FORCED POOLING IN TEXAS
THE MINERAL INTEREST POOLING ACT
WHEN CAN I USE IT AND HOW DOES IT WORK?

Presented by

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Tab H
# FORCED POOLING IN TEXAS

## THE MINERAL INTEREST POOLING ACT

### WHEN CAN I USE IT AND HOW DOES IT WORK?

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FORCED POOLING IN TEXAS
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I. INTRODUCTION.

The Mineral Interest Pooling Act (MIPA)\(^1\), which became effective on August 29, 1965,\(^2\) is one of the more complicated statutes to understand and even more difficult to apply. Undoubtedly because of the relatively few times the MIPA has been invoked, many experienced landmen, geologists, engineers and lawyers may assume that forced pooling is not an available remedy in Texas.\(^3\) Indeed, only 102 forced pooling applications have been granted in the statute’s 44 year history out of the 248 that have been filed through 2010 as shown on the tabulation attached to these materials.

II. HISTORICAL BACKGROUND.

Since the mid-1930s, noted commentators Robert Hardwicke\(^4\) and A.W. Walker\(^5\) have detailed the abuses resulting from small tract drilling and the need for a compulsory pooling law in Texas.\(^6\) Forced pooling statutes were first adopted by Oklahoma and New Mexico in 1935\(^7\) and became an integral part of the conservation law in those states.

Texas, however, was the home of the wildcatter and small tract driller. With allowable allocation formulae based upon 1/3 per well, 2/3 acreage in gas fields (1/3 - 2/3 formula) and 50% per well, 50% acreage for oil reservoirs (50/50 formula), small tract drilling was not only authorized but encouraged because small tract wells received disproportionately large allowables as compared to wells on larger tracts of the size required by field rules. See Stanolind Oil & Gas Co. v. Railroad Commission, 96 S.W.2d 664 (Tex. Civ. App.—Austin 1936, no writ), where the value of the oil underlying the tract in question was $2,500 and the cost to drill the proposed well was $10,000; Halbouty v. Darsey, 326 S.W.2d 528 (Tex. Civ. App.—Austin 1959, writ ref'd n.r.e.), where the gas and condensate reserves underlying the drillsite were valued at $20,000 and the cost to drill the well was $250,000; Atlantic Refining Company v. Railroad Commission, 330 S.W.2d 494 (Tex. Civ.

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\(^1\)Chapter 102 of the Texas Natural Resources Code (Code). All statutory citations in this paper shall refer to the MIPA unless specifically noted to the contrary.


\(^3\)The availability of forced pooling pursuant to Chapter 102 of the Code must not be confused with the statute which prohibits the compulsory joinder of a secondary or enhanced recovery unit formed pursuant to Chapter 101 of the Code.


\(^6\)For an excellent discussion of the historical background to the MIPA, see Smith, Ernest E., The Texas Compulsory Pooling Act, 43 Tex. L. Rev. 1003 (1965), referred to herein as the “Smith I Article.”

\(^7\)Id. at 1004.
Even though compulsory pooling bills were introduced before each session of the Texas Legislature for years, enacting a force pooling statute was not politically feasible until the Texas Supreme Court handed down the Normana decision on March 8, 1961. Atlantic Refining Co. v. Railroad Commission, 346 S.W.2d 801 (Tex. 1961). At issue in Normana was the validity of the 1/3 - 2/3 formula that the RRC had historically adopted for gas fields. In this case, Atlantic showed that under the 1/3 - 2/3 formula, the lessee of a 0.3 acre tract with only $7,000 worth of gas in place could produce $2-1/2 million worth of gas over 20 years. The court held this allocation formula unconstitutional and thereby removed the incentive for small tract owners to oppose the passage of a forced pooling law. This result was emphasized when the same court struck down the 50/50 formula for oil allowables three years later in Railroad Commission v. Shell Oil Company, 380 S.W.2d 556 (Tex. 1964).

Following these decisions, the small tract owners and independent producers who had historically been the strongest opponents of compulsory pooling became some of its leading advocates. Smith I Article at 1007. As a result, the Texas Legislature enacted in August of 1965 what was originally codified as TEX. REV. CIV. STAT. ANN. art. 6008c (1965). This statute was recodified as Chapter 102 of the Code in 1997.

III. PREREQUISITES FOR INVOKING THE MINERAL INTEREST POOLING ACT. §§ 102.003, 102.004, 102.011, 102.013.

The following checklist is set forth to determine whether the MIPA may be invoked:

A. Discovery Date of Field. In accordance with § 102.003, the provisions of the MIPA do not apply to any reservoir discovered and produced before March 8, 1961, the date of the decision by the Texas Supreme Court in Atlantic Refining Co., supra. An easy preliminary step is to check the RRC's discovery date for the field in question. But the statute's requirement that the reservoir must have been "produced" before the cut off date may necessitate further inquiry as to the date of the first production from the field if the discovery date is close to March of 1961.

B. Existence of a Field. There must be an existing RRC designated field into which the applicant seeks to force pool his interests. Significantly, this requirement means there cannot be force pooling in a wildcat zone or well. § 102.011.

C. Special Field Rules. The RRC must have adopted special field rules, on either a temporary or permanent basis, for the field in question before the force pooling application can be approved. § 102.011. If the field is operated pursuant to statewide rules, the force pooling applicant may apply to the RRC to establish special field rules for the reservoir as a prerequisite to force pooling. Because of
the time required to force pool, the RRC will permit an applicant to combine an application for special field rules with the pooling application. This approach could cause the application to be denied if the RRC adopts special field rules which conflict with the density the applicant assumed would be applicable in making the required voluntary offer to pool prior to filing the force pooling application. But the RRC has accepted offers, as discussed below, to pool based upon a stated size of unit, or in the alternative, a unit size in conformity with the field rules that will be established in conjunction with a force pooling application.

D. State Lands.

1. The provisions of the MIPA do not apply to land owned by the State of Texas or to land in which the State of Texas has a direct or indirect interest. But with the approval of the Commissioner of the General Land Office, or any board or agency having jurisdiction over the state lands in question, the state's interest may be pooled under the provisions of the MIPA. § 102.004.

In Oil & Gas Docket No. 03-262001, Application of George L. McLeod, Inc. Pursuant to the Mineral Interest Pooling Act for a Pooled Unit for the Milagro Exploration, L.L.C. Cockburn Yegua Well No. 1, Magnet Withers (Martinez Sand) Field, Wharton County, Texas, the Commission dismissed McLeod’s Application because the applicant did not have the State’s consent to the force pooling action.

McLeod filed the Application with the Commission to force pool a portion of the Milagro Cockburn Lease with the adjoining McLeod lease to form a pooled unit under the MIPA. Before the Application went to hearing, Milagro petitioned the School Land Board, pursuant to Section 52.076 of the Natural Resources Code, to authorize the pooling of a portion of the Milagro lease acreage with the adjoining unleased Colorado Riverbed acreage for the formation of a 441 acre unit. The SLB agreed resulting in Milagro and the State executing an agreement pooling a portion of the acreage covered by the Milagro lease with approximately 13 acres of the Colorado riverbed acreage. Thereafter, Milagro filed a motion to dismiss the McLeod Application on the grounds that McLeod was seeking to force pool acreage in which the State had an ownership interest, or acreage in which the State at least had either a direct or indirect interest under the pooling agreement, which required the State’s consent that McLeod did not have. Milagro also argued, relying on the court’s decision in the Buttes Resources case discussed at XI. C., that Milagro had a constitutionally protected, vested property right to do anything it wished with its property, including contracting and pooling interests with other parties, up until the Commission issued a final order in the MIPA.

McLeod made a number of arguments including that it was not proposing to force pool the State’s riverbed and the State did not have an interest because there was no cross conveyance of interests between the State and Milagro.
under the agreement. McLeod also argued that its MIPA Application was filed with the Commission before the SLB approved the 441 acre pooled unit that included the State’s riverbed acreage and therefore should take precedence over the SLB pooling agreement.

