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Please find attached the Opening Brief of Applicant Snake River Oil and Gas, LLC re: Just and Reasonable Factors.

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BEFORE THE IDAHO DEPARTMENT OF LANDS

In the Matter of Application of Snake River Oil and Gas, LLC, to Integrate the Spacing Unit Consisting of Section 24, Township 8 North, Range 5 West, Boise Meridian, Payette County, Idaho **SNAKE RIVER OIL AND GAS, LLC, Applicant.**	Docket No. CC-2023-OGR-01-001 **OPENING BRIEF OF APPLICANT SNAKE RIVER OIL AND GAS, LLC RE: JUST AND REASONABLE FACTORS**

Applicant Snake River Oil and Gas, LLC ("Snake River" or "Applicant"), submits its *Opening Brief* pursuant to the *Order Vacating Hearing and Notice of Hearing to Determine "Just and Reasonable" Factors*, issued by the Administrator on January 31, 2023

A. <u>The same factors as used in the previous three integration proceedings should be used here</u>.

As set forth in its application, Snake River requests that the Administrator apply the same factors to determine that the integration order is made "upon terms and conditions that are just and reasonable," in accordance with Idaho Code § 47-320(1), as were used in the most recent completed integration proceedings, Docket No. CC-2021-OGR-01-001, Docket No. CC-2021-OGR-01-002, and Docket No. CC-2022-OGR-01-002, specifically:

1. Are the proposed terms addressed in another source of law?

2. Are the proposed terms and conditions (a) consistent with industry standards; (b) consistent with terms previously accepted or rejected by courts or other oil and gas administrative agencies; and (c) applicable to the unit and its operations?

3. Are the proposed terms and conditions similar to other agreements within and nearby the unit? If a proposed term is not similar, is there a reason why a different term or condition is appropriate?

4. Are any proposed terms, including those addressed at drilling, equipping, and operating the well, consistent with the Oil and Gas Act and necessary given site-specific conditions?

5. Will the proposed operations, including the drill site, physically occupy the property of uncommitted owners, and are any additional terms necessary to address physical occupation?

6. If the proposed operation includes use of uncommitted owners' surface estate, is the operator's compliance with Idaho Code § 47-334 adequate to protect the surface owner?

7. Do the unit's circumstances and operations require additional bonding with the Department?

8. Does the integration order ensure that integrated owners that do not choose to participate as an owner retain the private right of action against the operator for any future harms?

The Applicant is not aware of any special conditions in Section 24 or relating to its planned operations there which require the application of different factors. The Administrator previously found in the above three applications that the factors used there meet the Administrator's guidelines for determining factors, i.e., they comply with existing statutes and rules, they are within the Commission's statutory authority and discretion, and they do not impose burdens, conditions or restrictions in excess of or inconsistent with the Oil and Gas Conservation Act. The Applicant respectfully suggests that the facts set forth in its application in this matter and in the supporting Declaration of Richard Brown and Declaration of Travis Boney support the adoption of the requested factors.

B. <u>Factors not related to ensuring mineral owners' receipt of their equitable share of production and prevention of waste are outside the scope and purpose of integration</u>.

The history and development of integration and pooling statutes is a reaction (along with the creation of well spacing requirements) to the impacts from the Rule of Capture, and reflects a legislative effort to ensure that uncommitted mineral owners within a well spacing area receive

their equitable share of production from the well. Viewed in that context, "just and reasonable" terms are economic terms imposed to ensure an uncommitted owner receives their equitable share of production from a well (i.e., protect their correlative rights), and to prevent waste (i.e., prevent inefficient production or reservoir damage), to the extent those terms are not already prescribed in statute. The requirement of "just and equitable" terms is not an open invitation by the Legislature to impose operational requirements already covered by existing statute or regulation and unrelated to the allocation of production (or the revenue from it) to mineral owners. One commentator described the history as follows:

