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**PERFECTION OF PARTIES' RIGHTS AS CREDITORS  
UNDER THE MODEL FORM JOINT OPERATING  
AGREEMENT**

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# PERFECTION OF PARTIES' RIGHTS AS CREDITORS UNDER THE MODEL FORM JOINT OPERATING AGREEMENT<sup>1</sup>

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## I. INTRODUCTION<sup>2</sup>

Oil and gas exploration and production ("E&P") is usually conducted by two or more parties in cooperation with each other. This is so because of the high investment risk, the large capital investments required, the long payout period, the need for shared technical expertise, specific regional experience, possession of seismic and other necessary information, and, in some instances, compulsory regulatory requirements. This cooperation usually begins at the earliest stages, such as bidding and the initial well, and continues for the economic life of the interests in which the parties are invested. The cooperation may also extend to joint marketing and construction of gathering lines and other facilities through the use of different contracts reflecting the nature of the risk, rights and obligations involved.

In the U.S., the joint operating agreement is the operational agreement that is most basic to this relationship. Properly drafted, it regulates the rights and obligations of the parties to it, spelling out on a percentage of interest basis, the respective rights, obligations and liabilities of each party. The joint operating agreement also allows the parties to share risks and costs; establish an economy of scale in contracts and procurement for the covered E&P operations; establish joint bidding procedures; impose confidentiality restrictions; create areas of mutual interests; impose limits on transfers; create certain tax advantages; and in Texas, prevent the joint and several liability of the parties to third parties.

In Texas, the American Association of Professional Landmen ("AAPL") forms have become the industry standard form joint operating agreement for most onshore projects. These forms were first introduced as the Ross-Martin form 610 Model Form Joint Operating Agreement in 1956 and have been revised in 1977, 1982, and 1989. In addition, the 1989 version was revised in 2013 to include provisions relating to horizontal operations.<sup>3</sup>

In this paper, unless expressly noted otherwise, we will focus on the 1989 AAPL Model Form Joint Operating Agreement (the "JOA") that does not include the horizontal revisions. The logic is that the issues to be discussed are universal to all E&P operations. You should note that the suggestions which will be discussed in this paper will require physical changes to the JOA,

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<sup>3</sup> For a discussion of the horizontal revisions *see* Michel E. Curry, "The Model Form Joint Operating Agreement Subsequent Operations and A Discussion of Related Horizontal Well Issues", 2014 Fundamentals of Oil, Gas and Mineral Law (University of Texas Law School); and Jeff Weems, "Changes Within the AAPL 610-1989 Model Form Operating Agreement: Horizontal Modifications and Other Developments Regarding the Model Form Operating Agreement", 2013 Advanced Oil, Gas & Energy Resources Seminar (State Bar of Texas).

not simply filling in a blank or making an election provided in the JOA. Because this paper is prepared for presentation to Texas lawyers who are either new to Texas oil and gas or are looking for a refresher course, it will focus primarily on the basics of identifying creditors and debtors under the JOA, the liens and security interests created under the JOA, and the methods of perfecting those liens and security interests. For the same reasons and because of the current economic climate for E&P companies, this paper it will also provide a brief review of other options provided by the JOA to parties who are trying to protect their financial interests.

## II. ORGANIZATION

The JOA is organized into several distinct categories which are intended to answer a series of specific broad questions. One of those questions is “Who pays what?”<sup>4</sup> Ancillary questions are “What liens and security interests are granted?” and “How are the liens and security interests perfected?” The answers to the first two questions are provided in the JOA; the answer to the third is provided by Texas law.

## III. WHO PAYS WHAT?

Generally speaking a party who consents to the subject operation also agrees to pay its share of all necessary expenditures incurred in connection with the proposed operation.

Article III.B. provides that:

*Unless changed by other provisions, all costs and liabilities incurred in operations under this agreement shall be borne and paid, and all equipment and materials acquired in operations on the Contract Area shall be owned, by the parties as their interests are set forth in Exhibit “A.” In the same manner, the parties shall also own all production of Oil and Gas from the Contract Area subject, however, to the payment of royalties and other burdens on production as described hereafter. (Emphasis added.)*

In addition, Article VI.C.1 provides as follows:

1. Completion: Without the consent of all parties, no well shall be drilled, Deepened or Sidetracked, except any well drilled, Deepened or Sidetracked pursuant to the provisions of Article VI.B.2. of this agreement. *Consent to the drilling, Deepening or Sidetracking shall include:*

☐ *Option No. 1:* *All necessary expenditures for the drilling, Deepening or Sidetracking, testing, Completing and equipping of the well, including necessary tankage and/or surface facilities.*

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<sup>4</sup> Curry *supra* at note 3.

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