From:	Molly Garner
To:	Kourtney Romine; Michael Christian (mike@smithmalek.com); Fugate, Kristina; External - Joy M. Vega
Cc:	James Piotrowski
Subject:	Submission of CAIA & Certain Non-Consenting Owners re: Factors for Establishing Just and Reasonable Terms Dkt CC-2021-OGR-01-001
Date:	Friday, May 28, 2021 02:09:52 PM
Attachments:	CAIA Brief on JR Factors 05-28-21.pdf

Please find the attached for filing in Dkt. No. CC-2021-OGR-01-002, submitted on behalf of CAIA and Certain Non-Consenting Owners:

- Factors for Establishing Just and Reasonable Terms

Thank you,

-Molly Garner
Office Manager
Piotrowski Durand, PLLC

James Piotrowski, ISB # 5911
Marty Durand, ISB # 5111
PIOTROWSKI DURAND, PLLC
1020 W. Main St., Suite 440
P.O. Box 2864
Boise, ID 83701
Telephone: (208 331-9200
Facsimile: (208) 331-9201
james@idunionlaw.com
marty@idunionlaw.com

BEFORE THE IDAHO DEPARTMENT OF LANDS

In the Matter of the Application of Snake River Oil and Gas, LLC for Spacing Order Consisting of the E 1/2 of the SE ¼ of Section 9, SW 1/4 of Section 10, N 1/2 of the N 1/2 of the NW 1/4 of Section 15, and the N 1/2 of the NE 1/4 of the NE 1/4 of Section 16, Township 8 North, Range 5 West, Boise Meridian, Payette County, Idaho	Docket No. CC-2021-OGR-01-002 SUBMISSION OF NON-CONSENTING OWNERS AND CAIA RE: FACTORS FOR ESTABLISHING JUST AND REASONABLE TERMS

COME NOW Dale Verhaeghe, Linda Dernoncourt, Sharon Simmons, Alan and Glenda Grace, Edward and Cheryl Adair, William and Roxie Tolbert, Wendell and Normal Nierman, Cheryl and Richard Addison, Jimmie and Judy Hicks, Antonio and Danielle Anchustegui, Philip and Kathleen Hendrickson, Dawna and George Jackson, Karen Oltman, Bonnie McGehee, Lorinda Shuman, Samuel Butorovich, Tim Kilbourne, Kate Kilbourneand, and Citizens Allied for Integrity and Accountability, by and through counsel of record and hereby submit their statement of position regarding the appropriate factors to be addressed or considered in establishing just and reasonable lease terms for mineral rights owners who shall be compelled either to enter into lease agreements or to be deemed leased if they fail to enter such agreements.

Dale Verhaeghe, Linda Dernoncourt, Sharon Simmons, Alan and Glenda Grace, Edward

and Cheryl Adair, William and Roxie Tolbert, Wendell and Normal Nierman, Cheryl and Richard Addison, Jimmie and Judy Hicks, Antonio and Danielle Anchustegui, Philip and Kathleen Hendrickson, Dawna and George Jackson, Karen Oltman, Bonnie McGehee, Lorinda Shuman, Samuel Butorovich, Tim Kilbourne, Kate Kilbourneand, are property owners holding surface and mineral rights within the spacing unit approved by Idaho Department of Lands. Citizens Allied for Integrity and Accountability (hereafter "CAIA") is a non-profit, membership-based organization committed to the responsible development of natural resources in the State of Idaho. CAIA has members within the proposed spacing unit and appears here in its representative capacity.

Idaho Code §47-320 provides that when an applicant seeks an integration order the bonus payment and royalty amount associated with compelled leases of mineral rights shall be established either by statute, or by the prior conduct of the party petitioning for a spacing and integration order. All other terms must be established or reviewed so as to ensure those terms are "just and reasonable." The phrase "just and reasonable" is not defined in either the Oil and Gas Conservation Act nor elsewhere in any legal authority that applies directly to these proceedings. The Idaho Oil and Gas Conservation Commission ("IOGCC") has determined that it will establish the factors relevant to a determination of "just and reasonable" on a case by case basis.

Certain factors appear to flow directly from the statutory command and the context in which that command arises. Such factors should be considered to be implied by the Idaho Oil and Gas Conservation Act. Other relevant factors can be gleaned from the existing standards established under the due process clauses of the U.S. Constitution. Still others will reflect the unique circumstances presented by each application or petition, such as the existing and

reasonably foreseeable surface estate uses, as well as matters such as the spacing unit's proximity to both natural and manmade features.

