# Overview of State Pooling and Unitization Law

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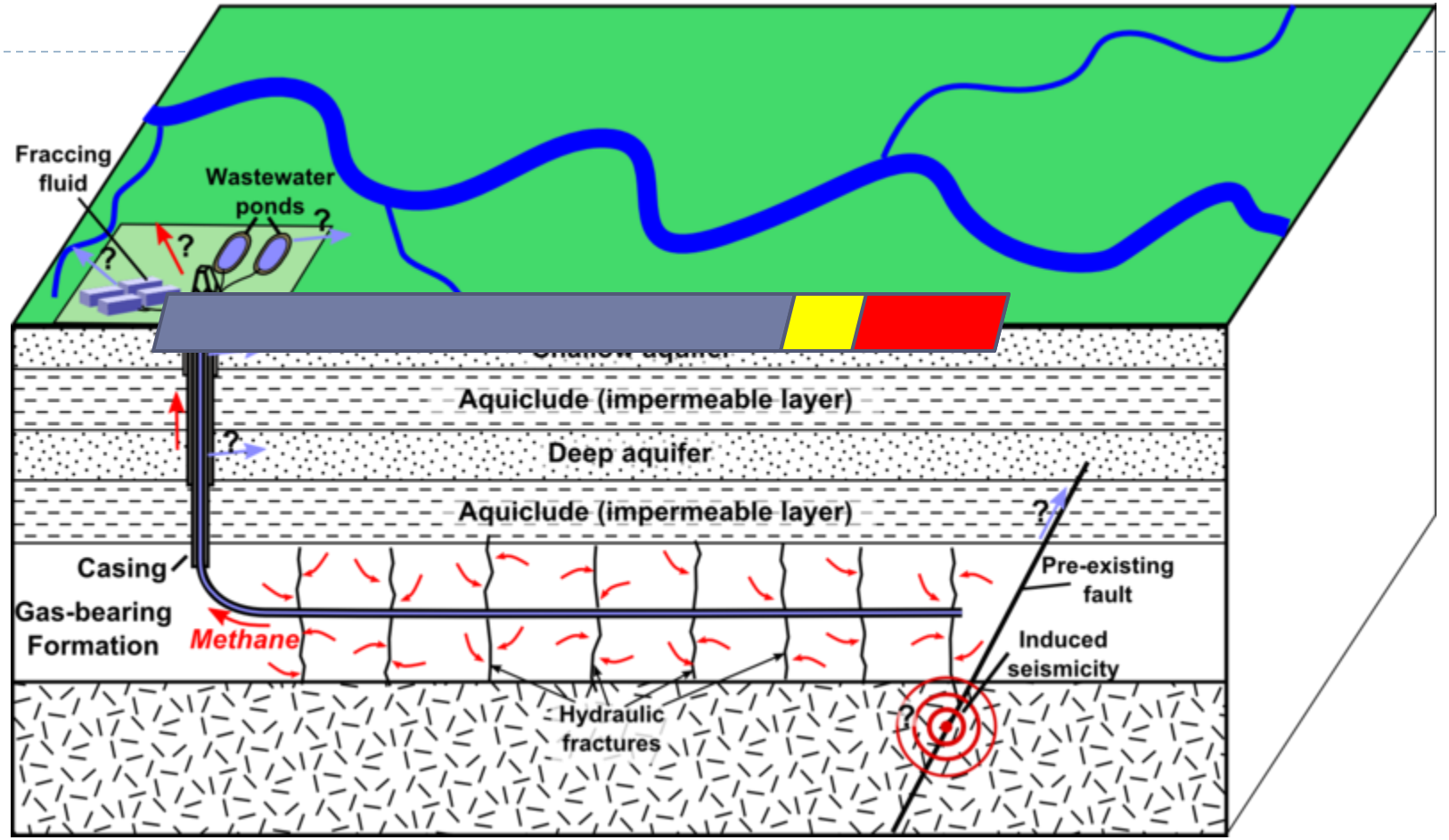
# Policy goals

- There are a number of policy rationales that have been put forward for compulsory pooling including
  - (a) protection of mineral owner rights where oil or gas can migrate from the owner's estate to another owner's well,
  - **(b)** ensuring that all recoverable portions of a resource are removed from the ground,
  - **(c)** facilitating extraction of a resource by a landowner or mineral rights owner who wants to develop a mineral resource but cannot access the means to recover it economically because of an intervening landowner's decision not to develop his resource, and
  - **(d)** minimizing development costs for gas operators.
- Likewise, there are policy rationales that have been put forward in opposition to compulsory pooling including
  - (a) protecting the right of individual property owners to control their own mineral resource and not be forced by the government or private industry to develop it and
  - (b) the freedom of individuals to contract for the development of their own resources on their own terms.

