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**THE MODEL FORM JOINT OPERATING AGREEMENT
SUBSEQUENT OPERATIONS and
A DISCUSSION OF RELATED HORIZONTAL WELL
ISSUES**

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I. INTRODUCTION

Originally introduced as the Ross-Martin form 610 Model Form Joint Operating Agreement in 1956, the American Association of Professional Landmen model form operating agreement has been revised in 1977, 1982, 1989 and most recently in 2013 the 1989 (Horizontal Revisions) version has been approved.¹ This form, in each of its versions, has become the industry standard model form operating agreement for most projects. The AAPL model form operating agreement is the focus of our discussion today. For purposes of this paper, we will refer primarily to the 1989 version, or to the 1989 (Horizontal Revisions) version, unless expressly identified otherwise. In every event, the model form operating agreement is only a standardized beginning point designed to streamline negotiations by dealing with common, recurring issues in a predictable and consistent manner.

All versions of the Model Form Operating Agreement until the recent horizontal modifications contemplated matters only in the context of a vertical well. Because technology does not stand still, the manner in which oil and gas wells have traditionally been drilled has changed so that a large proportion of new wells drilled are horizontal wells. From a legal standpoint, we are only beginning to understand the

significant differences between vertical and horizontal wells. We are continuing to develop terminology, and we are still somewhat removed from all of the solutions. As a result, the Model Form Operating Agreement continues to evolve and a new, comprehensive form dealing with both vertical and horizontal issues, and including revisions based upon important case law, is currently in the works.

The provisions, and in some cases the alterations and revisions that we will discuss in this paper are not simply those which require filling in a blank or making an election provided for in the form. Our primary focus will be to discuss and understand those provisions relating to ongoing operations and which should be considered in allocating, assessing and accepting the geological, mechanical and financial risks of a particular project. Because this paper is intended to be presented to an audience composed of those who are either new to Texas oil and gas legal practice or are looking for a refresher, we will be focusing somewhat on the basics.

II. ORGANIZATION.

The Model Form Operating Agreement is organized according to several distinct categories in answer to a series of specific broad questions:

1. What are we doing?
2. Who makes decisions and how?
3. Who owns what?
4. Who pays for what?
5. How do we get out?

¹ All references are to the American Association of Professional Landmen ("AAPL") model form operating agreements and will be identified by the vintage for the individual form where reference is made to other than the 1989 version. For ease of reference, the 1989 Model Form (Horizontal Revisions) may also be referred to as the "Horizontal Model Form" or "Horizontal Revisions Form".

For the most part, each of these questions interrelates with some or all of the others and each of these questions are common to almost every contract related to an ongoing project or business arrangement. In this paper, we will be exploring primarily answers to the first two questions.

III. WHAT ARE WE DOING?

The question, "what are we doing?" seems to have the simplest answer of all. Of course, the obvious answer is that "we" are drilling an oil or gas well. That answer is the thirty thousand foot view. The parties are actually "doing" a number of different things that are related to or the result of drilling.

Although the point of all operating agreements is to plan for drilling and oil or gas well on the lands and leases included in the Contract Area, not every operating agreement contemplates an immediate drilling operation. Often we see the Initial Well provisions of Article VI.A left blank, deleted or the words "there is no Initial Well" inserted. This happens most often when parties come together to jointly acquire one or more leases or to sell or acquire an interest in a block of acreage for which there is no immediate drilling plan. In those instances, the parties do not want to leave the negotiation of a mutually acceptable operating agreement to future uncertainty. Instead, they will determine the contents of an acceptable operating agreement as part of the initial deal structure, but will not require that an Initial Well be drilled at a predetermined location or time, or that participation in the first well is obligatory for all of the parties. In that event, the first well drilled on the project will in effect be subject to the provisions relating to the Subsequent Operations provisions.

Second, and probably of equal importance, the parties are dealing with ongoing operations. That is, whether or not the first well is the obligatory Initial Well or is proposed as a Subsequent Operation under Article VI.B, the parties must consider matters such as completion elections, day to day producing operations, repairs, reworks, additional drilling, liability for expenditures and, ultimately, plugging operations. Each of these matters require that decisions be made, actions taken, costs allocated and, potentially, that the relationships of the parties adjusted. These are the elements that we will touch on in the remainder of this paper.

IV. THE INITIAL WELL

Article VI.A of the Model Form provides for the "Initial Well" and is among the shortest provisions of the Model Form, taking up less than four full lines of text with space left to fill in the essential details. Participation in the Initial Well is obligatory by all parties and is qualified only by the casing point election found in Article VI.C.² In most cases, events leading up to execution of the operating agreement have informed the parties of all they need to know with respect to participating in the Initial Well. At the time an operating agreement is signed, the parties will most likely have had significant discussions and exchanges of information with respect to the leasehold ownership, where and when the first well should be drilled, the objective depth, the target formation, the expected cost and most other matters of importance. The location of

² Art. VI.A. "The drilling of the Initial Well and the participation therein by all parties is obligatory, subject to Article VI.C.1. as to participation in completion operations [casing point election] and Article VI.F. as to termination of operations and Article XI as to occurrence of force majeure."

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