A. The IOGCC Should Utilize Factors Clearly Implied by the Oil and Gas Conservation Act.

The Idaho Legislature has established some of the relevant standards and procedures for integration of tracts. These standards and procedures raise implied terms of any integration order.

Idaho Code §47-320(3) provides, for instance, that "Each such integration order shall authorize the drilling, equipping and operation, or operation, of a well on the spacing unit." This necessarily implies then that the manner and method of "drilling," the choices made for "equipping," and all matters related to "operation of a well" (not multiple wells) should be set out in the integration order, and that such terms should meet the standard of being "just and reasonable."

The same section likewise makes reference to "designat[ing] an operator," and "shall prescribe the time and manner in which all the owners may elect to participate" in the operation of the well. I.C. §47-320(3). The subsections following within §320(3) raise questions about the terms of working interest owners, non-consenting working interest owners, leased owners and deemed leased owners. Each of these provisions raise questions about royalty amounts, methods of operation, decision making concerns and more.

The Idaho Oil and Gas Conservation Act thus implies on its own that at the very least, the following matters must be considered and explicitly addressed in any integration order that is entered:

(1) whether a well is authorized to be drilled, and which precise well ("a well" in the terms of the statute) is authorized;

(2) how the well will be drilled, by what methods;

(3) how the well will be equipped once drilled;

(4) how the well will be operated including

(a) whether, how and under what conditions well treatments will be applied;

(b) whether and how mineral rights owners will be permitted to participate in decisions about well treatments, and whether and how they will be informed of well treatments before they are decided upon;

(c) how hydrocarbons produced will be delivered to market and whether other methods would yield better results;

(d) whether mineral rights owners will be notified of and permitted to participate in decision making about how to market hydrocarbons produced;

(e) whether and how well operations will be monitored and reported to mineral rights owners;

(5) Royalty rates for those who choose to lease following integration;

(6) Bonus payment amounts for those who choose to lease and those who end up deemed leased;

(7) whether specific lease terms, including the selection of alternative terms from any form of standard or industry-adopted contract, are more or less just and reasonable than those selected by the operator;

(8) All matters closely related to those listed above.

These factors should be deemed to be implied by the statute itself and thus relevant to every integration application.

B. Since the IOGCC's Order Will Necessarily Affect a Property Interest, Just and Reasonable Terms Should Incorporate Standards Developed in Case Law Under the Due Process Clauses of the U.S. Constitution.

The United States Constitution provides in two separate amendments that no person shall "be deprived of life, liberty or property without due process of law." U.S. Const. Am. 5, Am. 14. As was recently re-affirmed by the United States District Court for the District of Idaho, mineral rights are a form of property. This outcome should surprise nobody involved in the oil and gas industry since obtaining ownership of oil and gas in order to sell that ownership to others is actually the very purpose of that industry. In the context of compelling property owners to sell their property to others on terms established by the State, there is considerable legal authority for imposing certain conditions, all within the framework of ensuring due process of law. The relevant factors should address both "procedural" and "substantive" due process protections.

1. Procedural Due Process Protections Should be Incorporated

The legal doctrine known as "procedural due process" answers the question "how much process is due?" Procedural due process requires that before a state or the IOGCC can transfer one person's property to another, it must provide a fair process, one that provides "such procedural protections as the particular situation demands." *Matthews v. Eldridge*, 424 U.S. 319, 334 (1976). "The fundamental requirement of due process is the opportunity to be heard 'at a meaningful time and in a meaningful manner.'" *Id., quoting Armstrong v. Manzo,* 380 U.S. 545, 552 (1965).

Several obvious elements of "just and reasonable" terms are strongly implied by these requirements. First, all of those whose property interests will be affected by any decision reached by IOGCC must receive notice and an opportunity to be heard. The statutory system of requiring a spacing order governing an entire "pool" of hydrocarbons is likewise built on the

assumption that everyone whose property includes mineral rights to that pool will be included in any proceedings to space or integrate wells. I.C. §§47-318, 320. The first requirement for just and reasonable terms must be that all persons affected by an integration application have been given notice and an opportunity to be heard.