The Commission found that the agreement did effect a cross conveyance of ownership interests throughout the entire unit acreage including that acreage McLeod sought to force pool. The Commission also concluded that because the State’s participation in production would be reduced if the force pooling were granted, the State had either a direct or indirect interest in the lands requiring McLeod to have the State’s consent to the force pooling. Because McLeod was unable to obtain the State’s consent the Commission dismissed the application for want of jurisdiction under Section 102.004 of the MIPA.

2. The RRC has ruled that school district lands are not within this exemption or prohibition on the basis that a school district is a political subdivision, not a board or agency of the State. Application of Southwest Minerals, Inc., League City Townsite (Andrau, U.) Field, Galveston County, Texas, Oil & Gas Docket No. 3-81,363.

3. Section 52.076 of the Texas Natural Resources Code authorizes the School Land Board (SLB) to "pool or bring an action to force pool unleased riverbeds and channels." § 52.076(a)(4). The SLB has exercised this power to pool unleased riverbeds in numerous cases and also authorized an action to force pool unleased riverbed acreage into an adjacent producing unit on at least one occasion.8 The SLB’s willingness to exercise the powers afforded by this statute provides incentive for state lesses to include riverbed acreage in their production from, and development of, adjacent lands.

E. Two or More Tracts. To force pool, there must be two or more separately owned tracts in the common reservoir. § 102.011. An undivided interest owner in a single tract, who would otherwise enjoy the position of a co-tenant without a risk penalty, may not be force pooled if the application only involves that single tract.

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8 Oil & Gas Docket Nos. 03-0231332 and 03-0231333; Applications of Long Run Oil Company and Powers Mineral Group, Inc. for a Pooled Unit pursuant to the Mineral Interest Pooling Act for the Tri-C Resources, Inc., Governor Bill Daniels Well Nos. 1 and 2, Moss Bluff, North (Yegua EY-4) Field, Liberty County, Texas involved agreements between the applicants and the State to pursue pooling the unleased river bed tracts that adjoined Tri C’s Daniels lease.
1. A leases from a cotenant owning 75% of mineral interest and B leases remaining 25%. A drills a well on the tract and then seeks to force pool B's interest and invoke the maximum risk penalty provided by the MIPA. The RRC has no jurisdiction to consider A's application because there are not two or more separately owned tracts. Application of J.M. Huber Corporation, Calvin (Dean) and/or Calvin (Spraberry) Fields, Reagan County, Texas, Oil & Gas Docket No. 7C-82,646.

2. The existence of a voluntarily pooled unit covering the same acreage as the proposed force pooled unit does not negate separate ownership. If some tracts in the unit contain unpooled interests that are not present in other tract(s) in the unit, the requirement of two or more separately owned tracts is satisfied. Application of H.S. "Gus" Edwards, Prudence (Atoka) Field, King County, Texas, Oil & Gas Docket No. 8A-75,286; Application of BTA Oil Producers, Howe (Atoka) Field, Ward County, Texas, Oil & Gas Docket No. 8-76,365.

F. Common Reservoir. Under the MIPA a forced pooling application applies to a "common reservoir." § 102.011. The RRC has interpreted this term "common reservoir" to include those reservoirs regulated as a common reservoir pursuant to the RRC’s authority in §§ 86.012 and 86.081 of the Code even though such reservoirs are separate accumulations of oil or gas and are not in natural communication within the interval recognized by the RRC as the field. The Texas Supreme Court upheld this interpretation in Railroad Commission v. Pend Oreille Oil & Gas, 817 S.W.2d 36 (Tex 1991).9

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9 In Railroad Commission v. Bishop Petroleum, 736 S.W.2d 724 (Tex. App.—Waco 1987), aff’d in part and rev. in part, 751 S.W.2d 485, issued before the Pend Oreille decision, the Waco Court of Appeals in a matter of first impression reasoned that the RRC had no authority under the MIPA to pool separate reservoirs regulated as a “common reservoir” under sections 86.012 and 86.081 of the Code. Nevertheless, the Court upheld the RRC’s pooling decision because of the failure of Bishop to preserve error with respect to the RRC’s authority to pool stratigraphic, lenticular reservoirs within the field that were not in natural communication.
G. **Existing or Proposed Well.** At least one of the owners of the right to drill must have either drilled or proposed to drill a well on the existing or proposed proration unit to the reservoir in question before the MIPA may be invoked. § 102.011. Thus, a royalty owner could not bring a forced pooling action involving a proposed well.

H. **Size Limitations.** The forced pooled unit must contain the "approximate acreage" of the standard proration unit established by the special field rules. § 102.011.

1. The field rules in effect at the time of the RRC's order establishing the force pooled unit control the permissible size of the unit with the exception authorized by § 102.014. See IX, below. Application of Panola Production Company, Carthage (Cotton Valley) Field, Panola County, Texas, Oil & Gas Docket No. 6-75,587.

2. The forced pooled unit may not exceed 160 acres for an oil well and 640 acres for a gas well plus 10 percent tolerance. § 102.011. The oil unit size limitation is particularly troublesome if the MIPA application involves a horizontal well. Both Statewide Rule 86, which governs horizontal wells, and special field rules adopted for horizontal wells in certain fields, provide for oil proration units substantially larger than 160 acres and gas proration units considerably larger than 704 acres. The drafters of the MIPA obviously did not contemplate, when the law was enacted in 1965, well spacing/density rules needed for horizontal wells and the larger drilling and proration units they require.

3. All the acreage in the forced pooled unit must be productive. See VIII below. As a result of this requirement, the RRC will determine the productive acreage of the lands making up the existing or proposed proration unit involved.

I. **Statutory Purposes.** The RRC may order force pooling only for the purposes of a) avoiding the drilling of unnecessary wells, b) protecting correlative rights, or c) preventing waste. § 102.011. Almost no applications are for the purpose of preventing waste. Applicants normally allege that relief under the MIPA is needed to protect correlative rights and to prevent the drilling of unnecessary wells. Protecting correlative rights can involve either giving applicants the opportunity to receive a fair share of their reserves if they cannot drill and develop their acreage or to participate in reserves that are being drained and produced by others.

J. **Voluntary Offer to Pool.** See VII, below. The MIPA requires, as a jurisdictional prerequisite to invoking RRC jurisdiction, that the force pooling applicant make a fair and reasonable voluntary pooling offer to all interest owners within the existing or proposed proration unit that is the subject of the application. § 102.013. The Texas statute is unique in this regard. Unlike the force pooling statutes in other jurisdictions, Texas does not allow the RRC to invoke the MIPA on its own initiative. In addition, the proponent of pooling must first exhaust reasonable, good faith
efforts to pool voluntarily before the RRC can order pooling. Smith I Article at 1009.

IV. PARTIES AUTHORIZED TO BRING A FORCE POOLING ACTION. § 102.012.

A. Authorized Force Pooling Applicants. The following interest owners are granted standing to apply to the RRC for the pooling of mineral interests:

1. The owner of any interest in oil and gas in an existing proration unit;
2. With respect to a proposed unit,
   a. the owner of any working interest, or
   b. any owner of an unleased tract other than a royalty owner.\(^{10}\)

B. Statutory Construction Problem. The re-codification of the MIPA into the Natural Resources Code created a statutory construction problem. The statutory requirement has been interpreted as it is organized above, but the provisions of the MIPA were re-arranged inadvertently when it was re-codified into the Code in a way that conflicts with the original enactment and would render part of the provision meaningless. § 102.012 in the Code reads:

   § 102.012. Owners Authorized to Apply for Pooling

   The following interested owners may apply to the commission for the pooling of mineral interests:

   (1) the owner of any interest in oil and gas in an existing proration unit or with respect to a proposed unit;
   (2) the owner of any working interest; or
   (3) any owner of an unleased tract other than a royalty owner.