Compulsory Pooling Study Group , Draft Objectives, 12/19/12




- http://en.wikipedia.org/wiki/File:HydroFrac.png

# Hunter Co. v McHugh

- 1943
- State has power to regulate in order to:
  - Prevent waste
  - Secure equitable apportionment
  - Fairly distribute costs and apportionment

320 U.S. 222; 64 S. Ct. 19; 88 L. Ed. 5; 1943 U.S. LEXIS 1129

# North Carolina

**§ 113-3. Duties of the Department.**

(a) It shall be the duty of the Department, by investigation, recommendation and publication, to aid:

1. In the promotion of the conservation and development of the natural resources of the State;
2. In promoting a more profitable use of lands and forests;
4. In coordinating existing scientific investigations and other related agencies in formulating and promoting sound policies of conservation and development; and

§ 113-8. Powers and duties of the Department.

The Department shall make investigations of the natural resources of the State, and take such measures as it may deem best suited to promote the conservation and development of such resources.

N.C. GEN. STAT. § 113-3, -8 (2013)

# Standards of pooling

Ex: Oklahoma

1) "Reasonably calculated to increase the ultimate recovery of oil and gas from the shale reservoir"
2) "Feasible, will prevent waste, will protect correlative rights, and will with reasonable probability result in the increased recovery of substantially more oil and gas from the shale"
3) Estimated additional cost is less than the value of additional oil and gas recovered
4) "For the common good and will result in the general advantage of the owners of the oil and gas rights within the unit"

OKLA. STAT. tit. 52 § 87.9 (2012)

# Starting the Process : State

Ex: New York

"In the absence of voluntary integration as permitted by section 23-0701 of this article and after finding as required by subdivision 2 of this section, the department shall make an order integrating all tracts or interests in the spacing unit for development and operation."

NY CLS ECL § 23-0901 (2012)

# Starting the Process : Petition

In Alaska, petitioner must submit :

- Map and description of proposed unit
- Allegation that statutory requirements are met
- Recommendation for a plan of unitization which he considers to be fair, reasonable and equitable

ALASKA STAT. § 31.05.110 (Michie 2012)

# Starting the Process : Petition of Quorum of Stakeholders

Ex: Missouri

Owners of at least 75% interest in the right to drill into and produce oil and gas from the total proposed unit area and by persons

And

Owners of legal title to at least 75% of production payments must agree

MO. REV. STAT. § 259-120 (2012)

# Process for pooling

- Verify standards are met
  - Mostly administrative due process
    - Specify who provides justification and notice
      - Alabama v Kentucky
  - Colorado requires proof that reasonable, voluntary offers were made prior to petition
    - "terms no less favorable than those currently prevailing in the area"
    - "estimated drilling and completion cost of the well, the location and objective depth of the well, and the estimated spud date for the well"
- Notice and hearing
  - Louisiana does not accept electronic communication as sufficient

ALA. ADMIN. CODE. CH. 400-7 (2012)
KY. REV. STAT. tit. XXVIII, § 353 (2012)
COLO. REV. STAT. § 34-60-116-7d, (2012)
LA. REV. STAT. § 30-10(A)(2) (2012)

# Order is Issued, then …

- Stakeholders must agree
- 6 months is standard time period
- Illinois – more than one must agree

