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The Model Form Joint Operating Agreement
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The Basics

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THE MODEL FORM JOINT OPERATING AGREEMENT – THE BASICS

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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, in 2013 as the 1989 (Horizontal Revisions), and the new 2015 model form released in April of 2016.¹ This set of forms has collectively become the industry standard beginning point for operating agreements in all producing regions of the United States. In every event, the model form operating agreement is designed only as a starting place intended to streamline negotiations by dealing with common, recurring issues in a predictable and consistent manner. Additionally, the model form a methodology for making decisions that affect operations, accounting for expenses and, to some extent, revenues, and establishes the legal relationship among the parties.

As originally written, all versions of the Model Form Operating Agreement through the 1989 version 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 dramatically so that the majority of new wells currently being drilled are horizontal wells. We are still only beginning to understand the legal similarities

and differences between vertical and horizontal wells, and we are continuing to develop and standardize terminology in a rapidly changing technical environment.

Our primary focus in this paper will be to discuss and understand the basic provisions and working of the operating agreement from both a legal and practical perspective. For purposes of this paper, we will refer primarily to the 1989 (Horizontal Revisions) the 2015 versions unless expressly identified otherwise.

II. The Contract Area.

The operating agreement is designed to govern a specific geographic area, referred to as the Contract Area. A description of the Contract Area is so important that it appears on both the title page and in detail on Exhibit "A". Typically, the cover page of the operating agreement will reference Exhibit "A" for the Contract Area description. This practice assures that a discrepancy between the cover page and the detail in Exhibit "A" does not result in an ambiguity concerning the Contract Area.

On Exhibit "A", the lands covered by the operating agreement, including any depth limitations, and the leases are to be listed in detail with the effect that the operating agreement will govern the activities of all signatory parties within the specified geographic area. However, some operations

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. The 1989 Model

Form (Horizontal Revisions) may also be referred to as the "1989 Horizontal Form". Capitalized terms not defined herein have the meaning ascribed to such term in the operating agreement.

contemplated by the parties may actually occur outside of the area covered by the contributed leases and, therefore, is technically not within the Contract Area. Those items may include such things as off lease locations, central tank battery facilities, oil, gas and produced water transportation, and the installation of electric power. Critical thought should be given to these items and others that might be mandated by the nature of the project to make certain that they are properly dealt with and included in the terms of the operating agreement. Failure to adequately deal with these issues could, under some facts, result in having to defend against liability as a partnership and could impact the operator's right to reimbursement from the joint account. In that regard, the land and legal team should interact with the operations group to understand how the project will actually be executed.

III. The Operator.

A. Selection.

Article V.A names the operator and, subject to the limitations contained in the agreement, delegates to the operator exclusive control and conduct of activities on the Contract Area and obligates the operator to act as a reasonable prudent operator and to conduct operations in a diligent and workmanlike manner. This delegation of exclusive control is not only important for the practical management of activities to be conducted, but also is an essential element in assuring that the joint activities of the parties does not constitute a mining partnership. Mining partnerships, like all general partnerships, impose joint and several liability on the partners, the actions of any partner can effectively bind all partners and each partner is a fiduciary to the others. Eliminating those shared responsibilities is

not a byproduct of the operating agreement, it is central to its purpose and should be protected in any revisions that might be made to the model form.

All of the model form versions are written with the assumption that the operator will also own an interest in the oil and gas leases or minerals within the Contract Area. Thus, there are many provisions in the operating agreement where the operator is empowered to make proposals, vote, or to take over non-consenting or defaulting interests. However, because of the liabilities associated with control of operations, many oil and gas companies conduct operations through separate, wholly owned subsidiary or affiliates that own no interest in the underlying oil and gas estate, generally referred to as a "contract operator". To the extent that the contract operator is in fact a party to the operating agreement and named as Operator in Article V or by a vote of the working interest owners, the actual effect of the default provisions may be somewhat erroneous. In that regard, a modification should be made by adding a provision to Article XV Additional Provisions. An example of such a provision is as follows:

Resources Operating LLC owns no interest of any nature in the oil and gas leases and/or interests in the Contract Area covered by this Agreement. For so long as Resources Operating LLC, or any affiliate, serves as Operator hereunder without owning a working interest in the Contract Area, the phrase "no longer owns an interest in the Contract Area" shall be deemed to be deleted from Article V.B.1. of this Agreement. Whenever or wherever this Agreement contemplates an election or vote by Operator, Resources Energy LP, (or its successor related entity whose principal owners are substantially the same as the current owners of Resources Energy LP) shall make such proposal, election, or vote on behalf of or pursuant to authority

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