The literal language of Section 102.012(1), which uses the same wording but is organized differently from its predecessor statute before re-codification into the Code, grants standing to any mineral interest owner in an existing or proposed proration unit. Such an interpretation not only conflicts with the original statute, but renders meaningless the wording in Section 102.012 (2) and (3).

\(^{10}\)While the language used above is virtually identical to the wording in Section 102.012, the organization of this language is different and tracks more closely § 102.012's predecessor statute, art. 6008c, § 2(a), Tex. Rev. Civ. Stat. Ann. (1965). This difference in organization of the wording allows the argument for a different interpretation regarding which parties have standing to bring an MIPA action.
Operator X forms a voluntary unit consisting of Tracts A through E. Sections 102.012(2) and (3) clearly grant the lessee or an unleased mineral owner in Tract F standing to seek force pooling. A royalty owner in Tract F, however, has no standing to invoke the MIPA. See Application of the Wilson Heirs, M Half Circle (10,200) Field, Jefferson County, Texas, Oil & Gas Docket No. 3-79,584, where the examiners recommended the result suggested above. Because the applicant/royalty owners withdrew their MIPA application prior to the commissioners' signing a final order, the value of this case is merely instructive as to a likely ruling in a similar case but is not precedent.

C. Distinction Between Existing and Proposed Proration Units. The distinction between an existing and proposed proration unit is important. See VI, below, where this distinction is illustrated and explained. Any mineral interest owner in an existing proration unit has standing to bring a force pooling action. If, however, the action involves a proposed proration unit, then only a working interest owner or unleased mineral owner (not a royalty owner) has standing to bring the application. § 102.012.

D. School Land Board Standing to Force Pool Riverbeds and Channels. As noted above, the Texas Legislature has specifically authorized the SLB to force pool unleased riverbeds and channels. § 52.076(a)(4), Code. The amendment is limited in its scope to riverbeds and channels and does not apply to fee acreage or Relinquishment Act lands.

V. REQUIREMENTS FOR NOTICE OF MIPA HEARINGS. § 102.016.

At least thirty days notice of the MIPA hearing must be given to all interested parties.

A. Actual Notice Sufficient. An application will not be dismissed for defective notice if the protestant received actual notice of at least 30 days before hearing and fails to demonstrate surprise. Application of W.H. Mengden, Dyersdale N. (Y-5) and
B. **Legal Description Not Required.** Neither the MIPA application nor the notice of hearing is required to contain a legal description of the property to be pooled that satisfies the requirements of the statute of frauds. Application of Jordan Engineering, Inc., Bryan (Woodbine) Field, Brazos County, Texas, Oil & Gas Docket No. 3-79,474. The RRC may include a plat showing the existing and proposed units as part of its notice of the hearing.

C. **Notice to Royalty Owners Within Existing Units.** Notice must be given all royalty owners in the existing voluntarily pooled unit unless the operator has actual authority to represent them. In at least one case, the applicant could not rely on the representation of the operator as to its authority to waive notice to the royalty owners. Application of Southwest Minerals, Inc., League City Townsite (Andrau, U.) Field, Galveston County, Texas, Oil & Gas Docket No. 3-81,363.

VI. **DISTINCTION BETWEEN EXISTING AND PROPOSED PRORATION UNITS.**

As pointed out above, the distinction between an existing proration unit and one that is proposed can be dispositive in determining those parties that would have standing to force pool, which parties are entitled to notice of the hearing, and perhaps in assessing whether a voluntary pooling offer is "fair and reasonable."

![Figure 3](image)

Operator X pools Tracts A-D; Tract C, however, contains an undivided mineral interest leased to Y that is not pooled. Whether Y or Y's royalty owner seeks to force pool, the unit's geographic boundaries will not change. This is an example of an *existing* proration unit.
VII. REQUIRED VOLUNTARY POOLING OFFER. § 102.013.

A. **Unique Requirement.** The voluntary pooling offer requirement is a unique feature of the MIPA and distinguishes this statute from most states' force pooling laws. Smith I Article at 1009.

B. **Jurisdictional Prerequisite.** The making of an offer to pool voluntarily is a jurisdictional prerequisite to invoking the MIPA. If the voluntary offer is not fair and reasonable, the RRC must dismiss the pooling application for want of jurisdiction. § 102.013(b).

C. **Elements.** What is a fair and reasonable offer to pool?11

   1. In *Carson v. Railroad Commission*, 669 S.W.2d 315,316 (Tex. 1984), the Texas Supreme Court, while declining to define precisely what constitutes a fair and reasonable offer, held:

   [t]he offer must be one which takes into consideration those relevant facts, existing at the time of the offer, which would be considered important by a reasonable person in entering into a voluntary agreement concerning oil and gas properties.

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11Many of the citations in this paper are to RRC decisions in prior MIPA proceedings along with court decisions. The previous RRC rulings are not entitled to the same precedential weight as a court decision. They may be reversed or modified by new commissioners receiving recommendations from different examiners. These agency decisions are included to provide guidance as to prior RRC rulings but should not be conclusively relied upon for cases involving different facts or even substantially similar facts presented to different commissioners.
2. Unfair and Unreasonable Offers.

a. Until recent times, an offer to lease or farm-out was not considered an offer to pool. In the last three years, however, with cases arising in the Newark, E. (Barnett Shale) Field involving town lots and offers to home owners, the Commission has accepted for MIPA purposes offers that include alternative proposals to pool as working interests, or to lease or to farmout the town lots. See Section XVIII. below.

b. An offer to pool unpooled drllsite royalty interests in an existing proration unit on the same basis that all other owners in the unit were pooled and participating (surface acreage) was held not to be fair and reasonable, at least when the offer was made after the well had been drilled. *Carson v. Railroad Commission*, 669 S.W.2d 315 (Tex. 1985). The supreme court, in a 9-0 decision, reversed the RRC, the Ward County District Court and the El Paso Court of Appeals.

c. An offer to participate in eight proposed wells on an all-or-none basis was not fair and reasonable. *Windsor Gas Corporation v. Railroad Commission*, 529 S.W.2d 834, (Tex. Civ. App.—Austin 1975, no writ).

d. A voluntary pooling offer to pool acreage is not fair and reasonable, even though the acreage to be pooled and the target well are in the same field, if the well produces from a different reservoir than where the applicant’s acreage is located and the well cannot drain the offeror’s acreage without being reworked. *Oil & Gas Docket No. 3-85,139, Application of Broussard-Hebert for a MIPA Unit for the Prudential Drilling No. 1 Well, Elwood (Vicksburg) Field; Railroad Commission v. Broussard*, 755 S.W.2d 951 (Tex. App.—Austin 1998, writ denied).

e. For a proposed dual completion well, the applicant’s (i) failing to include a provision for apportionment of costs or ownership as between the two prospective zones and (ii) attaching a blank form joint operating agreement to the voluntary pooling offer made the offer incomplete and unreasonable. Application of Walter H. Mengden, Sr., Dyerdale, North (Y-5) Field, Harris County, Texas, Oil & Gas Docket No. 3-87,031.

3. Fair and Reasonable Offers.

a. An offer to pool may be fair and reasonable even though it did not include an offer to pay a risk penalty. *American Operating Company v. Railroad Commission*, 744 S.W.2d 149 (Tex. App.—
An offer to pool made after the MIPA application is filed but before the hearing was not unfair and unreasonable merely because of timing. Application of Andromeda Enterprises, Inc., Personville, N. (Cotton Valley Lime) Field, Limestone County, Texas, Oil & Gas Docket No. 5-82,383; Application of J.L. Schneider, Jr., Alvin, North (8550') Field, Brazoria County, Texas, Oil & Gas Docket No. 3-77,898.

c. Pooling offers proposing to pool acreage, all of which was not productive, were not necessarily unfair and unreasonable, where there was a reasonable explanation for doing so.