225 ILL. COMP. STAT. 725 (2012)

| State | % to Form (Operating Rights/Cost Payers) | % to form (royalty recipients) |
|---|---|---|
| Alabama | 50 | - |
| Arizona | 63 | 63 |
| Arkansas | 75 | 75 |
| California | 75 | 75 |
| Delaware | 75 | 75 |
| Florida | 75 | 75 |
| Georgia | 75 | 75 |
| Illinois | 51 | 51 |
| Kansas | 63 | 63 or 75 |
| Kentucky | 75 | 75 |
| Michigan | 75 or 0 | 75 or 90 |
| Mississippi | 33 | - |
| Missouri | 75 | 75 |
| Montana | 70 | 60 |
| Nebraska | 65 | 75 |
| Nevada | 62.5 | 62.5 |
| New Mexico | 75 | 75 |
| New York | 60 | 60 |
| North Dakota | 60 | 60 |
| Ohio | 65 | 65 |
| Oklahoma | 63 | 63 |
| Oregon | 75 | 75 |
| South Carolina | 75 | 75 |
| South Dakota | 60 | 60 |
| Utah | 70 | 70 |
| Virginia | 25 | - |
| West Virginia | 75 | 75 |

# Order Terms

- Impression that consenting and nonconsenting treated the same once pool is created and operational EXCEPT how operating expenses are paid
  - Utah – operations cover lease requirements
  - Kansas - Unit operation "shall constitute a fulfillment of all the express and implied obligations of each lease"
- Generally, nonconsenting repay from production
  - 'Risk fee' may be assessed

KAN. STAT. § 55-1306 (2012)

UTAH CODE ANN. § 40-6-8 (2012)

# Alternative Model: Arkansas/Idaho/Illinois/Kentucky/West Virginia

- Order contains options for nonparticipating owners
- Option 1: Surrender interest to the participating owners on reasonable conditions
- Option 2: Participate on a limited or carried basis
  - Repaid out of production
  - Illinois specifies acceptable range of risk fees (100-300%)
  - Kentucky and West Virginia specifies 100% risk fee
- State settles disputes

ARK. CODE ANN. § 15-72-304 (2012)

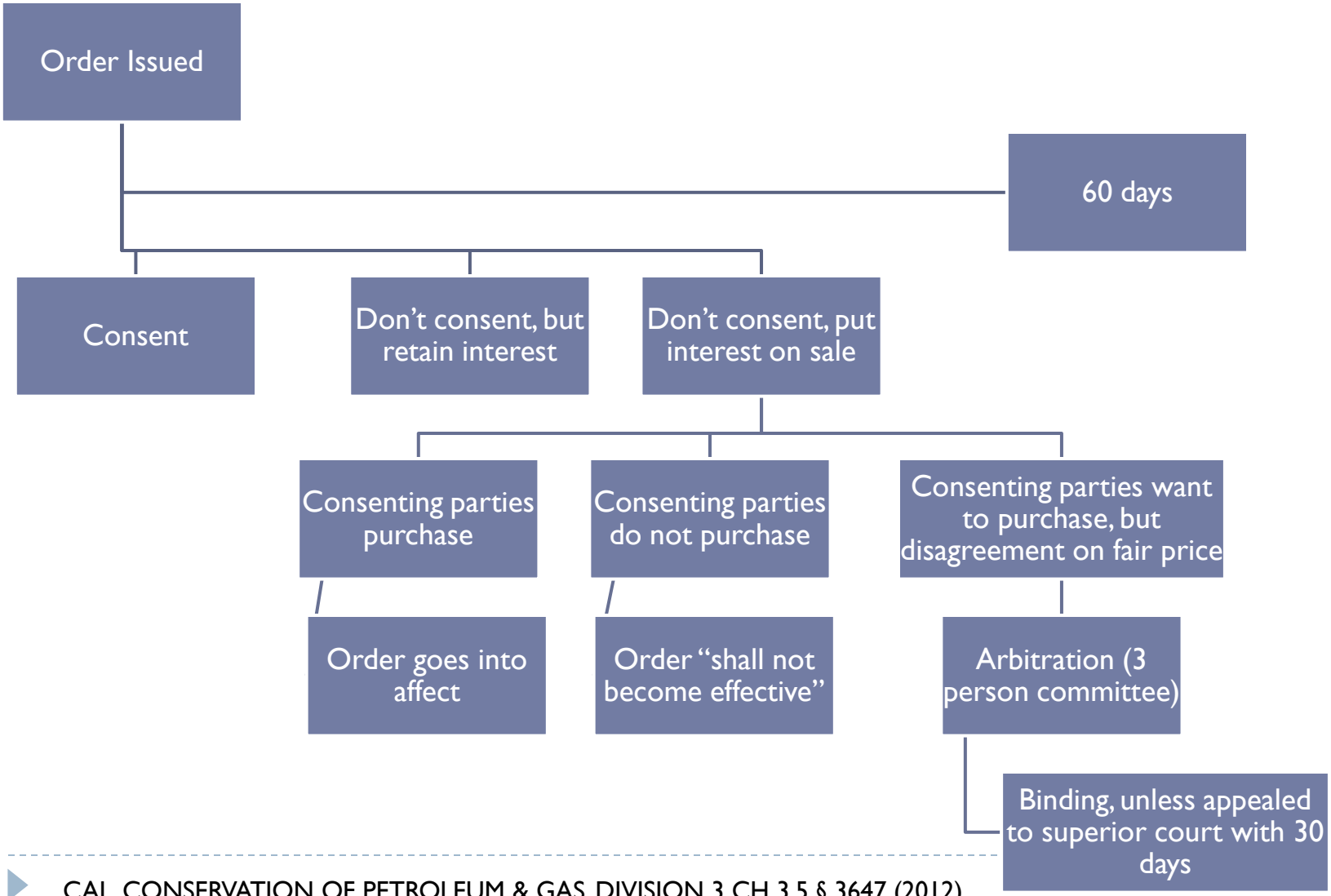
IDAHO CODE § 47-322, (2012)

