

Oil & Gas Law

Class 6:

**RoC: Regulatory Responses (3 of 4) –
Unitization**

A Little Something ...



Courtesy of Mother Nature ...

- ... From CL 5 ...
- =====
- ... Review of Voluntary Subdivision Problems
 - CL 5: SL 11 – 13
- ... Review of Pooling Calculation
 - CL 5: SL 21 – 23

Voluntary Subdivision Rule Prob. – 1

■ Assume a 40-acre / well limit:

- 1. The nearest production to a parcel of land is 25 miles away. A farmer, Thompson, owns 50 acres (in what is a “wildcat area” → “wildcat well” p. 4 FN3), and leases the north 10 acres to Green Oil Co. for oil & gas development. Is the lessee entitled to an exception?
- 2. The nearest production to a parcel of land is 25 miles away. A farmer, Thompson, owns 50 acres in wildcat territory and deeds the north 10 acres to Jones, another farmer. Subsequently, Jones leases the 10 acres to Brownman E&P Co. Can B E&P Co. receive an exception?

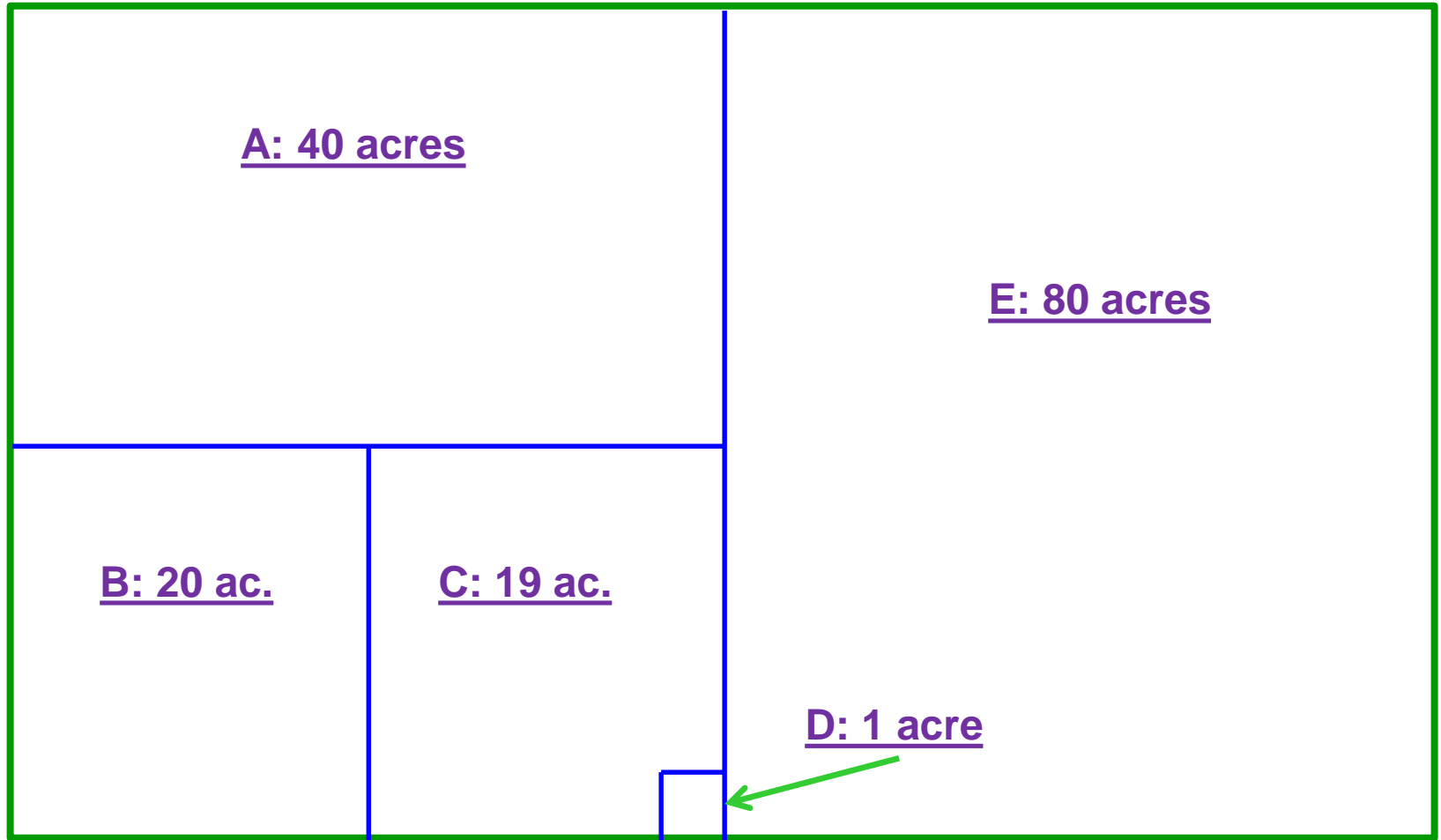
Voluntary Subdivision Rule Prob. – 2

- 3. At a time when there's no drilling or development of O&G in the vicinity, the owner of an 80-acre farm conveys a ½-acre lot to Jones. Several years later, oil is discovered in the vicinity, and Jones seeks a Rule 37 exception to prevent confiscation. **Will he get it? Would it make any difference whether there was a well on an adjacent tract that was draining Jones' tract?**
- 4. A new discovery well is completed 3 miles outside of town. Stevens, who owns a large tract of land on the edge of town, sells the tract, except a small corner lot where he plans to build a Sonic. Additional drilling reveals that the new reservoir extends laterally beneath the town. Stevens concludes that an oil well would be more profitable than a Sonic. **Should the RRC grant his application for a Rule 37 permit?**

Voluntary Subdivision Rule Prob. – 3

- 5. Dad owns 40-ac. tract in wildcat territory. In 1980, he leases to CQ Oil Co.; in 1982, he deeds half to Son, other half to Daughter; in 1984, O&G are discovered in the area. Is CQ Oil Co. entitled to 1 permit, or 2 permits?

P. 706 ¶ 1: Example - Situation



P. 706 ¶ 1: Example - Comparison

- 160-ac.
field
allowable =
1,600 bbl.
- =====
- Compare
- “acreage
only”
allocation
- 50-50
allocation
- 1/3 wells,
2/3 acreage
allocation
- “wells only”
allocation

		ACREAGE <u>ONLY</u>	<u>BLENDED</u> (50-50)	<u>BLENDED</u> (2/3-1/3)	PROD. <u>ONLY</u>
A 80/160		800	560	640	320
B 40/160		400	360	373.33	320