> The Rule of Capture was based on the concept of "first in time, first in right," and meant that if a reservoir of oil or gas lay under both A's property and B's property, A could legally extract *all* the oil from the reservoir and receive all the benefits." Therefore, to preserve her right to the oil that lay partially under her property, B would need to erect a well and extract the reservoir's content before or concurrently with A. The Rule of Capture led many landowners whose property overlaid oil or gas reservoirs to build multiple wells on their land so they could extract their resources as quickly as possible.
>
> Too many wells were inefficient and unnecessary. The cost of drilling excessive wells was estimated to be millions of dollars a year. Production waste and inefficiency, caused by the reduction in geologic pressure, made it more difficult and costly to extract the oil and gas. Overproduction caused oil and gas market prices to decline. By the 1930s and 1940s, states enacted spacing and pooling laws to address these issues and protect their interests in market control, waste prevention, and resource development.
>
> Texas promulgated the first linear setback requirements in the United States. These regulations, known as Rule 37, required a minimum of 300 feet between wells and 150 feet between wells and property lines. States also created density requirements that limited a single well to a given area by requiring drilling units to contain minimum acreage. This required landowners not owning the minimum acreage to pool (or integrate) their land with their neighbors' lands to form drilling units so they could exercise their mineral rights. In turn, states enacted voluntary and forced pooling laws to regulate this process.
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> * * *
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> States with voluntary pooling laws also have statutes and regulations that allow owners and operators to *use forced* pooling to achieve a similar result. These laws

> require "fair, reasonable, and equitable" or "reasonable" terms in the sharing of oil and gas production. Forced pooling laws (also known as involuntary pooling or compulsory integration) attempt to resolve the problem of non-consenting owners: landowners with oil or gas rights who refuse to voluntarily pool their ownership rights with other landowners (referred to as participating landowners). If a certain statutory - or regulatory - defined percentage of landowners want to exercise their oil or gas rights and there are nonconsenting landowners, the owners who want to develop their mineral rights or well operator, can initiate an administrative procedure to forcefully pool non-consenting landowners' oil and gas development rights with participating landowners. Forced pooling laws are an imperfect, yet practical, way to balance efficient resource production and landowner rights.

Frank Sylvester and Robert W. Malmsheimer, "*Oil and Gas Spacing and Forced Pooling Requirements: How States Balance Energy Development and Landowner Rights*," 40 Dayton L. Rev. 47, 49-51 (2015)(citations omitted).

Pooling or integration is "intended to allow for more efficient oil and gas drilling by decreasing waste and avoiding drilling of unnecessary wells." *Wildgrass Oil &Gas Comm. v. Colorado*, 447 F.Supp.3d 1051, 1057 (D. Colo. 2020). Integration "reduces the number of wells drilled while also compensating [interest] owners for their share of the resources extracted." *Id*. at 1057.

Integration "is the remedy that permits development of the drilling unit in the event that the mineral-interest owners cannot agree to pool voluntarily." *Gawenis v. Arkansas Oil & Gas Commission,* 464 S.W.3d 453, (Ark. 2015) (citation omitted). Integration procedures "constitute a proper exercise of [the state's] police power" to protect "property rights by requiring a just, orderly, and efficient process for neighbors to extract common resources." *Kerns v. Chesapeake Exploration, L.L.C*., 762 Fed. Appx. 289, 297 (6th Cir. 2019) (citations omitted). "Each landowner's property interest in the minerals remains intact; it is simply regulated." *Id*. (citation omitted).

All of this is reflected in the Act. Idaho Code § 47-311 declares that is in the public

interest "to foster, encourage and promote the development, production and utilization of natural resources of oil and gas in the state of Idaho in such a manner as will prevent waste." Idaho Code § 47-311 also provides that it is in the public interest to provide for oil and gas development "in such a manner that a greater ultimate recovery of oil and gas may be obtained and that the correlative rights of all owners be fully protected." Thus, the Act emphasizes the public interest in developing oil and gas, while preventing waste and protecting correlative rights. What is "just and reasonable" for an integration order must be evaluated in that context.