225 ILL. COMP. STAT. 725/22.2 (2012)

KY. REV. STAT. tit. XXVIII, § 353.640 (2012)

W.VA. CODE § 22c-9-7 (2012)

# Alternative Model: California




CAL. CONSERVATION OF PETROLEUM & GAS, DIVISION 3 CH 3.5 § 3647 (2012)

# Kansas Orders Must Include:

- Legal description of land
- Describe proposed operation
- How production is allocated
  - Agreed upon by all interest owners
  - Absent agreement, state determines
- How costs will be divided
  - Procedure for if someone doesn't pay
  - Procedure for nonconsenting owners
- Operator guidelines
  - Supervision and conduct
  - "Particular records"
  - Selection, removal, and replacement procedures
- Voting procedure
- When operations begin
- How operation will stop
- Procedures for settlement of final accounts

KAN. STAT. § 55-1305 (2012)

# Determination of "fair and reasonable"

Washington State prohibits orders from allowing operators to have:

1. Preferential right to purchase mineral interests in the unit
2. A call on or option to purchase production from the unit
3. Unreasonable overhead charges (particularly central office expenses)
4. Prohibition against nonoperators questioning the operation of the unit

WASH. REV. CODE § 78-52-253 (2012)

# Length of Order: Texas/Washington

A unit is automatically dissolved:

- One year after its effective date if no production or drilling operations have been had on the unit
- Six months after the completion of a dry hole on the unit
- Six months after cessation of production from the unit.
  - Washington : "unless, prior to the expiration of such six-month period, the operator shall, in good faith, commence drilling or reworking operations in an effort to restore production"

TEX. NAT. RES. CODE ANN. § 1012-082 (2012)

WASH. REV. CODE § 78-52-257 (2012)

# Various concerns

- Bonus and royalties
  - No bonus, royalty standard seems to be 12.5% of proceeds
- Pugh Clause
  - Pooling orders generally specify the area they apply to, so no need
- Royalty recipients auditing operator
  - Why not?
  - Could require monthly or quarterly reports to all stakeholders
- Dispute resolution procedure could be required

# Other Considerations

- Kentucky, Ohio, and West Virginia – surface owners must consent
- Texas requires wells or proposed wells
- Ohio – nonparticipating owners not responsible for damage caused by drilling
- New Mexico – Order includes procedure for replacing operator

KY. REV. STAT. tit. XXVIII, § 353-654 (2012)

OHIO REV. CODE ANN. § 1509-27 (2012)

W.VA. CODE § 22c-9 -7(2012)

TEX. NAT. RES. CODE ANN. § 102-011 (2012)

N.M. STAT. ANN. § 70-7-7(G) (Michie 2012)

# Thanks and Contact Information

- Special thanks for Ted Feitshans for his guidance and mentorship

Please contact me by email

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