C 20/160		200	260	240	320
D 19/160		190	255	233.33	320
E 1/160		10	165	113.33	320

P. 706 ¶ 1: Example - Calculations

160 acres, producing 1,600 bbl./d from 5 wells

Per producer: 320 bbl./d [each owner gets this]

Per acre: 10 bbl./d [each owner gets this, multiplied
by the number of acres they have]

=====

ASSUME we're looking at Owner A, owner of 80 ac.

If “blended” on a 1/3 – 2/3 basis (i.e., 1/3 per producer
+ 2/3 per acre), the calculation is as follows

$$320 \quad \times 1/3 = 106.67$$

$$800 \quad \times 2/3 = \underline{533.33}$$

$$640.00$$

Unitization

- *What's the conceptual difference between "Pooling" and "Unitization"?*
- =====
- **POOLING:** bringing together of small tracts or fractional mineral interests for the drilling of a single well in a single spacing unit
- **UNITIZATION:** the combining together of several producing leases and/or several wells over a pool of oil or gas to form one large "unit" (i.e., joint operation of all / some of a reservoir that is already producing)

Unitization – Gen'l. Comments

- While not required, unitization typically occurs in the context of “enhanced recovery” (a/k/a secondary or tertiary recovery), while pooling typically occurs when drilling the first well [1st difference]
 - Like pooling ... [4 similarities]
 - unitization can be compulsory or voluntary
 - voluntary unitization requires unanimous consent ...
 - compulsory unitization generates arguments about what’s “fair & reasonable”, and there’s often “one in every crowd”
 - compulsory unitization occurs after admin. process (e.g., application, hearing, and agency order) -- requires allocation of revenues and costs
 - BUT .. unlike pooling (based mostly on surface acreage, or combination of acreage and “per person” factors), unitization is more complicated – based on “operational / production” factors [listed on p. 753, 2nd and 3rd ¶s; AND p. 781 1st ¶]
- [2nd difference]

Unitization – Gen'l. Comments

- Having unit allows the wells to work together "as a team" to more efficiently produce O&G that would otherwise be unrecoverable
 - Some wells would be used as "injection" wells into which a substance would be injected to "push" previously unrecoverable quantities of oil and gas out of the other wells in the unit
 - Other wells would become "recovery" wells, from which the "pushed" production is removed from the field
 - Typical "5-spot" formation → "PRESSURE"