"Waste" is defined in the Act (as applied to gas) to "include the escape, blowing or releasing, directly or indirectly, into the open air of gas from wells productive of gas only, or gas in an excessive or unreasonable amount from wells producing oil or both oil and gas; and the production of gas in quantities or in such manner as will unreasonably reduce reservoir pressure or unreasonably diminish the quantity of oil and gas that might ultimately be produced; excepting gas that is reasonably necessary in the drilling, completing and testing of wells and in furnishing power for the production of wells." Thus, "prevention of waste" is concerned with the protection of reservoir quality and reasonable production, which is largely accomplished through well spacing.

"Correlative rights" are defined in the Act as "the opportunity of each owner in a pool to produce his just and equitable share of oil and gas in a pool without waste." Idaho Code § 47-310(4).

"There appear to be two aspects of the doctrine of correlative rights: (1) as a corollary of the rule of capture, each person has a right to produce oil from his land and capture such oil or gas as may be produced from his well, and (2) a right of the land owner to be protected against damage to a common source of supply and a right to a fair and equitable share of the source of

supply." *Slawson v. North Dakota Indus. Com'n*, 339 N.W.2d 772, n. 1 (N.D. 1983).

Thus, the Act generally, and the integrations provisions specifically, are concerned with (a) encouraging production; (b) ensuring that mineral owners have the opportunity to receive their equitable share of production; and (c) preventing waste. "The purpose of forced pooling is to equalize the risk of loss [related to the expense of drilling and exploration] by forcing all of the oil and gas interest owners to choose in advance whether they will share in both the benefits and the risks of oil and gas exploration." *Ranola Oil Co. v. Corporation Com'n of Oklahoma*, 752 P.2d 1116, 1119 (Okla. 1988). "Voluntary pooling agreements and forced pooling orders are the mechanisms used to enforce correlative rights." *Cowling v. Board of Oil, Gas and Min., Dept. of Natural Resources for State of Utah*, 830 P.2d 220, 226 (Utah 1991); *see also Crest Resources and Exploration Corp. v. Corporation Commission*, 617 P.2d 215, 219 n. 3 (Okla. 1980) ("Compulsory pooling is a reasonable exercise of the state police power to protect the correlative rights of owners in a common source of oil and gas supply."); *Application of Kohlman*, 263 N.W.2d 674, 678 (S.D. 1978) ("The legislature has declared that it is the public policy to develop without waste a valuable natural resource of the state. One of the methods to prevent waste is through compulsory pooling of oil interests within a spacing unit.").

The Administrator is also limited in determining the terms and conditions of integration, as set forth in Idaho Code § 47-320(3). Owners who elect to share in the expense of drilling and operating a well are entitled to their share of the well's production. Idaho Code §47-320(3)(a). Nonconsenting working interest owners are entitled to their share of production after all expenses and the assessed risk penalty have been recovered by the operator and consenting owners. *Id*., § 47-320(3)(b). Mineral owners who elect to lease receive a royalty no less than 1/8th and a lease bonus equal to the highest bonus paid to other owners prior to the application for an integration

order. *Id*., § 47-320(3)(c). Those deemed leased receive a set royalty of 1/8th and a lease bonus equal to the highest bonus paid in the unit prior to the application. *Id*, § 47-320(3)(d). These provisions do not give the Administrator authority to order additional compensation to uncommitted mineral owners to address allegations of various risks. The Administrator has flexibility to set the royalty for those who elect to lease, but where the majority of owners in the unit have all voluntarily leased at 1/8th royalty, awarding holdouts a higher royalty based on non-market considerations would result in their receiving more than their equitable share of production.

A factor involving the examination of the relative risks and benefits of owners for purposes of determining whether to order integration also is inappropriate. The Legislature made integration mandatory when an operator meets statutory terms. Idaho Code § 47-320(1). That section provides that "the Administrator, upon the application of any owner in that proposed spacing unit, *shall* order integration of all tracts or interests in the spacing unit for drilling of a well or wells, development and operation thereof and for the sharing of production therefrom." Thus, whether a mineral owner believes there are risks outside the equitable sharing of production is neither relevant to nor an impediment to integration. As a practical matter (as recognized in the factors used in previous integration proceedings), those risks are generally covered and mitigated by other areas of law (e.g., well drilling, treatment, operating, production metering and reporting, and reclamation requirements in IDAPA 20.07.02, air and water quality requirements covered in Idaho Code Title 39, Chapters 1, 36 and associated state administrative rules, and associated federal statutes and rules).

