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POOLING AND UNITIZATION IN TEXAS: A PRIMER

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I. INTRODUCTION

Pooling issues are a staple of oil and gas law practice in our state. The splintering of mineral ownership within tracts and the subdivision of larger tracts into smaller tracts, through inheritance and sale, creates increasingly fragmented ownership of minerals. Pooling tracts and leases, usually voluntarily and, occasionally by use of Texas' forced pooling statute, is often an effective and efficient way to solve those problems. This paper presents "the fundamentals" on voluntarily pooling in Texas, including lease authority, regulatory considerations, the duty to pool in good faith, and case law developments. Fieldwide unitization for enhanced recovery projects and production sharing agreements are also addressed herein.

II. DIFFERENCES AMONG VARIOUS KINDS OF "UNITS"

Terminology is critical. One first has to understand what a pooled unit is – and what it is not. The term "unit" is widely used in oil and gas leases and has numerous meanings in the oil and gas industry. At least seven different types of units are widely used in Texas oil and gas development. Only one of these is a "voluntary pooled unit."

Other common types of "units" include: drilling units, proration units, force pooled units, and enhanced recovery units. Each of these units is based on the conservation statutes and/or rules of the Railroad Commission of Texas ("RRC") that apply to the regulation of oil and gas drilling and production. Even though many of these types of units are regulatory creatures, the terminology appears often in oil and gas leases. Finally, the lease may refer to other types of "units," such as a retained acreage tracts, adding more possibilities for confusion.

By contrast to the regulatory purpose "units", a pooled unit is created under the terms of oil and gas lease provisions or other private contracts between lessees and lessors. In recent years, the production sharing agreement unit has developed as a variant on the pooling clause. The production sharing agreement unit is also created by private contract. The term "unit" in the context of oil and gas has several different meanings that cause considerable confusion for courts and within the industry. Below are the most common types of "units" that one encounters in Texas.

A. Voluntary Pooled Units

A voluntary pooled units result from the lessee's exercise of authority granted in a lease pooling clause or other agreement of the parties. A voluntary pooled unit is created by combining separately owned mineral interests and leases covering different tracts of land into one "pool" or tract. This kind of unit is typically established by an instrument called a unit declaration or designation of unit. Production proceeds are usually allocated among the various mineral interest owners pro rata on the basis of their fractional mineral acres relative to total

mineral acres in the unit. Operations and/or production on any portion of the pooled unit are deemed to be operations/production on each of the leases and tracts included within the unit, thereby maintaining all of the leases that are pooled.

B. Force Pooled Units

Force pooled units are relatively rare. These units are created by an order of the RRC under the Mineral Interest Pooling Act ("MIPA").[1] An MIPA order compels the joinder or inclusion of otherwise unpooled interests in the force pooled unit subject to the specific provisions of the statute. The MIPA designates who may make application for force pooling and under what circumstances. These units are limited to an individual well proration unit and to a specific RRC field or producing reservoir. The maximum size of an MIPA unit is 160 acres for an oil well and 640 acres for a gas well plus ten percent tolerance. The statute does not address horizontal wells.

C. Drilling Units

A drilling unit is "the acreage assigned to a well for drilling purposes." RRC Rule 38(a)(2).[2] Until recently, to obtain a drilling permit, an operator had to depict a drilling unit for a to-be-permitted well on the plat submitted with its drilling permit application. A drilling unit had to contain at least the minimum acreage prescribed by the applicable density rule for the target field, otherwise a Rule 38 exception would be required. Notably, the RRC allowed drilling permit applicants to designate more than the minimum acreage prescribed by the applicable rules as the "drilling unit" for a well. Presently, operators are no longer required to formally designate drilling units on their permit plats. Instead, the RRC now confirms compliance with Rule 38 by requiring operators to state (a) the number of acres in the lease (or unit), and (b) the number of wells applied for, permitted or completed on that lease/unit in the targeted field. If the number of acres per well is equal to, or greater than the density rule for the field, the well is deemed to be in compliance with Rule 38. While drilling units are no longer required by the RRC, references to drilling units in oil and gas leases are not infrequent.

D. Proration Units

A proration unit includes the acreage an operator has assigned to a completed well to receive a production allowable. RRC Rule 38(a)(2). Every well does not have a proration unit. Proration units exist only when the RRC has adopted special field rules that use acreage, or some other reserve-based factor involving area or acreage, as a factor in the allocation formula. The allocation formula divides the total field allowable among the various wells in the field. Each proration unit applies to a single well.

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[1] Chapter 102, TEX. NAT. RES. CODE ANN.

[2] All references to rules are to RRC statewide rules, found at 16 TEX. ADMIN. CODE §§ 3.1-3.100, unless otherwise specifically noted.

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