The opportunity to be heard is not enough to satisfy due process if that opportunity is not granted "at a meaningful time and in a meaningful manner." For property owners not engaged in the oil and gas extraction industry, time is limited, and hearings held during weekdays and at locations distant from their homes are significantly less meaningful. Just and reasonable terms should thus include provisions ensuring that no integration order is entered unless and until affected property owners have had a reasonable opportunity, not just any opportunity, to be heard.

Procedural due process also addresses the extent of process available. When the state is infringing upon a property right, as it does when it sets the terms (price, timing, methods, etc.) of a forced sale, the due process clauses of the constitution require that the process provided be adequate to meet the needs of the particular case.

> Identification of the specific dictates of due process generally requires consideration of three distinct factors: first, the private interest that will be affected by the official action; second, the risk of erroneous deprivation of such interest through the procedures used, and probable value, if any, of additional or substitute procedural safeguards; and, finally, the Government's interest, including the function involved and the fiscal and administrative burdens that the additional or substitute procedural requirements would entail.

Matthews v. Eldridge, 424 US 319, 335 (1975).

In this case, the pre-hearing order relating to proving just and reasonable terms should specify the following elements of procedural due process:

(1) identification of the party bearing the burden of proof;

(2) provisions for the issuance of subpoenas (since the information relevant to the determination will necessarily rest largely in the hands of the integration applicant and/or the proposed operator);

(3) provisions for IOGCC and/or the Department to retain qualified, independent experts to assess matters such as market conditions, risks to property owners and third parties, and the viability of collection, processing and transmission facilities;

(4) provision of adequate time between any order establishing what factors will be considered and the hearing at which evidence on those factors must be presented, so as to allow all parties to develop and marshal the relevant evidence (90 days should be considered a minimum).

2. Substantive Due Process Protections Should Be Incorporated

Notions of substantive due process differ from procedural due process in one important way. While procedural due process standards reflect what procedures must be followed to ensure a fair opportunity to be heard, substantive due process describes those things that the government simply may not do regardless of the procedure it follows. Substantive due process protections relevant to the oil and gas industry are well developed.

In setting the terms of sale where the government is establishing those terms under a requirement that they be "just and reasonable," an administrative agency must determine and then act within "a zone of reasonableness within which the [agency] is free to fix" terms as long as those terms are not "confiscatory." *FPC v. Natural Gas Pipeline Corp.,* 315 U.S. 575, 585 (1942), citing *Banton v. Belt Line Ry. Corp.,* 268 U.S. 413, 422, 423 (1925)*; Columbus Gas Co. v. Commission,* 292 U.S. 398, 414 (1934); *Denver Stock Yard Co. v. United States,* 303 U.S. 470,

483 (1938). That zone of reasonableness will be established by consideration of numerous factors including:

- Protection of reasonable, market-based investment expectations "commensurate with returns on [other] investments," *Hope Natural Gas,* 320 U.S. at 603;

- the establishment of terms "sufficient to assure confidence in the financial integrity" of all entities involved, *Id.;*

- "the requirements of the broad public interests" protected by the relevant statute, *Permian Basin Area Rate Cases,* 390 U.S. 747, 791 (1968);

- the avoidance of terms that are "unjust, unreasonable, unduly discriminatory, or preferential" to one party over another, *Natural Gas Pipeline Corp.,* 315 U.S. at 583;

- ensuring the terms "fairly compensate investors for the risks they have assumed," *Mobil v. FPC,* 417 U.S. 283, 30 (1974).

These requirements suggest a set of specific factors which should be reflected in the determination of "just and reasonable" terms of lease, including:

(1) Whether the compelled leases will result in financial losses to those whose property interests are integrated (e.g., losses occasioned by declining property values, or other property degradation the value of which exceeds the bonus payment and anticipated royalty amounts);

(2) Whether the compelled leases will result in violation of existing contractual requirements associated with the property of those whose interests are integrated;

(3) Whether the proposed terms protect, equally, the interests of all integrated owners including those with higher and lower levels of risk aversion, and with varying levels of exposure should risks of development result in harmful outcomes;

(4) Whether the proposed terms shift risk from the operator to the property owners;

(5) Whether operator is seeking to impose terms that are "unjust, unreasonable, unduly discriminatory or preferential" to any party while protecting the interests of any other party such as the operator, voluntary lessors, or others.

C. Just and Reasonable Terms Should Also Ensure that Property Owners' Reasonable Expectations, Current Property Uses and Foreseeable Property Uses Are Fully Protected Against Unanticipated Harms.