1. A pooling offer that followed lease boundaries in describing the proposed unit by metes and bounds and thereby included a small amount of nonproductive acreage that was in the vicinity of a field bounding fault was held to be fair and reasonable as a voluntary offer because the RRC would determine the productive limits as part of the MIPA case. American Operating Company v. Railroad Commission, supra;

2. A pooling offer to pool down-structure acreage in a water drive reservoir with acreage upstructure is not unreasonable merely because at the time of the hearing all of the down-structure acreage included in the offer is no longer productive and cannot be force pooled. Application of J.L Schneider, supra; Buttes Resources v. Railroad Commission, supra.

d. The fact that the target well is not and cannot drain the exact acreage tendered for forced pooling does not make an applicant’s pooling offer unfair or unreasonable as long as the subject well is capable of draining the equivalent size unit proposed for pooling. Oil & Gas Docket No. 5-81767, Application of Walter Farrington et. al. for a MIPA unit, Donie (Pettit) Field, Freestone County; Railroad Commission v. Bishop Petroleum, supra at note 9.

e. An offer by an owner of a royalty or any other interest within an existing proration unit to share on the same yardstick basis as the other owners within the unit are then sharing is deemed fair and reasonable by statute. § 102.013 (c). But see Carson, supra, where the supreme court did not apply this statutory provision to a
drillsite royalty owner in an existing producing unit when the voluntary offer was made after production had commenced.

f. An voluntary offer to pool undivided, unpooled non-drillsite interest into an unit with 4 producing wells is not unfair and unreasonable for MIPA offer purposes merely because the Commission is limited to force pooling for one well on a proration unit. Oil & Gas Docket No. 06-0245016, Application of Patricia C. Nowak for Formation of a Pooled Unit, Proposed Waldrop Gas Unit 1-A, Carthage (Cotton Valley) Field, Panola County, Texas.

D. Recipients of Voluntary Offer. The voluntary offer must be made to the interest owners in the existing or proposed proration unit that is the subject of the MIPA application.

1. An offer needed only to be made to those owners whose consent was necessary to pool the other mineral interests, e.g., an operator who has the power under an operating agreement to pool non-operators' interests or a lessee with pooling authority under its lease. Application of Iverson Exploration, Inc., JKT (Canyon) Field, Schleicher County, Texas, Oil & Gas Docket No. 7C-79,134; Application of Pantera Petroleum Company, Del Mar (Lower Hirsch) Field, Webb County, Texas, Oil & Gas Docket No. 4-83,648.

2. An offer made to the working interest owners in an existing unit was sufficient and did not need to be made to the royalty owners directly. The lessee who accepted the offer had the duty to seek the agreement of its royalty owners. Application of Panola Producing Company, Carthage (Cotton Valley) Field, Panola County, Texas, Oil & Gas Docket No. 6-75,587.

3. Where the operator refused the voluntary pooling offer, there was no requirement that the applicant make the pooling offer to other owners in the unit even though they were not represented by the operator. Buttes Resources Company v. Railroad Commission, 732 S.W.2d 675 (Tex. App.—Houston [14th Dist.] 1987, writ ref’d n.r.e.). The refusal by one of the necessary parties for voluntary pooling was sufficient to permit invoking the MIPA.

E. Timing of Voluntary Offer. The timing of a voluntary offer to pool can be important.

1. Whether the offer is extended before or after the adoption of special field rules is important. If before, the applicant risks that the RRC will adopt special rules contrary to the density assumed in making the voluntary offer, thereby jeopardizing whether the RRC would deem such offer to be fair and reasonable.
2. Whether the offer is made before or after the drilling of the well for the proration unit involved is also very important. See Carson v. Railroad Commission, 669 S.W.2d 315 (Tex. 1984), where the Texas Supreme Court held that a voluntary offer to pool royalty interests in the drillsite tract was not reasonable when the well had already commenced producing on an existing unit. The court indicated, however, that this same offer may have been fair and reasonable if made before the unit well was drilled because the unit well might not be drilled on the royalty owner/offeree’s tract.

3. Prior to the Texas Supreme Court's decision in Carson, the statute appeared to define clearly what constituted a fair and reasonable voluntary offer to pool in an existing proration unit. See § 102.103(c). The Carson decision, however, has clouded when a yardstick basis pooling offer deemed fair and reasonable by the MIPA will be determined to be fair and reasonable by the RRC or the courts.

F. Court Standard for Review of Voluntary Offer. For a period of time, the appellate courts were in a quandary concerning the proper legal standard or basis for reviewing the RRC's determination that an applicant's voluntary pooling offer either was or was not in compliance with MIPA. The Texas Supreme Court created this uncertainty with its statement in Carson, 669 S.W.2d at 316, that whether an offer to pool is fair and reasonable "is not a substantial evidence review . . . it is a jurisdictional review." § 2001.174 of the APA, however, provides for a "substantial evidence" review of RRC orders. Because the Carson case expressly set out that the proper review of this issue was not substantial evidence, but also stated explicitly that the relevant facts must be considered, several appellate courts had been uncertain as to what standard to apply. See Railroad Commission v. Broussard, 755 S.W.2d 951 (Tex. App.--Austin 1988, writ denied).

This confusion seems to have been cured by the supreme court's opinion in Railroad Commission v. Pend Oreille Oil & Gas Company, Inc., 817 S.W.2d 36 (Tex 1991). The court stated that a fair and reasonable voluntary offer is jurisdictional for the RRC to act, but that the courts must apply the substantial evidence rule under the APA to determine if the RRC's conclusion in this regard is reasonable. In distinguishing its earlier pronouncement in Carson, the court noted that "jurisdictional review" was limited to the narrow issue presented in Carson, i.e., whether an offer to participate on the same yardstick basis is always a fair and reasonable offer as a matter of law.

VIII. ACREAGE SUBJECT TO FORCE POOLING. § 102.018.

One of the MIPA's requirements that often adds to the complexity and time to process a forced pooling application is the acreage which may comprise a forced pooled unit.

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12Administrative Procedure Act, Chapter 2001 et. seq., TEX. GOV'T CODE (Vernon Supp. 2008), referred to herein as the "APA."
A. **Productive Acreage at Time of Order.** Section 102.018 provides that the RRC shall pool only the acreage which is productive as of the time of its order. At least one court, however, has ruled that it is sufficient for the RRC to pool the acreage shown to be productive by the evidence offered in the hearing even though such evidence may be out of date at the time of the final order. Application of J.L. Schneider, *supra*; *Buttes Resource Company v. Railroad Commission, supra*. In Schneider, the RRC ordered force pooling establishing a pooled unit that was smaller than the unit proposed in the voluntary pooling offer. The RRC under § 102.018 is limited to pooling only the acreage that at the time of its order "reasonably appears to lie within the productive limits of the reservoir." In Schneider, the reservoir producing mechanism was a water drive, which with the upstructure producing well of Buttes was continually changing and reducing the productive limits of the reservoir. Buttes argued that the RRC had in effect to update the evidence of the productive limits of the reservoir before ordering pooling because a year lapsed from the date of the hearing to the date of the order. The RRC declined to do so and the Court of Appeals in Buttes upheld the RRC decision.

B. **RRC Determination of Productive Acreage.** Because of the productive acreage requirement, most force pooling hearings at the RRC require the agency's determination of productive acreage within the proposed unit. The standard for MIPA proceedings conflicts with normal productive acreage determinations because of the MIPA's requirement that the compulsory unit be composed of acreage that is currently, as distinguished from originally, productive. Application of J. L. Schneider, Jr., *supra*.