Unitization – Gen'l. Comments

- What this means ...
 - Each ownership percentage will be reduced (each producer now owns a smaller piece of a larger drilling unit)
 - Each party paid for oil and gas that would otherwise remain in the ground can now be produced and commercially used
- A field is not normally unitized until conventional methods of recovery have either been exhausted, or (more likely) become less efficient
 - thus it usually occurs some time after initial production from the field is obtained
- Compulsory unitization statutes (P. 752, FN 106)
 - 32 states have them; *TX does NOT*

Unitization – Gen'l. Comments

- Once unitization has been accomplished (whether voluntarily or forced), it's governed by a **Unit Operating Agreement** (similar to a Joint Operating Agreement)
 - pp. 754-755

Unitization

- And just to add to the confusion ...
- When you pool and when you unitize, you end up with “units”
 - Voluntary-pooled unit:
 - what results after voluntary pooling
 - Force-pooled unit:
 - results from a conservation agency order
 - Drilling unit (a/k/a spacing unit):
 - acreage assigned to a well that demonstrates that there's enough acreage to meet Rules 37 (spacing) & 38 (density)
 - Proration unit:
 - created under Rule 38(a)(2) → Special Field Rules
 - Production unit:
 - what results after unitization

Unitization – Gen'l. Questions

■ Who can unitize?

- Producers only? Anyone else?

■ Defining the Unit boundary –

- Include someone who doesn't want to be?
- Exclude someone who wants to be included?

■ The participation formula

- How to accommodate injection wells?
- Owner group vote “strategically” for favorable formula
 - State Agency “supposed to” review formulas
 - **BUT ...** encourage enhanced recovery, so review is sometimes cursory

Trees, p. 758 (not assigned)



- a “one in every crowd” case
 - ❑ i.e., the non-consenting owner to a proposed secondary recovery project
 - ❑ Trees operates 1 well in an area that CHK wants to waterflood ... doesn’t want to participate in the CHK / Anadarko / Oxy project
 - ❑ Chester **and** Morrow Formations



Trees (cont'd.)



■ Issues

- ❑ State statute re defn of “pool”
 - ❑ Were the unit participation factors fair and reasonable / adequately compensate owners?
 - ❑ Was inclusion of Trees’ tracts supported by substantial evidence?
 - ❑ Denial of motion to present supplemental testimony
- Good description of hrg. process: pp. 760-763
- P. 774 (1st 2 ¶s under II): what case is really about

Trees (cont'd.)

- **P. 781 N2**: curtailment orders issued by agency to “encourage” unitization
 - **Could such orders, especially those limiting production, cause producers (esp. those in need of revenues) to agree to a unitization allocation formula that they don’t like or that’s unfair? → see p. 782, 2nd ¶**
 - **TX (p. 782 N3): RRC Orders which “encourage” unitization**

Baumgartner, p. 784

- Who's suing whom, and what's the alleged bad behavior?
- Legal theories?
- What's the basis for the trespass claim?



Baumgartner (cont'd.)

- Water injection ... a “negative rule of capture”
- Overcome by the non-participating owner having a “fair opportunity” to participate
- What is a “fair opportunity”?
- Elements:
 - 1. equal share of production as the other participants
 - 2. equal share of costs on the same basis
 - 3. some supportable basis for those sharing mechanisms

Baumgartner (cont'd.)

- If an owner is NOT given any opportunity to participate, or if that opportunity is not a “fair opportunity”, what is that owner’s remedy?
- Will different terms ALWAYS be proof of an unfair opportunity?

QUIZ NEXT TUES. Feb. 11th –
Admin. / Logistics

- Will take the entire class session
- **Closed book**
- Combination of **short-** (fill in blank / M.C.)
and medium-answer (2-6 sentences)
- Anonymous: Number Sheet
- **Low tech: Bring one (or more)**
writing implements !!!

QUIZ NEXT TUES. Feb. 11th – *Substantive Matters*

- **Will cover all 7 classes we will have had**
 - Includes material in book / supp. cases / PPTs
- **Review Prob.**
 - Townships / Sections [CL 3]
 - Pooling Calculation [CL 5]
 - Vocab Terms [through tonight (CL 6): 33 terms]
 - POSTING?

Next Class (TH 2/6) ...

- CL 7 in Syllabus
- RoC: Regulatory Responses (4 of 4)
- pp. 631 – 647 AND 674 – 685

NOTE TO ME ...

- In 2014, CL 5 was cancelled for weather ...
- ... **AND** in the re-scheduled CL 5 (held on the date CL 6 should've been held), the projector failed ...
- ... **T/F**, here in CL 6, I had to go back over the Vol. Subd. Problems and the Pooling Calculation Example from CL 5 (these are contained in SL 2-8)
- **NORMALLY ...** I won't include them here in CL 6