C. Factors related to the prospective productivity of the planned well are not relevant to integration.

Factors related to the geology of the unit or the prospective productivity of the planned

well are not relevant to integration, including for the reasons discussed above. For example, the Oklahoma Supreme Court rejected a request that the operator seeking a pooling order provide uncommitted mineral owners with access to geologic information and well projections, particularly in less developed areas, reasoning:

> Geologic studies in such areas are closely guarded by their owners as proprietary information. Any conclusion reached relative to future production from the contemplated well derived from these tests remains problematical, conjectural, and depends in great part upon the expertise of the persons making the evaluation. The future value of the well and the unit it is placed upon is thus pure speculation. The issue to be determined in this pooling proceeding is the Present market value which, as is noted herein, is amply supported by testimony of market value determined by recent transactions and not Future value reflected by the prospects of the contemplated well. Appellant contends that under 52 O.S.1971, § 87.1(d) the requirement that ". . . All orders requiring such pooling shall be made upon such terms as are just and reasonable . . ." requires the divulgence of these studies. We perceive no such requirement mandated by that broad statement, and hold the order is supported by substantial evidence equating the Present value of a right to drill on the tract as the price offered and accepted for leases in the unit.

Home-Stake Royalty Corp. v. Corporation Commission, 594 P.2d 1207, 1209-1210 (Okla. 1979). The reasoning in *Home-Stake* is consistent with the history of integration discussed above and is consistent with the provisions of the Act discussed above.

The Applicant lastly wishes to point out that the judgment in *CAIA v. Schultz,* 335 F. Supp. 3d 1216 (D. Idaho 2018), did not mandate this procedure. The judgment in that case only directed the Department to "hold a new hearing [then, with respect to the Fallon #1-10 unit] that complies with due process by explaining the factors that will be considered when determining whether the terms and conditions of an integration order are 'just and reasonable.'" 335 F.3d at 1230. Judge Winmill concluded that vacating the order at issue in that case and requiring a rehearing would not be overly burdensome because "[t]he only change required will be specification of the basis on which Defendants determine factors to be relevant or irrelevant to the determination of 'just and reasonable' terms." *Id.* at 1228. Thus, only requirement imposed upon the Administrator by the

judgment was to "explain[] the factors that will be considered" at the merits hearing of the application to establish just and reasonable terms and conditions of integration. The objecting owners are receiving due process well exceeding that ordered in *CAIA v. Schultz* through the provision for multiple rounds of briefing and an intermediate hearing to provide input on the development of the factors.[1]

DATED this 1st day of March, 2023.

HARDEE, PIÑOL & KRACKE, PLLC

MICHAEL CHRISTIAN
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[1] Applicant has never agreed that *CAIA v. Schultz* was correctly decided. No other court has found the exercise of discretion in determining "just and reasonable" terms and conditions of integration or pooling to be constitutionally deficient, and as noted, pooling and integration statutes have existed in producing states for half a century or more. The only other court to face similar issues recently chose not to follow *CAIA v. Schultz* and abstained under *Burford v. Sun Oil Co.*, 319 U.S. 315 (1943), concluding that complex state law issues were involved, and the state courts were well-equipped to address them. *Wildgrass Oil & Gas Comm. v. Colorado*, 447 F.Supp.3d 1051, 1069 (D. Colo. 2020), *aff'd*, *Wildgrass Oil & Gas Comm. v. Colorado*, Case No. 20-1151 (10th Cir. 2021).

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on this 1st day of March, 2023, I caused to be served a true and correct copy of the foregoing by the method indicated below, and addressed as follows:

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