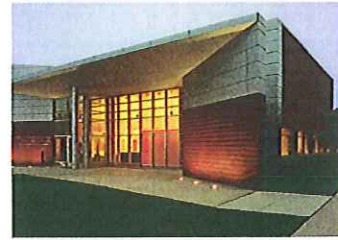
The only action that *must* be taken to perfect a mechanics' lien on an oil or gas project is for a contractor, subcontractor, material provider, or laborer to file an Affidavit of Lien with the county. Ohio Rev. Code § 1311.06. This affidavit must be filed within 120 days from the last date on which the claimant performed work or furnished material. Ohio Rev. Code §1311.06(B)(2). The affidavit must contain all the information required by the code section applicable to other liens, except that it does not have to list the first date that labor was performed or materials provided. Compare Ohio Rev. Code §1311.021(C)(3) with § 1311.06.

The original contractor's informational affidavit. On oil and gas projects, several procedural requirements may impact a claimant's right to obtain a lien. First, an owner or lessee can request an affidavit from the contractor with which it has contracted (the "original contractor"). Ohio Rev. Code §1311.021(C)(5). This affidavit should contain the following information regarding each of the original contractor's subcontractors, laborers, and materials providers: the name, the address, a description of the work performed or materials furnished, the total

amount of the contract and the balance due. If the owner or lessee requests this affidavit, the original contractor must comply or it will lose its right to file a mechanics' lien against the owner or lessee.

Using the information provided on the affidavit, an owner or lessee is entitled to insist upon receipt of a lien waiver from

the subcontractor or supplier prior to paying the original contractor or pay that subcontractor or supplier directly. Ohio Rev. Code §1311.021(C)(6)(a). Additionally, if the owner or lessee pays the subcontractor directly, it is entitled to set-off any payment made against the amount owed the original contractor.



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Ohio Rev. Code §1311.021(C)(7).

The subcontractor's written notice. Second, a subcontractor, laborer, or material supplier may serve the owner or lessee with a "notice in writing." Ohio Rev. Code §1311.021(C)(6)(c). This notice is similar to, but not the same as, the Notice of Furnishing that a subcontractor must serve in standard commercial context pursuant to Section 1311.05. The notice must include the following information: the nature of the work performed or to be performed, the materials furnished or to be furnished, the amount due or to be due, the identity of the person with whom the subcontractor contracted, the identity of the structure (i.e., well, oil derrick, oil tank, or pipeline) involved, the permit number for the structure, and the county where the structure is located. When provided with this notice, the owner or lessee can choose to pay the subcontractor directly. Ohio Rev. Code §1311.021(C)(6)(a).

**Summary.** To protect themselves from hidden lien claims that can attach to the property, the equipment, the oil and gas, or the proceeds from the sale of that oil and gas, developers (owners or lessees) should avail themselves of the right to request an informational affidavit from the original contractor and the right, if necessary, to make direct payments. Original contractors must adhere to the requirements for that affidavit or else they will lose their lien rights. Subcontractors, laborers, and material suppliers should provide the specified written notice to guard against the possibility that they will not be identified on the original contractor's informational affidavit. While claimants have more time to record an Affidavit of Lien, they should nonetheless move as quickly as possible.

Because there is no Notice of Commencement, it will take more time to gather the appropriate information to include in the Affidavit of Lien. While Ohio has seen a trickle of oil and gas activity over the years, the boom associated with the new means of extracting gas from the Utica and Marcellus shale formations means that many companies will be working on such projects for the first time. In our experience, contractors working on new types of projects and working with new contracting partners run into trouble more often. All parties involved with oil and gas projects should proceed with caution in order to take full advantage of their legal rights in case a problem develops. **BXM**

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