The ownership of real property and its associated mineral rights constitutes a substantial investment whether made by individual homeowners, agricultural owners, municipal entities or business entities. The relative value of mineral rights compared to the total investment owners have in their property is often not just small but *de minimus*. While correlative rights of other property owners are protected by statute, the full financial interests of non-consenting owners should be protected as well. Terms of leases should ensure that property owners do not suffer an actual loss in value. While SROG will undoubtedly complain that the financial terms of leases are set by law, the loss of value can be addressed through terms other than the royalty rate and bonus payment. Such complaints also seem petty in comparison to SROG's claim that it would bear the burden of the costs of delay in this case, despite the fact that property owners with investments multiple times that of SROG will bear the burden of the costs of mistakes in this process. Just and reasonable terms could include stop-loss provisions requiring the cessation of operations when and if the market value of hydrocarbons is too low to offset risks of loss in property value, mitigation of factors likely to cause losses, and other tools the parties address in the course of hearings in this matter.

Current land uses in the spacing unit subject to this application include agricultural, residential and light commercial uses. The factors to be considered based on the current property uses should include, at a minimum:

1. Whether oil and gas development is of sufficient financial value to justify potentially deleterious effects on current uses, including, for example, potential effects of gas development on groundwater resources vital to agricultural use, effects interfering with the protection of

residential property values, interference with reasonably foreseeable future uses such as additional residential or commercial development;

2. Whether gas development presents dangers fundamentally inconsistent with existing uses such as residential use by at-risk individuals;

3. Whether gas development enhances or reduces foreseeable future uses so as to reduce future values of the properties for residential, municipal, commercial, agricultural or industrial sites;

4. Whether steps can be ordered by the Department and Commission to reduce risks from development and operation of hydrocarbon resources, such as requirements for monitoring, the use of "tracker" chemicals or isotopes, monitoring of ground water resources, and the like;

5. Whether the development and operation of a well would place at risk municipal water supplies on which many Idahoans rely;

6. Whether steps can be ordered by the Department and Commission to reduce risks to municipal water resources;

7. Whether the financial value of the risks to groundwater, municipal and other water resources outweigh the value of the hydrocarbons to be produced;

8. Whether lessors and/or the operator are attempting to externalize the costs or potential harms of development and operation while internalizing only the profits.

For all the reasons set forth, a complex and interrelated set of factors, as set out above, should be included in determining what terms will satisfy the statutory and constitutional requirement that integration orders setting the terms of forced sale of natural gas and other hydrocarbons be "just and reasonable."

Dated this 28th day of May, 2021.

PIOTROWSKI DURAND, PLLC

/s/ James M. Piotrowski
James M. Piotrowski
Attorneys for CAIA and Certain Non-Consenting Owners

CERTIFICATE OF SERVICE

I hereby certify that on this 28th day of May, 2021, I caused to be served a true and correct copy of the following item in Docket No: CC-2021-OGR-01-002: *SUBMISSION OF NON-CONSENTING OWNERS AND CAIA RE: FACTORS FOR ESTABLISHING JUST AND REASONABLE TERMS* by the method indicated below and addressed to the following:

Idaho Department of Lands Attn: Mick Thomas 300 N. 6th Street, Suite 103 PO Box 83720 Boise, ID 83720 kromine@idl.idaho.gov	U.S. Mail Hand Delivery Certified Mail E-Mail	☒ ☐ ☐ ☒
Snake River Oil and Gas c/o Michael Christian Smith & Malek, PLLC 101 S. Capitol Blvd, Suite 930 Boise, ID 83702 mike@smithmalek.com	U.S. Mail Hand Delivery Certified Mail E-Mail	☐ ☐ ☐ ☒
Kristina Fugate Deputy Attorney General PO Box 83720 Boise ID 83720-0010 kristina.fugate@ag.idaho.gov	U.S. Mail Hand Delivery Certified Mail E-Mail	☐ ☐ ☐ ☒
Joy Vega Deputy Attorney General PO Box 83720 Boise ID 83720-0010 joy.vega@ag.idaho.gov	U.S. Mail Hand Delivery Certified Mail E-Mail	☐ ☐ ☐ ☒
James Thum Idaho Department of Lands PO Box 83720 Boise ID 83720-0050	U.S. Mail Hand Delivery Certified Mail E-Mail	☒ ☐ ☐ ☐

/s/ James M. Piotrowski
James M. Piotrowski