

Oil & Gas Law

Class 7:

**RoC: Regulatory Responses (4 of 4) –
Municipal Regulation +
Ops. / Prod. / Mktg.**

Regulating Production

- 2 caveats
- **First:** Understanding regulation of production typically requires some knowledge of engineering and technical subjects, and of economics
- **Second:** **NOT !!!**

MER and Mkt. Demand Proration – 1

- 2 types
 - Maximum Efficient Recovery (“MER”) – engineering studies determine the amount the field can produce most efficiently [results in an “allowable” (Wronski)]
 - Market-Demand – less than MER, it’s the amount that the market is demanding at the prevailing price
- Mkt. Demand Proration created in 1930s
 - E. TX Oil Field discovered – sharp increase in supply when demand was declining
 - Strengthened by 1935 Federal law – prohibited transport in interstate commerce of oil produced in excess of amounts permitted by state law
 - Depending on who you ask, Market-Demand Prorationing results either in price stability, or artificially high prices

MER and Mkt. Demand Proration – 2

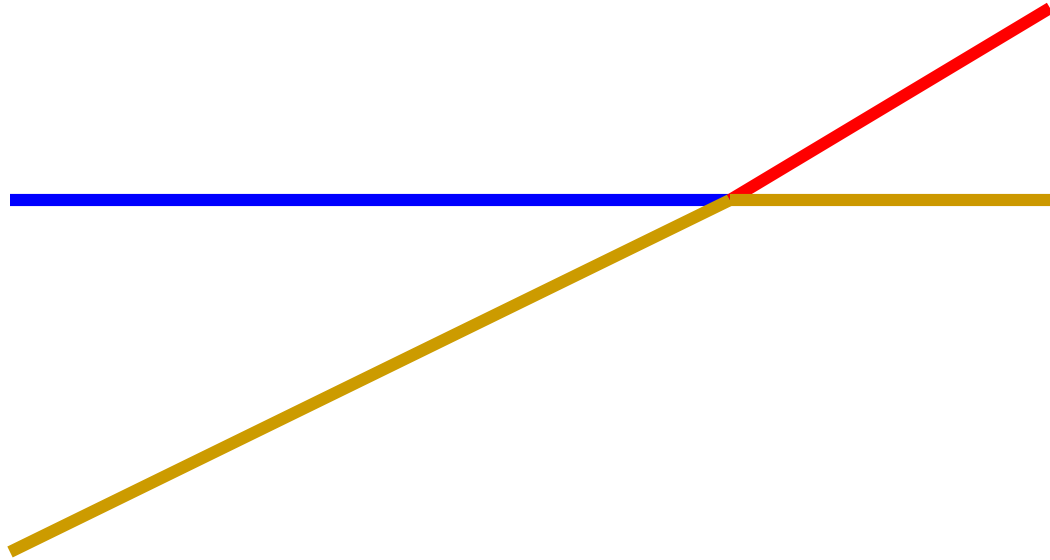
- MER allowables more prevalent when demand exceeds production (supply) → market wanting more than field can efficiently produce
 - Ex: WW II; 1970s - 1980s
 - Producing “full out” could damage field and reduce total recovery
- Today, Mkt. Demand limits are typically set at 100% of MER and wells produce as much as they efficiently can / as much as operators want
- BUT ... mechanism / regulations are still in place if future circumstances require

MER and Mkt. Demand Proration – 3

■ **MER**



■ **Mkt-
Demand**



Pickens v. RRC

- *What is the RRC trying to determine?*
- *Is the issue whether RRC was right, or whether RRC was reasonable?*
- Formula for determining production rate for allowables in a field
 - ❑ The 50-50 formula using both surface acreage and underground productive zone
 - ❑ **CT**: whether the RRC order was supported by substantial evidence (if not, deemed as arbitrary and capricious, and t/f, reversible)
 - ❑ A classic “battle of the expert witnesses” case

Range Resources

- *What are the producers' claims?*
- *What are the Town's primary contentions on appeal?*
- *How did the Court rule and why? (2 reasons)*
- NOTE: December 2013, PA Sup. Ct. ruled that local governments can use zoning laws to restrict drilling within their borders

Municipal Regulation of O&G

- State: **primary jurisdiction** over O&G
- Local: **additional jurisdiction** over O&G w/in its borders
 - Creates **possibility of overlapping, perhaps inconsistent, regulation** – esp. where city / county regulates, limits, restricts or outlaws actions that State would otherwise allow
 - Conflicting regulatory requirements – reflect the underlying reality of **divergent interests / goals**
 - State: production = \$; City: = ↓ prop. values, ↑ noise etc.

Municipal Regulation of O&G

- **TX:** 1944 Galveston appellate case supported by 1982 Ft. Worth appellate case
 - RRC's jurisdiction **DOES NOT** preempt cities from passing their own regulatory requirements
 - Cities have broad powers and legal autonomy
- **OK:** 1933 – US Sup. Ct. upheld OKC ordinance requiring drillers to post \$200,000 bond before drilling well inside city limits
 - “room for debate”; t/f, won't substitute its judgment for that of local officials
 - other drillers could, and did, meet requirements
 - city: protect safety and general welfare

Municipal Regulation – Issues (1)

- Constitutional taking?
 - 14th Amend. Due Process / Equal Protection claims
 - Prohibited activity increases production / avoids waste
 - Complete limit on property use, or partial?
 - Ordinance is probably defensible if it:
 - doesn't govern matters preempted by the State Agency
 - is validly enacted
 - advances a legitimate governmental interest
 - is substantially related to protecting the public's safety and general welfare
 - is NOT arbitrary or discriminatory
- Statewide uniformity of operating requirements

Municipal Regulation – Issues (2)

- Scope: Total ban vs. regulating certain aspects?
- [like RoC...] Can local gov't. pass ordinance / bring suit to limit O&G activities outside its boundaries that have EFFECTS inside?
- Annexation – city acquires land, then imposes city laws on it; land use pre- or post-annexation

Municipal Regulation of O&G

- **EX:** Town of Flower Mound, TX (pop. 66,000)
 - One of the most stringent ordinances in TX (2003)
 - 500' from lease line OR lot/tract boundary (vs. RRC S.F.R. 330' and 20 ac.)
 - 500' from street; 1,000' from home or park
 - Env. limits – special pollution prevention controls, env. insurance coverage, 500' setback from designated “Environmentally Sensitive Areas”

Examples

- El Centro Oil Co. and Lasker E&P Inc. both want to drill wells within the city limits of Emerald City, TX
- *Valid for EC to pass a city ordinance ...*
- *... prohibiting all O&G drilling / production in city limits?*
- *... prohibiting all O&G drilling / production inside city limits and within ½ mile outside city limits?*
- *... prohibiting all O&G drilling / production in city limits by companies whose name starts with L?*
- *... requiring all companies wanting to drill / produce within city limits to (a) file a map, (b) disclose all technical info and (c) submit a \$10 million bond?*

NEXT WEEK...

■ **QUIZ ON TUESDAY**

- ❑ **Bring 1+ writing implements !!!**
- ❑ **Remember the number YOU selected !!**

■ =====

■ **Thursday, 2/13:**

- ❑ Oil & Gas Lease (1 of 7)
- ❑ Ch. 2 Sec. A and B1-3: **pp. 176 – 203**
- ❑ Ch. 3 Sec. E1: pp. **484 – 498**