IX. **PRODUCTIVE ACREAGE EQUAL TO STANDARD PRORATION UNIT ("MUSCLE-IN")** § 102.014.

A. **Generally.** Section 102.014(a) prohibits the forced pooling of a tract the productive acreage of which is "equal to or in excess of the standard proration unit for the reservoir," unless the MIPA applicant has adjoining productive acreage that is smaller than such standard unit and the applicant has not been afforded a reasonable opportunity to pool voluntarily. Thus an applicant who owns productive acreage equal to the standard unit size prescribed by field rules would be required to drill its own well and would not be allowed to force pool into another's proration unit.

B. **Larger Allowable Authorized for a “Muscle In”.** For the owner of a tract smaller than the standard proration unit who has not been given the opportunity to pool, the Commission will allow that owner to “muscle in” to an adjoining full size unit. The RRC is authorized to pool the smaller tract on a fair and reasonable basis and authorize a larger allowable for the compulsory unit. § 102.014(b).

C. **Definition of "Standard" Proration Unit.** "Standard proration unit" in § 102.014(b) means the larger proration unit under field rules that provide for optional units. Application of Andromeda Enterprises, Inc., Personville, N. (Cotton Valley Lease) Field, Limestone County, Texas, Oil & Gas Docket No. 5-82,383. This issue arises when the special field rules provide for prescribed units (normally larger in size)
with optional (normally smaller, or 1/2 the size of the larger) units. The muscle-in provision would not be applicable to optional units. Thus, the operator of an optional sized unit does not get the protection from forcing pooling provided by the statute for standard size units to prevent an applicant from force pooling acreage with the optional unit acreage.

D. Undivided Interest Not Exempt. Oil & Gas Docket No. 09-0262864, Application of Grenadier Energy Partners, LLC for an MIPA Unit, EOG Resources, Inc. Whiteside Unit No. 1H Well, Newark, E. (Barnett Shale) Field, Montague County, Texas. In this case the Commission dismissed the application where Grenadier sought to force pool its undivided mineral interest in a nondrillsite tract included in EOG’s existing pooled unit. The Commission granted EOG’s motion to dismiss because Grenadier’s lease on the undivided interest covered additional productive acreage that was in excess of the standard unit size of 40 acres for oil wells.

X. PROHIBITED PROVISIONS IN OPERATING AGREEMENT. § 102.015.

A. Generally. A pooling agreement, offer to pool, or pooling order is not considered fair and reasonable if it provides for an operating agreement containing any of the following provisions:

1. Preferential right of the operator to purchase mineral interests in the unit;
2. A call on or option to purchase production from the unit;
3. Operating charges that include any part of district or central office expense other than reasonable overhead charges; or
4. Prohibition against non-operators questioning the operation of the unit.

B. Effect of Prohibited Provisions Upon MIPA Applications. If an applicant includes any of the above provisions in an operating agreement accompanying its voluntary pooling offer, § 102.015 requires the RRC to conclude that such offer is not fair and the application would be dismissed. A voluntary offer to pool explicitly negating the above prohibited provisions avoids this potential problem.

XI. EFFECTIVE DATE OF THE COMPULSORY POOLING ORDERS.

One of the major deterrents to the use of the MIPA is the time required before any successful applicant begins to participate in production from an existing well that is the subject of the application.

A. Importance of Effective Date. Because an MIPA applicant does not participate in production from a well until the RRC's pooling order takes effect, the effective date of such order is crucial for all interested parties. This factor alone provides significant economic incentive for respondents seeking to prevent an applicant
from force pooling into existing production to refuse to cooperate and delay the proceeding as much as possible.

B. **RRC's Historical Practice.** For many years the RRC's pooling order was made effective prospectively on the date it was signed by the commissioners. This practice provided even more incentive to delay RRC action approving the pooling application. In the early 1980s and in response to increasing delays in the issuance of final orders, the RRC began making its MIPA orders effective 60 days after the date of the force pooling hearing, even though the date the order was entered and signed may have been months after the early effective date. See, e.g., Application of Wainoco Oil & Gas Co., West (Huff) Field, Kleberg County, Texas, Oil & Gas Docket No. 4-78,246; Application of J.L. Schneider, Jr., Alvin, North (8550') Field, Brazoria County, Oil & Gas Docket No. 3-77898.

C. **Court Reversal of Retroactive RRC Orders.** In *Buttes Resources Company v. Railroad Commission*, 732 S.W.2d 675 (Tex. App.—Houston [14th Dist.] 1987, writ ref'd n.r.e.), which involved the appeal of the J.L. Schneider, Jr. Application, the Houston Court of Appeals struck down this practice and found that the RRC order could only be effective from the date it was signed, not the earlier date provided in the order. The court of appeals reasoned that an earlier effective date in pooling orders would be unconstitutional as a retroactive action interfering with vested property rights. *Id.* at 682

D. **Interim Order Procedure.** In response to the *Buttes Resources* decision, the RRC developed an interim order procedure designed in part to make compulsory pooling orders effective prior to the date of the final order in the case. In the Application of Betty McGlothlin Armstrong and W.C. McGlothlin, Jr., Henderson, North (Cotton Valley) Field, Rusk County, Texas, Oil & Gas Docket No. 6-89,061 (August 17, 1987), the RRC issued an interim order a short time after the hearing but months before the final order was entered in the case. The interim order required the force poolee operator to escrow the proceeds that would be attributable to applicant's interest in the well until the RRC entered a final order. The final order force pooling the acreage in the case was subsequently issued making the pooling effective from the date of the interim order.

E. **Court Review of Interim Orders.** The Corpus Christi Court of Appeals and the Texas Supreme Court reviewed the RRC's interim order practice in *RRC v. Pend Oreille Oil & Gas Company, Inc.*, 817 S.W.2d 36 (Tex. 1991). The RRC had entered an interim order in May of 1984 force pooling Forney's acreage into Pend Oreille's proration unit, granting Pend Oreille's well additional allowable from such Forney acreage and ordering Pend Oreille to escrow the additional proceeds. The interim order was entered pending the outcome of a separate RRC proceeding involving the amendment of the Limes Field's allocation formula from acreage to net acre-feet. The RRC concluded this net acre-foot proceeding by entering a final order in September of 1985 but made no change to the MIPA interim order at that time. The RRC subsequently executed the final order in the MIPA case in August
of 1987 but with an effective date that was the same date the interim order was originally signed (May 1984).

The court of appeals upheld the order for the period from August 1984 until September of 1985 because there was additional allowable available to Pend Oreille's well based upon Forney's proposed MIPA unit and hence no interference with vested property rights had occurred. This court, however, held the order unconstitutionally interfered with Pend Oreille's vested property rights from September of 1985 until August of 1987 because there was no additional allowable granted to Pend Oreille's well under the then existing interim order and the net acre-foot allocation that became effective in September of 1985.

The supreme court held that the court of appeals erred in concluding that the effective date of the final MIPA order was unconstitutionally retroactive because the lower court had improperly treated allowables as if they were vested property rights. The court found that operators do not have a vested property right in assigned monthly allowables, citing *RRC v. Aluminum Co. of Am.*, 380 S.W.2d 599, 602 (Tex 1964). The court stated that the final pooling order was not necessarily unconstitutional unless some other vested right was interfered with because of the retroactive MIPA order. The court, however, never reached this issue, holding instead that Pend Oreille was estopped to complain about the retroactive order under the facts in the RRC proceeding.

F. Modification of Interim Order Procedure By Parties’ Agreement. In *Long Run Oil Company, supra* at note 8, the RRC modified its interim order procedure by adopting the parties’ agreement which provided that the escrowing of proceeds from production based on the pooling offer would begin only after payout of what would be the applicant’s share of drilling and completion costs if the RRC were to grant the pooling application.

G. No Interim Orders Absent Agreement By Parties.

Based upon a pre-hearing ruling affirmed by the commissioners, the interim order procedure normally utilized in MIPA proceedings since the *Pend Oreille* case is no longer viable absent the consent of the parties. In Oil and Gas Docket No. 05-0243445, in 2005, Bonanza Resources (Texas), Inc. sought to force pool 49 acres into a 320 acre proposed proration unit around a prolific gas well operated by Burlington Resources. Bonanza also sought an interim order, following a preliminary hearing, to (i) set the effective date for the forced pooling unit at the conclusion of the proceeding, and (ii) require Burlington to escrow production proceeds from the well in question that would be allocated to Bonanza if its application were to be approved.

The hearing examiners, in a pre-hearing ruling, concluded that absent the consent of all parties to the establishment of an escrow account, and an agreed formula to determine the amount of funds to be deposited in the account, the requested interim order would be impermissibly retroactive under *RRC v. Pend Oreille Oil*
H. **Conclusion.** There may be a number of tactical advantages for a force poolee/respondent to agree to an interim order establishing an effective date for the final order and the allocation method for determining the amount to escrow each month. Absent such an agreement or a RRC reversal of position, however, the Bonanza case ruling indicates that there will not be any effective date for a force pooling order in advance of the date the commissioners sign the final order.

XII. **RISK PENALTIES.** § 102.052(a).

A. **Generally.** Section 102.052(a) authorizes the RRC to impose a maximum risk penalty of 100% where the applicant did not assume the risks of drilling the well. This provision means that applicants will have to pay or be charged in the accounting with up to 200% of their pro rata share of the reasonable drilling and completion costs plus their share of operating expenses for the well before participating in production. In addition, the payout period does not begin until the RRC enters its final order, which sets the date for pooling. The pro rata share is based upon the respective ownership of acreage within the force pooled unit established by the RRC. These costs and charges may be paid out of production. § 102.052(a).

B. **Inadequacy of Maximum Penalty.** The 100% statutory maximum risk penalty no longer reflects the customary non-consent penalties found in operating agreements currently in use.

C. **Standard for Risk Penalty Amount.** The standard for assessing a fair and reasonable risk penalty is the actual chance of a successful completion at the time the well was drilled. Applications of General Production Corp., et al., Giddings (Austin Chalk, Gas) Field, Lee County, Texas, Oil & Gas Docket Nos. 3-77,090 and 3-79,517. In the absence of evidence of risk, and where most wells drilled in the field appear to be commercially producible, the RRC has concluded that a nominal risk penalty (e.g. 10%) is appropriate. Application of Panola Producing Company, Carthage (Cotton Valley) Field, Panola County, Texas, Oil & Gas Docket No. 6-75,587.

XIII. **DISPUTES REGARDING COSTS.** § 102.052(b).

A. **Generally.** Section 102.052(a) authorizes the RRC to provide for reimbursement of drilling, completion and operating costs to parties advancing the same and to resolve disputes regarding costs and their allocation among owners.

B. **Certain Costs Excluded.** "All actual and reasonable drilling, completion, and operating costs" do not include lease acquisition costs. Legal expenses incurred to obtain a pooling order cannot be included as operating expenses. Application of Taubert & Steed, Neuhoff (Woodbine) Field, Wood County, Texas; Oil & Gas & Gas Co., Inc., supra. This pre-hearing decision was appealed by Bonanza to the commissioners but was affirmed by their refusal to act on the appeal.
Docket No. 6-85,661. Actual, rather than depreciated, costs should be used and both tangible and intangible costs are included. Applications of General Production, et al., Giddings (Austin Chalk, Gas) Field, Lee County, Texas, Oil & Gas Docket Nos. 3-77,090 and 3-79,517. Operating costs incurred prior to the effective date of the force pooled unit should not be included. Id.

C. Procedure for Resolving Cost Disputes. The RRC has authority to resolve disputes as to proper costs and their allocation to the working interest owners after notice to the interested parties and a hearing. § 102.052(b).

XIV. OWNERSHIP OF PRODUCTION IN THE FORCED POOLED UNIT. § 102.051

The MIPA requires that production in the pooled unit shall be allocated to the respective tracts within the unit in the proportion that the number of surface acres in each tract is of the total acreage in the unit. If, however, the RRC finds that surface acreage allocation does not allocate to each tract its fair share, the statute requires that the RRC allocate on some basis that will provide a fair share allocation. This requirement is further qualified with the § 102.051(b) providing that the allocation method cannot allocate to any nonconsenting owner less that the owner would receive under a surface-acreage allocation.

XIV. REQUISITES OF THE COMPULSORY POOLING ORDER. § 102.017.

The MIPA imposes few requirements for the pooling order itself.

A. General Requirements. Section 102.017(a) requires that the terms of an order be fair and reasonable and afford the owners of each tract within the unit an opportunity to recover their fair share.

B. Specific Requirements. Section 102.017(b) requires the order to include only the following:

1. A description of land included in the unit, identifying the reservoir to which it applies;
2. A designation of the location of the well; and
3. The appointment of an operator for the unit.
4. The order need not contain a legal description, as long as the land can be located or identified from documents in the agency record, whether specifically referred to in the order or not. Buttes Resources v. Railroad Commission, supra.
XVI. TERMINATION OF COMPULSORY UNITS. §§ 102.081, 102.082.

The MIPA addresses the manner in which a compulsory unit may be terminated.

A. Consent of Owners. Section 102.081 specifically prevents the modification or dissolution of a compulsory unit unless affected mineral owners have consented or unless the unit is enlarged through another MIPA proceeding.

B. Automatic Dissolution. Section 102.082 sets forth three different events, any one of which will cause the compulsory unit to dissolve automatically.

1. One year after the effective date of the unit if there has been no drilling operations or production on the unit;

2. Six months from the date a dry hole is completed on the unit; or

3. Six months after the cessation of production from the unit. There is a question whether a temporary cessation of production, such as a shut-in to make up overproduction, would trigger this provision. The RRC's authority to order a reduced rate of production to make up overproduction appears to alleviate this problem. Applications of General Production Corp., Giddings (Austin Chalk, Gas) Field, Lee County, Texas, Oil & Gas Docket Nos. 3-77,090 and 3-79,517.

C. Termination of Pooled Lease. Section 102.083 provides that on the termination of a lease pooled by an order of the RRC the interests covered by the lease are pooled as unleased mineral interests.

XVII. APPEALS OF MIPA ORDERS. § 102.112.

A. Venue. Section 102.112 provides the venue for appeals of MIPA Orders.

1. Prior to recodification of the MIPA into the Natural Resources Code, venue for the appeal of an order approving pooling was in the county where the land is located, but venue for an order denying or dismissing pooling was in the district court of Travis County. Railroad Commission v. Miller, 434 S.W.2d 670 (Tex. 1968).

2. After recodification, § 102.112 appears to have eliminated the dual venue result, but the language of this provision is not entirely clear. Further § 1.001(a) of the Code states that no substantive change of the law was intended by the recodification. As a result, a sufficient question exists such that some practitioners appealing a denial or dismissal order perfecting appeals both to the county where the land is located and Travis County. Once both appeals are timely filed, an attempt is made to proceed by agreement in Travis County while leaving the docket in the other county pending.
B. **Standard for Judicial Review of MIPA Orders.**


2. The Texas Supreme Court in *Carson v. Railroad Commission, supra*, stated that the review standard of whether the voluntary pooling offer was fair and reasonable is jurisdictional and indicated the review was not pursuant to the substantial evidence rule. As noted above, the supreme court clarified in *RRC v. Pend Oreille Oil & Gas Company, Inc., supra*, that the review is still subject to the substantial evidence rule to determine if the RRC’s ruling is reasonable and proper.

**XVIII. RECENT DEVELOPMENTS – FORCE POOLING IN RESIDENTIAL AND COMMERCIAL SUBDIVISIONS**

A. **Historical Background.** At the time of the MIPA’s enactment in 1965, many practitioners believed this statute would facilitate the drilling of additional wells by force pooling holdouts into proposed proration units for yet to be drilled wells. Despite this expectation, the MIPA had been used almost exclusively by parties left out of production seeking to force pool their interests into production from an existing well until the advent of mineral development in established subdivisions in the Newark, East (Barnett Shale) Field.

B. **Development Problems In Urban Areas of the Barnett Shale.** Operators attempting to drill and develop acreage in urban, subdivided areas of the Newark, East (Barnett Shale) Field have encountered special problems causing renewed interest in the MIPA. In subdivided residential and commercial areas, primarily in and adjacent to Fort Worth, there are invariably some lot owners who either cannot be found or refuse to lease or pool their property to allow wells to be drilled where the other owners have leased their tracts and desire to participate in production. If the unleased lots are located in the path of proposed horizontal drainholes, an operator’s alternatives are to either force pool these barrier tracts or not drill the wells.

C. **Finley Resources, Inc.’s MIPA Application, Oil & Gas Docket No. 09-0252773.** In one of the more significant cases decided by the RRC in recent years, the commissioners addressed the issue of whether the MIPA could be utilized to force pool unleased, small tract mineral owners who refuse to lease or pool into a

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13 Some would argue that the reason there were so few such MIPA applications is that the statute’s overall purpose of promoting voluntary pooling was achieving its desired result. The threat or availability of this remedy encouraged recalcitrant mineral interest owners to negotiate and work out a mutually agreeable solution instead of incurring the burdens and expenses imposed by a MIPA proceeding.

14 The RRC had approved at least one MIPA application force pooling certain royalty interests into a proration unit with existing production. Oil & Gas Docket No. 8-76,921, Application of ARCO Oil and Gas Co. to Establish Two Pooled Units in the Moore-Hooper (Ellenburger) and (Fusselman) Fields, Loving County, Texas (September 8, 1981).
1. Background Facts. Finley proposed to form what turned out to be a 96.32 acre pooled unit to drill a horizontal well in the Barnett Shale in a subdivision of 300-350 lots about one mile from downtown Fort Worth. Finley and other working interest owners had leased a total of 90.616 acres, leaving 26 lots totaling 5.704 acres within the proposed unit unleased. Although the unleased owners either refused to respond to Finley’s voluntary offers or could not be located, no protestant appeared at the hearing.

2. Finley’s Voluntary Offers to Unleased Owners. Finley made three alternative offers to the unleased owners that included the following:

a. To lease the owner’s mineral interest for a bonus of $2,100/acre, a 20% royalty, a 3-year primary term, a pooling clause, and a provision preventing any surface use; or

b. To pool the owner’s interest and participate as a working interest owner paying a pro rata share of well costs based upon a surface acreage allocation; or
c. To farm out the owner’s interest by conveying an 80% net revenue interest to Finley while retaining an override of 20% (proportionately reduced) until the well paid out when the unleased owner had the option to convert the override to a 25% working interest, proportionately reduced.

3. Finley’s Position. Finley argued that the proposed well could not be practically and economically drilled because of the circuitous route of the well path around unleased tracts and the danger of unintentional trespass. Finley also contended that approval would protect the correlative rights of the vast majority of mineral interest ownership within the proposed unit by providing them with an opportunity to participate in production for their fair share of Barnett Shale hydrocarbons. Finally, Finley argued that approval of its application could eliminate the drilling of unnecessary wells from unleased lots in the future and would prevent the waste of otherwise recoverable hydrocarbons.

4. Examiners Originally Recommended Denial of the Application. The original examiners’ recommendation (PFD) concluded that the MIPA could not be used to force an unwilling party into participation in a force pooled unit because this statute was limited to protect small tract lessees/owners and was not a broad authorization to protect correlative rights generally or allow large tract lessees more flexibility in development. The examiners further concluded that the purpose of the MIPA is to allow parties left out of potential production to participate but was not intended to force unwilling parties into a compulsory unit. The examiners finally determined that Finley failed to satisfy its burden to prove force pooling would achieve any of the MIPA’s three purposes of preventing the drilling of unnecessary wells, protecting correlative rights or preventing waste.

5. RRC Granted Finley’s MIPA Application After Oral Argument. A final order granting Finley’s application was ultimately signed by two of the three commissioners (Commissioners Jones and Carrillo voting in favor, Commissioner Williams dissenting) over one year after the hearing was held on the application.

6. Terms of MIPA Final Order. The order signed by the commissioners limited the force pooled unit to the Newark, East (Barnett Shale) Field with Finley as the operator and allocated production on the basis of surface acreage. Significantly, the order imposed no risk penalty on the unleased owners being force pooled; these interests were force pooled as to a 1/5th royalty and a 4/5ths working interest, proportionately reduced. The order also required that proceeds payable to unknown, unleased owners would be held in escrow and were "subject to disposition in a manner provided by law."
7. Significance of Finley Decision. The RRC’s decision in this case is important for several reasons:

a. The order establishes that force pooling is a remedy to drill wells over the objection of unleased parties who may not desire to participate.

b. The threat of force pooling may assist in encouraging reluctant unleased owners to negotiate in good faith for the development of hydrocarbons.

c. The order does not establish a minimum "sign-up" of the mineral interest percentage aligned with the force pooling applicant before this kind of force pooling could be approved.

d. Favorable terms imposed upon the force pooled parties (no risk penalty, 1/5th royalty and 4/5ths working interest) could encourage some unleased parties to hold out instead of lease or pool voluntarily.

8. Illustration Justifying RRC’s Final Decision.

- Operator leases and pools 640 acres to drill a well at proposed location as a step out well targeting 16,600’ field with 640 acre field rules.
• Field’s allocation formula is suspended - no gas allowables.

• Mineral owner or lessee of 10 acre tract refuses to lease, farmout or participate in drilling proposed well.

• 10 acre tract was subdivided in 1930 and is a legal subdivision entitled to a drilling permit as a matter of law.

• If Operator is unable to force pool holdout and drills a successful well, holdout would have a slam dunk offset location that would

  – Be an unnecessary well;
  – Cause a gross abuse of correlative rights by providing vastly more than the holdout’s reserves at the expense of the pooled unit owners;
  – Not prevent waste because all of the hydrocarbons produced by the holdout’s well would otherwise be produced.

D. XTO Energy, Inc.’s MIPA Applications for its Texas Steel “A” Unit, Texas Steel “B” Unit, Rosen Heights Unit and TWU A Unit. After the Commission issued its order approving the Finley Resources MIPA in August 2008, XTO filed in late 2008, in 2009 and 2010 four MIPA applications that have helped refine and further clarify how the Commission will interpret and apply the provisions of the MIPA to requests for force pooling of residential and commercial subdivided lots in the Newark Field.

1. Oil & Gas Docket No. 09-0260202, XTO’s MIPA Application for its Texas Steel “A” Unit. XTO filed to establish a force pooled unit of 434 acres of which it had 413 acres under lease. As in the Finley Resources MIPA, some owners refused to lease or pool as a working interest or could not be located. XTO used the Finley three prong voluntary offer to lease, pool or farmout. The proposed unit was not acceptable to the Hearings Examiners because the unit could not be drained entirely by the one proposed MIPA well.

The Examiners concluded among other reasons that because a large portion of the 434 acres could not be drained by one well as conceded by XTO’s expert witness and because the evidence showed that XTO intended to drill up to four wells to develop fully the proposed unit, the application had to be denied under the MIPA. The Examiners found that none of the statutory purposes of the MIPA of either protecting correlative rights, preventing waste or preventing the drilling of unnecessary wells would be served by force pooling the 434 acre unit. Further, the Examiners reaffirmed that the Commission’s authority under the MIPA, based on an earlier decision in the Patricia Nowak Application, discussed at VII. C.3.f. above, was limited to one well on an MIPA unit not multiple wells as XTO was planning. The Examiners noted that there were Rule 37
exception locations and regular well locations on its leases from XTO could drill economic wells to develop most of the acreage it owned.

The Examiners’ recommendation of denial was presented to the Commissioners for a final decision. After hearing oral argument, the Commissioners decided to send the case back for further hearings to determine how much of the 434 acre unit the proposed well would drain. At the reopened hearing, however, XTO proposed a new unit containing 312 acres that was a reduced version of the original unit. XTO presented new evidence that the proposed well “would likely drain” the unit acreage based on a pressure effect that it had observed during a fracture stimulation operation in two wells 2000 feet apart.

Again the Examiners issued their decision recommending denial of the application as modified. The Examiners used the XTO evidence of the expected recovery to conclude that regular locations and Rule 37 exception wells on the 303 acres XTO had under lease would have greater recoveries than the proposed well on the proposed MIPA unit with 312 acres. The Examiners also believed that XTO was still intending to do a multiple well development for the unit. Most significantly, the Examiner concluded that the proposed MIPA well would not “effectively and efficiently” drain the proposed 312 acre unit. The Examiners noted that it was counterintuitive with 330’ lease line spacing in the field and many wells 500’ apart that a proposed well would drain, in this instance, up to 1875’ laterally. The Examiners found that what was “impacted” or “likely” was not the proper drainage standard. The Examiners concluded that given the lack of effective and efficient drainage, the purposes of force pooling under the MIPA would not be served by establishing the proposed unit.

The Commissioners entered its final order in February of 2010, denying the application. But significantly, the Commissioners voted to remove as unnecessary to the decision the Examiners’ proposed “effective and efficient” drainage finding. At least one Commissioner was not sure that “effective and efficient” is the proper drainage standard if the proposed unit complies with the standard unit size, which for the Newark Field is 320 acre units with the 20 acre optional units.

2. Oil & Gas Docket No. 09-0261248, XTO’s MIPA Application for its Steel “B” Unit. This application, which XTO filed shortly after the Steel “A” case, had a similar procedural history but with a different outcome. XTO originally proposed a 317 acre MIPA unit, which the Examiners recommended be denied, because there would not be “effective and efficient” drainage of the entire unit area by the proposed well. The Commissioners again held oral argument and sent the case back for more hearings to determine the amount of acreage the proposed well would
drain. Again, XTO abandoned its original proposal and presented a unit containing approximately 270 acres, which was a portion of the original unit.

The Examiners, however, did not recommend an outright denial of the application after the second hearing. The Examiners concluded that the locations of the unleased tracts were similar to the facts in Finley Resources where the Commission ordered pooling because the acreage could not be developed with Rule 37 exceptions or other regular locations without risking subsurface trespass on unleased tracts. The Examiners were still concerned with the inability of the proposed well to drain all of the unit acreage. They concluded, however, that unitizing all of the acreage within 500’ of either side of the proposed well was appropriate and consistent with the MIPA. For this conclusion, the Examiners relied on XTO’s evidence of the well spacing for its multiple well development plan. From this evidence, the Examiners considered it reasonable to infer that a well could drain up to 500’ laterally on either side of the drainhole.

Based on their analysis, the Examiners proposed in the alternative the formation of a force pooled unit containing the acreage within 500’ of each side of the proposed lateral for the unit. This would result in a unit of approximately 90 acres. The Commission order approved the Examiners’ alternative unit pooling the unleased acreage on a 1/4th royalty and 3/4th working interest basis with no risk penalty for the working interest portion. Subsequently, the Commission granted XTO’s motion for rehearing to allow XTO to withdraw the application because XTO did not intend to drill a well on the substantially modified unit approved by the Commission over XTO’s objection.

3. Oil & Gas Docket No. 09-0261375, XTO’s MIPA Application for its Rosen Heights Unit. This application was filed around the time of the Steel “B” Application but it did not involve a reopened hearing as in the Steel “A” and “B” Applications. In this case, XTO proposed the formation of an approximately 262 acre force pooled unit. XTO used the three prong Finley type of voluntary offer of lease, or pool working interests, or farmout. The Examiner focused on the terms of the leasing proposal of the voluntary offer and decided that because of differences in the bonus amounts paid and offered to various owners to lease their tracts, the offer was not fair and reasonable. As result, the Examiner recommended that the application be denied. Almost as an aside, the Examiner noted that the proposed well would not drain the entire unit.

The bonuses paid and offered for leasing had varied from up to $25,000 per net mineral acre to $2500 per net mineral acre over many months of leasing activity. XTO presented evidence that the variation was due to a
significant change in the market conditions resulting from the fall in the price for natural gas, but the Examiner was not persuaded.

The Commissioners, however, disagreed with the Examiner and found that the terms of the voluntary offer were fair and reasonable and that the bonus offered could vary with the market conditions. The Commission then proceeded to approve a substitute unit containing 254 acres by excluding a tract that under any standard would not be drained by the proposed well. The final order pooled the unleased tracts on a $\frac{1}{4}$ royalty and $\frac{3}{4}$ working interest basis for participation in production with no risk penalty. Most significantly, the final order expressly provided that the force pooled unit would be effective only for the proposed well. Heretofore, the MIPA orders of the Commission have not contained such a restriction. In the Patricia C. Nowak MIPA Application, discussed above at VII. C. 3. f., the Commission did agree with the protestant that the Commission’s authority was limited to force pooling acreage and interests into a proration unit for only one proposed or existing well.

4. Oil & Gas Docket No. 09-0264211, XTO’s MIPA Application for its TWU A Unit, Well No. 1H, Newark, East (Barnett Shale) Field. This application involved a proposed 230 + acre unit containing 649 small tracts of which 579 tracts totaling 201+ acres were under lease. The owners of the un-leased tracts refused to lease or pool or failed to respond to the proposed offers of XTO. No parties appeared to protest the application. The evidence presented by XTO included drainage studies based on 166 wells within a five mile radius of the proposed unit area. These studies showed a range of drainage radii from 4 to 535 acres depending the wells selected from the study area and the recovery factors used of 10 and 20 %. XTO’s evidence supported the smaller drainage areas as reasonable along with the larger areas that were greater than the proposed 230 acre unit.

The examiners were consistent with the other XTO decisions in finding that the evidence was inconclusive that the proposed well could be expected to drain the acreage in the proposed unit. A drainage area of less than 200 acres was just as reasonable as one of more than 200 acres. The examiners also concluded that profitable Rule 37 exception wells could be drilled to develop the proposed unit area and would likely increase the recovery of reserves. The examiners stated that where Rule 37 exception wells can be drilled that will either prevent waste or protect correlative rights, it is not proper to order force pooling under the MIPA to achieve these statutory purposes.

The Commission entered its final order in December of 2010 accepting the examiners’ recommended denial of the XTO application.
E. **Going Forward.** The Commission decisions in these applications certainly are refining the issues and the Commission’s policy under the MIPA in the Newark Field. In particular, the Commission will no doubt continue its assessment of the proper standards for gauging the MIPA statutory purposes of protecting correlative rights, preventing waste and preventing the drilling of unnecessary wells. This exercise must necessarily focus on the type of drainage that the Commission will require to justify force pooling lands into an MIPA unit in the field. To this point, the Commission staff has largely required that the evidence show a well will “effectively and efficiently” drain the entire proposed unit. And while that is a no doubt a “safe harbor” for an applicant’s case, the Commissioners have yet to fully endorse that as the only drainage standard they will use in evaluating applications.

The Newark decisions and the policy developments that have and continue to arise may shape the Commission MIPA decisions in other fields around the state. Time will tell on that score, but the circumstances present in the Newark Field with the numerous small tract homeowners opposed to the oil and gas development are not as likely to be present in most fields that are more rural in location.
TABULATION OF MIPA APPLICATIONS
FILED WITH RAILROAD COMMISSION SINCE 1965

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<sup>1</sup>Adjusted to combine companion applications by the same operator involving the same lands.